VAT UPDATE
APRIL 2020

Covering material from January – March 2020

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VAT Update April 2020

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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 was updated on 15 January 2020.

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.

The dates cited for likely hearings must now be treated with caution because of Coronavirus disruption.

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

- *Alan McCord*: HMRC granted leave to appeal against the FTT decision that a car dealer was entitled to input tax on cars purchased for domestic sales, but denied input tax on cars purchased for sale to customers in the Republic of Ireland.
- *Anna Cook*: HMRC granted leave to appeal against the FTT decision that classes in Ceroc dancing qualified for exemption as "educational" (hearing scheduled for October 2020).
- *Beigebell Ltd*: HMRC granted leave to appeal against the FTT decision a company's directors did not have the means of knowledge of the connection of their company's transactions to a missing trader fraud (hearing scheduled for May 2020).
- *Blackrock Investment Management (UK) Ltd*: argument about application of reverse charge to software bought in for use in management of investment funds – UT dismissed HMRC's appeal on the "exemption" issue but referred the "apportionment" issue to the CJEU (hearing was December 2019 – Case 231/19).

- *Cheshire Centre for Independent Living*: HMRC have been granted leave to appeal against the FTT's decision that a charity's operation of PAYE for disabled people was sufficiently closely connected to welfare to qualify for exemption.
- *DCM (Optical) Ltd*: both sides have been granted leave to appeal to the Court of Session against the Upper Tribunal's decisions in relation to apportionment of sales between taxable and exempt supplies (hearing scheduled for June 2020).
- *Done Brothers (Cash Betting) Ltd and others*: HMRC have been granted leave to appeal against the FTT decision that the company was entitled to exemption of its gaming supplies on fiscal neutrality grounds (hearing January 2020).
- *Fortyseven Park Street Ltd*: company is applying for leave to appeal to the Supreme Court against the CA decision that their "high end timeshare" was covered by the "hotel exclusion" from exemption.
- *Good Law Project*: (not on HMRC's list) HMRC appealing against decision of High Court that it was lawful for them to disclose certain facts in relation to a dispute with a taxpayer, so it was not necessary for them to apply for a court order in order to be granted permission to do so (hearing scheduled for Court of Appeal in April).
- *KE Entertainments Ltd*: the company's appeal against the Court of Session's decision on its adjustment for output tax in relation to bingo calculations was scheduled to be heard by the Supreme Court on 28 and 29 April 2020.
- *Newey (t/a Ocean Finance)*: HMRC describes the CA decision as a "partial win for HMRC". The case has been remitted to the FTT for further consideration in the light of the CJEU judgment (hearing June/July 2019 – decision awaited).
- *Northumbria Healthcare NHS Foundation Trust v HMRC*: CA to hear HMRC's appeal against UT decision that provision of cars under a salary sacrifice scheme could not be regarded as a supply of services, so the Trust was entitled to claim VAT on leasing in full under s.43 (not on HMRC's list – hearing scheduled for June/July 2020).
- *Opodo Ltd*: HMRC have been granted leave to appeal to the Upper Tribunal (against FTT decisions that do not appear to have been published yet – HMRC were refused a reference to the CJEU).
- *Pacific Computers Ltd*: MTIC case remitted by the UT to differently constituted FTT for rehearing (not on HMRC's list).
- *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).
- *Rank Group plc*: HMRC has been granted leave to appeal against the FTT decision that certain supplies qualified for exemption on fiscal neutrality grounds (hearing listed for January 2020).

- *Royal Opera House Covent Garden Foundation*: HMRC has been granted leave to appeal against the FTT decision on the partial exemption recovery percentage (has disappeared from HMRC's list).
- *Target Group Ltd*: company is seeking leave to appeal against UT decision that its supplies of loan administration services did not fall within art.135(1)(d) (not on HMRC's list).
- *The Core (Swindon) Ltd*: HMRC have been granted leave to appeal against the FTT decision that certain products were "liquid meal replacements" rather than "beverages" (scheduled for October 2020).
- *The Ice Rink Co Ltd and another*: the UT remitted the case to the same FTT for reconsideration of whether the supply of children's ice skates was a separate zero-rated supply or part of a compound supply.
- *The Wellcome Trust Ltd*: HMRC granted leave to appeal against the FTT decision that the company was not subject to a reverse charge on investment management fees. The UT has agreed to refer questions to the CJEU (Case C-459/19).
- *Thorsteinn Gardarsson t/a Action Day A Islandi*: HMRC granted leave to appeal against the FTT decision that a trader's products qualified as "books" rather than "stationery" (hearing March 2020).
- *Tower Resources plc*: HMRC have been granted leave to appeal on two grounds, and are seeking leave to appeal on a third, against the FTT's decision that a holding company was entitled to recovery of input tax on some overhead costs.

1.2 Decisions in this update

- *LIFE Services Ltd/Learning Centre (Romford) Ltd*: the companies failed in their appeal to the CA against UT's decision that their supplies did not qualify for the exemption for welfare.

1.3 Other points on appeals

- *Baillie Gifford & Co*: HMRC are not appealing against the FTT's decision to allow a partnership to group with companies from 2013 based on the *Larentia + Minerva* decision of the CJEU.
- *Lloyds Banking Group plc and others*: various parties in the long-running dispute about the correct claimant in group registration *Fleming* claims were refused leave to appeal to the Supreme Court.
- *RSR Sports Ltd*: HMRC's list states that the decision (that summer camps were exempt childcare with incidental activities) was reached on the specific facts of the case and will not be appealed.
- *The Chancellor, Masters and Scholars of the University of Cambridge*: the CJEU found in favour of HMRC's position on management fees in relation to the endowment fund, and the Court of Appeal gave effect to the judgment by way of a Court Order.
- *Zipvit Ltd*: (not on HMRC's list) taxpayer's appeal to the Supreme Court against the CA confirmation of decisions below that the company could not claim input tax on the VAT element of payments to Royal Mail without a VAT invoice, even though it was clear that

taxable supplies had been made: judgment delivered 1 April 2020, referring questions to the CJEU – to be covered in the next update.

HMRC are not appealing the UT decision in *Pertemps Ltd* about the VAT consequences of a salary sacrifice scheme.

2. OUTPUTS

2.1 Scope of VAT: linking supplies to consideration

2.1.1 Secondment within a group

An Italian company seconded a director to a subsidiary to act as a director of one of its establishments. It invoiced the subsidiary for the cost of the director's salary and added VAT. The tax authorities refused a deduction for the subsidiary, arguing that the reimbursement of costs between a parent and subsidiary did not constitute consideration for a taxable supply. In particular, the lack of any mark-up, or additional duties over and above what might have been done as director of the seconding company, indicated that the transaction was outside the scope of VAT in accordance with a particular provision of Italian domestic law. The company's appeal was dismissed by the Italian courts, and questions were referred to the CJEU.

The questions referred asked whether the Italian law could validly disregard secondment of staff for VAT purposes. The court noted that a supply of services was effected for consideration within PVD art.2(1) and hence was taxable, only if there was a legal relationship between the provider of the service and the recipient pursuant to which there was reciprocal performance, the remuneration received by the provider of the service constituting the value actually given in return for the service supplied to the recipient. That was the case if there was a direct link between the service supplied and the consideration received.

In this case, all the conditions appeared to be satisfied. It was for the referring court to determine if that was the case, but if the payment of the invoiced amounts was in return for the secondment, and the secondment was conditional upon that payment, then it had to be regarded as a taxable transaction.

CJEU: (Case C-94/19): *San Domenico Vetraria SpA v Agenzia delle Entrate*

2.1.2 Manual change

HMRC's *VAT Supply and Consideration Manual* has been updated with HMRC's current views on the treatment of excess charges by contractors. The fees (commonly known as parking charge notices or PCNs) are now seen as outside the scope of VAT whether retained by the parking enforcement contractor or passed on to the landowner.

VATSC06140

2.2 Disbursements

Nothing to report.

2.3 Exemptions

2.3.1 Special investment funds

From 1 April 2020, the law has been changed to exempt fund management of "qualifying pension funds" within the exemption for special investment funds. This appears to go no further than the CJEU decisions in Case C-424/11 *Wheels Common Investment Fund Trustees Ltd* and Case C-464/12 *ATP Pension Services A/S*: a "qualifying" pension fund is one in which the pension members bear the investment risk, so it is similar to an open-ended investment company. The change will not apply to management of defined benefit pension schemes.

SI 2020/209

2.3.2 Vouchers in clubs

Another case has been heard by the FTT on the proper treatment of a special "currency" used in lap-dancing or table-dancing clubs, after the case of *Wiltonpark Ltd* reached the Court of Appeal in late 2016. The mechanics of the vouchers appears to have been similar:

- customers bought "Platinum Chips" in various denominations, paying a 20% premium over the face value;
- the vouchers were used to pay self-employed dancers for performing;
- the dancers redeemed the vouchers from the club; in the London club, this was only after deduction of a 20% fee when exchanged for cash;
- employees could also receive vouchers as tips, in which case they were charged a 40% fee on redemption.

The FTT was asked to rule in principle on various assessments raised by HMRC for periods from 07/10 to 07/15. The amounts of those assessments were not stated. The Tribunal had to consider separately:

- the VAT treatment on the supply of the vouchers to the customers;
- the VAT treatment on the redemption of the vouchers by the club.

Issue of vouchers

HMRC's assessment was raised on the basis that the whole amount paid by the customer was consideration for a taxable supply. The company argued that it was either an exempt supply, or that only the excess over the nominal value was consideration for a taxable supply.

The decision goes into detail about the way in which vouchers were issued to customers. The company's witness stated that the 20% fee was charged in relation to the credit risk of customers disputing the transactions, and claimed that a great deal of time and effort was involved in resolving such disputes. However, it appears that the club was very successful in enforcement: between January 2012 and June 2015 the London club alone issued vouchers with a face value of £14.5m, but the club as a whole only wrote off £5,828. In 2014/15 the total of disputed transactions was £76,933. In the light of the evidence as a whole, the judge did not consider that the 20% fee was simply intended to cover the

financial risk and the transaction fees incurred. It was intended to provide a significant income stream.

The club claimed that the chips could also be used to pay for services or goods supplied by other local businesses, or to make donations to a charity promoted by the club (Help for Heroes). The evidence suggested that £760 of chips were used in Leicester in this way between April 2015 and April 2016, during which time the face value of chips issued by the Leicester club was £500,000. After considering the evidence, the judge concluded that any use for purposes other than paying for dances was de minimis and could be ignored.

After making various findings of fact, the judge went on to consider the arguments. HMRC's assessment was based on the assumption that the issue of a voucher was a taxable supply, chargeable on the full consideration. The company argued that:

- either the chips were a "security for money" and were therefore exempt, following the decision in *Kingfisher plc* (High Court 2000);
- or they were "face value credit vouchers" within Sch.10A VATA 1994, and only the consideration above the face value was taxable; para.7A (effective from 10 May 2012) did not apply because the chips were not "single purpose vouchers".

The FTT and UT in *Wiltonpark* had concluded that the "Secrets money" in that case (which was similar to Platinum chips in some ways but different in others) constituted "security for money". HMRC argued that the chips were security for money in the hands of the dancers and employees of the club, because they could be exchanged for cash; however, they were not security for money in the hands of the customers who bought them, because they were not refundable (except in exceptional circumstances and only at the discretion of the club).

The judge accepted HMRC's argument. When held by a customer, the chip represented a bundle of rights to receive entertainment; only once it had been given to a dancer, as agreed consideration for services, did it become a security for money, because the dancer could redeem it for cash. The transaction between the club and the customer was therefore not within the exemption.

The judge went on to conclude that the chips were single purpose vouchers exchangeable for taxable entertainment services, and so taxable in full on issue after 10 May 2012. Their possible use for other purposes which might be outside the scope (tipping dancers or employees) did not affect that, because it did not represent a right to receive goods or services separate from the essential purpose of the voucher. Before 10 May 2012, only the excess over the face value was taxable.

Redemption of vouchers

HMRC's assessment was raised on the basis that the fee charged was consideration for a taxable supply from the club to the dancer. The club argued that there was no taxable supply.

In the period January 2012 to December 2015 dancers at the London club were charged £2.7m as commission on redemption of chips indicating that dancers received chips with a face value of £13.5m from customers. The judge accepted HMRC's argument that the situation was no different from

that considered by the Court of Appeal in *Wiltonpark*, where the discount on redemption was held to be part of the consideration charged to dancers for the provision of facilities for earning money by dancing. The dancers in both cases paid an entrance fee to the club to be allowed to dance, and the discount on redemption was similar in nature (and VAT liability) to that.

However, the discount charged to employees on encashment of tips was different. Employees were not charged an entrance fee, and were paid a salary. They were able to use the voucher system to receive extra money, but that was part of the relationship between employer and employee, and the discount did not represent consideration for a supply of services by the employer to the employee. That part of the assessment should be removed.

The appeal was therefore allowed in part.

First-Tier Tribunal (TC07494): *Romima Ltd and others*

2.3.3 Payment charges

A complex case involved consideration of intra-group charges, the exemption for financial transactions, and an allegation by HMRC of abuse of rights by the taxpayer. The first hearing of the case took place in November 2013; the judge noted the complex procedural history since then, including adjournments and postponements, changes of pleadings and directions hearings.

VML supplied cable TV, broadband and telephone services to the public. Customers made their payments to a group company, VMPL. Customers who did not pay by direct debit were billed a “payment handling charge” of £5 per month.

The long decision starts by summarising the issue: whether the interposition of a separate company, VMPL, between VML and the customer could make the result different from that in *Everything Everywhere Ltd*, where an extra charge for not paying by direct debit was held to be part of the consideration for a single supply of telephone services.

HMRC’s initial decision on the structure, issued in 2009, listed three separate possible outcomes:

- the preferred decision, which was that there was a single consideration for a single supply;
- the first alternative decision, which was that any separate financial element was incidental and ancillary to the taxable supply (*CPP*);
- the second alternative decision, which was that a separate non-incidental supply was not exempt.

One of the reasons for the long delay in the case was the reliance of the taxpayer on cases that proceeded to the CJEU in that time – *Everything Everywhere* and *AXA UK*. Other relevant cases have also been heard by the CJEU in the intervening years (e.g. *Bookit* and *DPAS*).

The company’s grounds for appeal against each of the decisions were, in brief summary:

- there was no direct link between the payment handling charge (which was only paid by those who did not pay by direct debit) and the taxable services (which were charged at the same price to everyone);
- *CPP* could not be applied to services supplied by different companies, in accordance with the *Telewest* decision;
- the payment handling charge was exempt, in line with the reasoning of the CJEU in *AXA* and the Court of Appeal in *Bookit* (2006). The charge was consideration either for "a transaction concerning payments" or else for "acting as an intermediary in relation to a transaction concerning payments".

By the time of the hearing, HMRC had also added an argument based on abuse of rights, contending that the interposition of VMPL was an artificial arrangement solely or mainly intended to obtain a VAT advantage by avoiding the consequences of the *Everything Everywhere* decision.

Judge Anne Scott commented that about the only point agreed between the parties was that very few of the facts were agreed, and she would therefore need to make extensive findings of fact in relation to complex and detailed circumstances. She noted that there were great difficulties in doing so, including errors in the basic facts as to the group structure of the Virgin Media group which required the head of the group's treasury function to give an amended witness statement on the last day of the hearing and be recalled to speak to it.

It was, however, not disputed that the five key issues for the Tribunal were:

(1) Is there a supply by VMPL to the Virgin Media customers who do not pay by Direct Debit?

(2) If there is a supply, then what is it? Does it have a free-standing fiscal identity or is it subsumed into the supply made by VML?

(3) If the payment handling services are a supply, do they fall within the scope of the exemption for financial services within the provisions of Group 5 Sch.9 VATA as "the transfer or receipt of, or any dealing, with money" or as intermediary services in relation to the "transfer or receipt of, or any dealing with money" (items (1) and (5) respectively)? If they are such an exempt supply do they then, in terms of art.135(1)(d) PVD amount to debt collection so as to be excluded from exemption?

(4) Do the answers to any of the three preceding issues alter because both appellants are in the same VAT group at all material times?

(5) Are the arrangements abusive within the principles set out by the Court of Justice in *Halifax*? In other words, if the payment handling charges are exempt, are the arrangements made by the appellants contrary to the purpose of the PVD?

The judge started with a "high-level" review of the group structure and history of the Virgin Media group, going back to the predecessor Telewest and NTL companies. When the business was rebranded in 2007, there 500 companies in the UK corporate group structure; in October 2013 there were 397 subsidiary companies in the VAT group.

The operation of the payment collection system was then examined in great detail, considering the different ways in which payments were made by customers, the costs of each method, and the contractual arrangements underlying them.

The argument for the appellant was summarised as follows:

- the customer has a choice of whether to incur the charge or not;
- the charge is for a service that is exempt within Group 5 Sch.9;
- even though VML and VMPL were in the same VAT group, s.43 VATA 1994 did not have the effect of characterising a supply to a third party as part of a single supply by representative member (i.e. s.43 did not negate the application of *Telewest* – both companies in *Telewest* were also in a VAT group).

The effect of VAT grouping had been considered most recently by the Supreme Court in *Taylor Clark Leisure plc*. The judge concluded from the reasoning in that case that UK law requires the "fiction" of s.43 to be applied consistently and comprehensively: the supplies made by all group members were to be treated as made by the representative member. This meant that *Everything Everywhere* would apply, as the situation would be directly analogous. The fiction did not affect anything other than VAT, but there was no inconsistency with precedent cases in holding that it applied to everything within VAT.

In deciding whether there was a separate supply made by VMPL (and if so, to whom), the judge cited the principles set out by the Upper Tribunal in *The Honourable Society of Middle Temple*:

(1) Every supply must normally be regarded as distinct and independent, although a supply which comprises a single transaction from an economic point of view should not be artificially split.

(2) The essential features or characteristic elements of the transaction must be examined in order to determine whether, from the point of view of a typical consumer, the supplies constitute several distinct principal supplies or a single economic supply.

(3) There is no absolute rule and all the circumstances must be considered in every transaction.

(4) Formally distinct services, which could be supplied separately, must be considered to be a single transaction if they are not independent.

(5) There is a single supply where two or more elements are so closely linked that they form a single, indivisible economic supply which it would be artificial to split.

(6) In order for different elements to form a single economic supply which it would be artificial to split, they must, from the point of view of a typical consumer, be equally inseparable and indispensable.

(7) The fact that, in other circumstances, the different elements can be or are supplied separately by a third party is irrelevant.

(8) There is also a single supply where one or more elements are to be regarded as constituting the principal services, while one or more elements are to be regarded as ancillary services which share the tax treatment of the principal element.

(9) A service must be regarded as ancillary if it does not constitute for the customer an aim in itself, but is a means of better enjoying the principal service supplied.

(10) The ability of the customer to choose whether or not to be supplied with an element is an important factor in determining whether there is a single supply or several independent supplies, although it is not decisive, and there must be a genuine freedom to choose which reflects the economic reality of the arrangements between the parties.

(11) Separate invoicing and pricing, if it reflects the interests of the parties, support the view that the elements are independent supplies, without being decisive.

(12) A single supply consisting of several elements is not automatically similar to the supply of those elements separately and so different tax treatment does not necessarily offend the principle of fiscal neutrality.

After further detailed consideration of the contracts with the customers and also between the group companies, the judge concluded that those who paid the handling charge signed up for a single supply. Most of them could not pay by DD (for whatever reason), which meant that they did not have a genuine choice of whether to pay the £5 or not; they either paid the higher price, or they did not receive the services. If that conclusion was wrong, the judge found that the supply was in reality made from VMPL to VML (collection services) rather than to the customers (payment services).

In considering the financial services exemption, the judge noted the references in successive CJEU decisions to the developing precedents on the issue and said the following:

It is clear to us that, over more than the last decade, the jurisprudence of the CJEU in relation to payment activities has evolved. The current position is that, read together, EE, Bookit, NEC and DPAS make it clear that any appellant seeking to establish entitlement to the financial exemption, where an alleged financial service or supply has been carved out of a transaction, has a significant hurdle to surmount.

The precedents were examined and the judge drew the conclusion that *Bookit* applied: even if there was a supply by VMPL to the VML customers that was separate from the supply of telecommunications services, it was not exempt. As a passing comment, the judge stated that if that was wrong, she did not accept that the supply would be debt collection, because it would be supplied to the debtor, not the creditor.

Turning to HMRC's argument on abuse of rights, this was not strictly necessary because the appeal was already lost on technical grounds. However, the judge considered and rejected it; there were other commercial reasons for the group structure, and nothing artificial about the commercial choices that the companies had made. It was not solely or mainly to obtain a tax advantage.

The judge summed up the Tribunal's findings at the end of over 400 paragraphs:

423. Our preferred decision is quite simply that the taxable person making supplies is VML and it is the representative member of the VAT Group. There is one supply of media services and the £5 consideration

paid, where payment is not made by Direct Debit, is an integral part of that supply. If we are wrong in that then the supply of payment handling services is an ancillary supply.

424. VMPL does not make a supply to the Virgin Media customers who do not pay by Direct Debit.

425. If we are wrong in that then the only supply made by VMPL is to VML when acting as agent to collect, process and apply payments due by customers. That is intra group so there is no VAT consequence.

426. VMPL does not have a free-standing fiscal identity for VAT purposes.

427. If we are wrong in that and VMPL does make a supply of payment handling services to the customers, in light of the decisions in Bookit and NEC in particular, those are not exempt supplies. Further in light of the decision in DPAS any such supply is simply technical and administrative and does not qualify as being exempt.

428. If we are wrong in that any such supply does not amount to debt collection.

429. In the event that we are wrong on every other issue, the essential aim of the transaction is not to secure a tax advantage so the Commissioners' argument on abuse fails.

The appeal was dismissed. As the law had been clarified by recent CJEU cases, it was not necessary to make a reference.

First-Tier Tribunal (TC07536): *Virgin Media Ltd and another*

2.3.4 Ordinarily taught?

An individual treated supplies of kickboxing classes as exempt. Following an enquiry in 2017, HMRC issued a decision that he did not qualify for the "private tuition" exemption; he should be registered with effect from 1 August 2011, and was assessed for the period from that date in the amount of £411,497. A statutory review moved the date to 1 September 2011 and slightly reduced the assessment. ADR led to the EDR being moved to 1 April 2018, and the assessment was cancelled. Nevertheless, the individual appealed against the decision that his supplies were standard rated.

The question before the Tribunal was whether the exemption in art.132(1)(j) PVD applied: "tuition given privately by teachers and covering school or university education". HMRC argued that the UK provision in Item 2 Group 6 Sch.9 VATA 1994, which exempts "private tuition in a subject ordinarily taught in a school or university by an individual teacher acting independently of an employer" accurately reflected the PVD; the appellant argued that the PVD did not refer to "subjects" and should not be limited to anything "ordinarily taught".

The judge stated that, as art.132 has direct effect in the UK, the appellant was entitled to rely on it, so the decision started with a consideration of whether the supplies properly fell within its terms. HMRC accepted that the supplies constituted "tuition" and were given "privately" for the purposes of the law. The appellant did not claim that kickboxing was a

university subject. The only question was therefore whether the classes in kickboxing were "school education".

The precedent cases were *Haderer* (Case C-445/05), *Eulitz* (Case C-473/08 and *A&G* (Case C-449/17). *Haderer* contained some relevant comments, but was focused on what was meant by "given privately"; the other cases also concerned the meaning of "privately", but dealt with the scope of "school education" as well. The CJEU appeared to use the word "activities" in a manner that was synonymous with the UK's use of "subjects".

The *Eulitz* case involved consideration of whether a teacher of courses on preventive fire protection could fall within the exemption. The CJEU held that the expression "school or university education" should not be narrowly interpreted, because the education systems in different member states were organised differently; the same type of service should be exempt throughout. It was not necessary for tuition to lead to a qualification or an examination, as long as it involved the transfer of knowledge and skills from a teacher to pupils or students.

The *A&G* case concerned a limited company which operated a driving school. The CJEU considered that driving instruction did not form part of the school or university curriculum anywhere in the EU, and was too specialised to fall within "school or university education". This was the most recent of the decisions and so, if there was any inconsistency between the precedents, it was to be preferred.

The UK Tribunal has also considered the expression in a number of cases, including *Cheruvier* (belly-dancing), *Hocking* (Pilates), *Newell* (motocross/motorcycle maintenance), *Tranter* (yoga) and *Cook* (Ceroc dancing). These were not binding but were considered for their relevant discussion. By contrast, two UK cases that preceded *Haderer* (*Allied Dancing Association Ltd* and *Clarke and partners*) were not accorded any weight because they had been superseded by the European case law.

The judge reviewed the background to kickboxing teaching, which is not subject to the same formalities as some traditional martial arts such as karate or judo. The taxpayer's representatives had carried out a survey of other similar businesses in an attempt to find out whether they taught kickboxing in schools; the judge considered that this indicated that this happened in only a few schools, and there was little evidence that it was part of the school day in those places it was taught (as opposed to being an extra-curricular option). It was not on the National Curriculum, and was mentioned in a Department of Education report as having been rejected because it was not recognised by Sport England. Other martial arts had also been rejected because they were too difficult for teachers and moderators to assess reliably.

The judge decided that it was necessary to answer four questions:

- whether it was necessary to focus specifically on the teaching of kickboxing in EU schools, or martial arts in general;
- whether it would be enough for there to be one school in the EU where it formed part of the curriculum, or whether it had to be "commonly taught";

- whether, on a balance of probabilities, the appellant had produced enough evidence to show the answer to that question;
- whether kickboxing or martial arts as a whole were "purely recreational", in which case they would fall outside the educational exemption.

In examining the first question, the judge agreed with HMRC that there were too many differences between the different martial arts to regard kickboxing as a subset that would enjoy exemption if, say, judo were found to be commonly taught. The differences between martial arts were more like the differences between squash and tennis than the analogy the taxpayer's representative had attempted to draw between indoor and outdoor cycling. It was therefore necessary to consider the other questions in relation to kickboxing alone, or even to the "striking" martial arts alone (as opposed to "grappling").

In relation to the second question, the taxpayer's counsel argued that there was no justification in the PVD for a quantitative test. The exemption for education in schools would apply to education provided by a single school in the EU; the exemption for private tuition should be equally wide. The judge considered the arguments in detail, but concluded that HMRC's case was stronger. There were differences between art.132(1)(i) and art.132(1)(j): school and university education itself was restricted to certain eligible bodies, but covered closely related supplies of goods and services as well. A different treatment of the two exemptions did not undermine the coherence of the provisions as a whole. The conclusion was that private tuition of an activity would only fall within art.132(1)(j) if the activity was commonly taught at schools or universities in the EU.

Turning to the next question (the evidence provided of the extent of teaching in the UK), the judge agreed with both parties that the fact that the subject was not on the National Curriculum was not determinative. It was what happened in practice that mattered. However, it did lead to a presumption that such teaching was not common, because it was not required. It was also necessary for the teaching to happen as part of the school's educational activities, rather than simply taking place on school premises in a lunch break or after school club. As the surveys dealt with martial arts in general, and even in relation to that did not produce conclusive results in relation to the question of whether they were "commonly taught", the taxpayer had failed to discharge the required burden of proof.

In relation to the fourth question (which was strictly unnecessary, because the taxpayer had already lost), the judge considered the question of what was "purely recreational" in some detail, and concluded that kickboxing was more than that: it "expressly promotes, in its participants, aspects of personal development such as self-discipline, respect for others, confidence, manners, teamwork and focus in addition to teaching various physical skills."

Finally, the judge considered briefly whether the UK legislation was consistent with the PVD as interpreted by the CJEU, and concluded that it was: "subjects" and "activities" were effectively the same, and the implication of the CJEU decisions was that "covering school and

university education" meant that an activity had to be "ordinarily" taught. The appeal was dismissed.

First-Tier Tribunal (TC07509): *Premier Family Martial Arts LLP*

2.3.5 Welfare services

Two providers of welfare services appealed against HMRC rulings that their supplies were taxable. By the time they arrived in the Court of Appeal, the cases had been joined together. Here is a brief history of the earlier decisions:

Life Services Ltd: in 2016 the FTT (TC05197) held that UK law breached fiscal neutrality in exempting any charity providing welfare but imposing extra conditions on a commercial entity in direct competition but, apart from that, the UK law did not allow exemption – it was not a "state-regulated entity" within item 9 Group 7 Sch.9 VATA 1994; in late 2017 the Upper Tribunal confirmed that the company did not qualify under the law, but stood over the fiscal neutrality point to be heard with the other case.

The Learning Centre (Romford) Ltd: in 2017 the FTT held that the company did not qualify as a state-regulated entity in England, but this breached fiscal neutrality because an identical business would have required state regulation in Scotland; in early 2019 the Upper Tribunal overturned this decision and ruled that fiscal neutrality was not infringed. In addition, the Upper Tribunal did not agree with the FTT in *LIFE Services* that there was unjustified fiscal discrimination between charities and unregulated commercial organisations: in reality, only those charities that had objects in the welfare sphere would supply such services, and therefore only that subset of charities would enjoy exemption.

The judge listed the principles from CJEU precedents in relation to the exemption for welfare services:

- First, the objective pursued by Article 13A(1)(g) is to reduce the cost of welfare services and to make them more accessible to the individuals who may benefit from them: Case C-498/03 *Kingscrest Associates Ltd v Commissioners of Customs and Excise* [2005] ECR I-4427 at [30].
- Secondly, the expression "charitable" in Article 13A(1)(g) is to be given an autonomous interpretation in EU law: *Kingscrest* at [27].
- Thirdly, the expression "organisations recognised as charitable" does not exclude private profit-making entities: *Kingscrest* at [47]; and Case C-174/11 *Finanzamt Steglitz v Zimmerman* [EU:C:2012:716] at [57].
- Fourthly, Member States have a discretion when laying down rules concerning the recognition of organisations other than bodies governed by public law as "charitable": Case C-141/00 *Ambulanter Pflegedienst Kügler GmbH v Finanzamt für Körperschaften I in Berlin* [2002] ECR I-6833 at [54]; *Kingscrest* at [49] and [51]; Case C-415/04 *Staatssecretaris van Financiën v Stichting Kinderopvang Enschede* [2006] ECR I-1385 at [23]; and *Zimmerman* at [26].

- Fifthly, in order to determine the organisations which should be recognised as "charitable" for the purposes of Article 13A(1)(g), it is for the national authorities, in accordance with EU law and subject to review by the national courts, to take into account, in particular, the existence of specific provisions, be they national or regional, legislative or administrative, or tax or social security provisions; the public interest nature of the activities of the taxable person concerned; the fact that other taxable persons carrying on the same activities already enjoy similar recognition; and the fact that the costs of the supplies in question may be largely met by health insurance schemes or other social security bodies: *Kügler* at [57]-[58]; *Kingscrest* at [53]; and *Zimmerman* at [31].
- Sixthly, the exemption provided for in Article 13(A)(1)(g) may be relied upon by a taxable person before a national court in order to oppose national rules incompatible with that provision. In such cases, it is for the national court to establish, in the light of all relevant factors, whether the taxable person is an organisation recognised as "charitable" for the purposes of that provision: *Kügler* at [61]; and *Zimmerman* at [32]
- Seventhly, where a taxable person challenges the recognition, or the absence of recognition, of an organisation as "charitable" for the purposes of Article 13A(1)(g), it is for the national courts to examine whether the competent authorities have observed the limits of the discretion granted by that provision whilst applying the principles of EU law, including, in particular, the principle of equal treatment, which, in the field of VAT, takes the form of the principle of fiscal neutrality: *Kügler* at [56]; *Kingscrest* at [52] and [54]; and *Zimmerman* at [33].
- Eighthly, the principle of fiscal neutrality is not a rule of primary EU law against which it is possible to test the validity of an exemption provided for under Article 13A or which makes it possible to extend such an exemption. Accordingly, the principle of fiscal neutrality does not preclude Article 13A(1)(g) from making it unnecessary for public bodies to be recognised as "charitable" while requiring such recognition in the case of other organisations: *Zimmerman* at [50] and [53].
- Ninthly, compliance with the principle of fiscal neutrality requires, in principle, that all the organisations other than those governed by public law be placed on an equal footing for the purposes of their recognition for the supply of similar services: *Zimmerman* at [43].
- Tenthly, national legislation may not, in implementing the exemption provided for under Article 13A(1)(g), lay down materially different conditions for profit-making entities, on the one hand, and non-profit making legal persons, on the other: *Zimmerman* at [58].
- Lastly, for the purposes of determining whether the limits of the discretion have been exceeded, the national court may, on the other hand, take into account in particular the fact that, under VATA 1994, entitlement to the exemptions provided for in Article 13A(1)(g) extends to all organisations registered under the Care Standards Act 2000, as well as the fact that that Act and VATA contain specific

> provisions which not only reserve entitlement to those exemptions to organisations supplying welfare services, the content of which is defined by those Acts, but also govern the conditions for providing those supplies, by making the organisations which provide them subject to restrictions and checks by the national authorities, in terms of registration, inspection and rules concerning both buildings and equipment and the qualifications of the persons authorised to manage them: *Kingscrest* at [57].

The CA confirmed the decisions below that the status of the appellants under the Care Act 2014 did not amount to "state regulation". Even though it was argued that they carried out functions that were delegated to them by local authorities, and the law deemed acts and omissions of delegates to be treated as acts and omissions of the local authority, nevertheless this did not mean that the delegate was approved or registered under the Act. The local authorities were not regulated; if they had carried out the services directly, they would have been exempt for a different reason. In addition, the CA did not consider that the relationship between the companies and the authorities amounted to delegation of functions within s.8(2)(b) of the Care Act, as contended by the taxpayer's representative, but under s.8(2)(a) and (c), which carried less implication of "approval" or "registration".

The CA also confirmed the decision of the Upper Tribunal on fiscal neutrality. The CJEU precedents showed that fiscal neutrality did not only require consideration of the services themselves, but also the context in which they were supplied. The law distinguished between those entities that could provide exempt welfare services – all charities, and state-regulated private welfare bodies – and those that could not, which were unregulated private welfare bodies. Charites had to be established solely for charitable purposes for the public benefit, and were subject to supervision by the Charity Commission. Members of the public regarded charitable provision in a different way to commercial provision: it was not in direct competition. There was little difference between services provided by charities and those provided by state-regulated providers; but there was a significant difference between services provided by unregulated providers and by charities.

The question of discrimination between Scotland and Northern Ireland, where similar services were state-regulated, and England and Wales, where they were not, was also dismissed by the CA as irrelevant. The distinction remained that between regulated and unregulated entities; the fact that a business was required to be regulated in some parts of the country and was not required to be so regulated in other parts did not invalidate the application of the VAT law.

The appeal was dismissed.

> Court of Appeal: *Leisure, Independence, Friendship and Enablement Services Ltd v HMRC; The Learning Centre (Romford) Ltd v HMRC*

2.3.6 Article

In an article in *Taxation*, Mitch Young discusses the FTT decision in *RSR Sports Ltd*, and compares the treatment of welfare services for children in other cases.

Taxation, 20 February 2020

2.4 Zero-rating

2.4.1 Digital newspapers

The publisher of *The Times*, *The Sunday Times* and *The Sun* claimed zero-rating for the daily digital editions of its newspapers on the grounds that they were "newspapers" and therefore covered by VATA 1994 Sch.8 Group 3 item 2, or else had to be given the same treatment as the paper versions on the grounds of fiscal neutrality. The FTT (Judge Brannan) heard appeals against decisions covering the periods September 2010 to June 2014 and January 2013 to December 2016.

The FTT judge (TC06385) noted the history of the relief for newspapers, which were free of Purchase Tax from 1940 to 1973; this was continued for VAT under the authority of what is now PVD art.110, which allows Member States to retain "exemption with deduction of input tax" for categories of supply that were so treated on 1 January 1991, provided that the rules were adopted for clearly defined social reasons and for the benefit of the final consumer, and were in accordance with Community law. The social policy required by Article 110 which lay behind the UK's decision to zero rate newspapers and books etc was the promotion of literacy, the dissemination of knowledge and democratic accountability by having informed public debate.

The judge reviewed the production of the titles and compared the printed and digital versions. It was suggested that the characteristics of a "newspaper" included that it was an "edition-based" publication, rather than comprising "rolling news" such as might be found on a website. The digital versions of these titles satisfied that definition.

The company's counsel argued that the purpose of the legislation would be served by treating digital publications as zero-rated. He also suggested that the 1973 wording should be updated to apply to present-day technology, rather than being frozen at the time it was written.

HMRC's counsel responded that the wording of Group 3 clearly referred to supplies of goods, not services. There was no doubt that digital newspapers were electronically supplied services (the rules on place of supply in Sch.4A include them in a definition). There was also a clear distinction in the EU legislation; allowing zero-rating would be an impermissible extension of zero-rating.

The judge agreed with HMRC that the implication of the wording of Group 3 was that it related to goods. The idea of legislation being interpreted in accordance with current technology ("always speaking") was set out in a speech by Lord Wilberforce in *Royal College of Nursing v DHSS* (1981), and it excluded the situation in which there was an apparent intention that the law should be restrictive in its operation. As zero-rating was an exception to the general rules of VAT, it was not possible to use a purposive interpretation to extend the scope of the relief beyond the straightforward meaning of the words.

The judge went on to consider the issue of fiscal neutrality. Although he was satisfied that the digital editions satisfied similar needs of customers to the print editions, he did not accept that this was enough to require an extension of the scope of the legislation. In accordance with the *Deutsche Bank* decision of the CJEU, fiscal neutrality could not override the clear words of the law; the 1991 "standstill" in art.110 was such a clear requirement.

HMRC's counsel sought to rely on the recent Commission consultation on the possibility of extending reliefs to digital publications, which implied that they were not currently entitled to the same treatment, and also on art.98, which excluded digital publications from the lower rate. The judge did not consider either argument was particularly relevant in the interpretation of UK law on zero-rating.

Nevertheless, he accepted HMRC's fundamental position and dismissed the appeals.

The company appealed to the Upper Tribunal, where it came before Mr Justice Zacaroli and Judge Greg Sinfield. They summarised the FTT decision as "although the digital versions are the equivalent to the newsprint editions, they are not 'newspapers' within the meaning of Item 2." The company argued that the digital editions were properly to be regarded as "newspapers", and even if they were not, the principle of fiscal neutrality required them to be treated in the same way as the print versions.

HMRC responded by arguing that the FTT's finding that the digital editions were similar to the print versions of the newspapers was one which no reasonable tribunal could have reached; they also introduced the new argument that the company's case was inconsistent with Articles 96 to 99, 110 and 114 of the PVD.

The decision starts with a consideration of what is meant by a "strict" interpretation of the statute, to be balanced with giving effect to Parliament's purpose. "A strict construction is not to be equated, in this context, with a restricted construction": it should be consistent with the objectives which underpin the provision and not in such a way as to deprive a relief of its intended effects.

The legislative purpose of Item 2 was a matter of common ground: to promote literacy, the dissemination of knowledge and democratic accountability by having informed public debate. This amounted to "clearly defined social reasons" within art.110 PVD, so as to justify the preservation of the zero-rating of newspapers upon the UK's accession to the EU.

The "always speaking" doctrine was examined, giving the example of dogs: "*If Parliament, however long ago, passed an Act applicable to dogs, it could not properly be interpreted to apply to cats; but it could properly be held to apply to animals which were not regarded as dogs when the Act was passed but are so regarded now.*" The FTT had concluded that "always speaking" was ruled out by the standstill clause operating from 1 January 1991. The Upper Tribunal disagreed, and distinguished the present situation from the *Talacre* case, in which the standstill provision had been considered by the CJEU: in that case, the UK law specifically excluded the contents of caravans from zero-rating,

whereas in the present case, the question was whether the term "newspapers" should be construed as including the digital versions that have come into existence since 1991.

The judges went on to consider the meaning of "newspapers" in item 2 of Group 3, and the FTT's conclusion that Group 3 only dealt with supplies of goods. They considered that the FTT had been wrong to decide this; the restriction in item 6 to physical supplies did not imply that items 1 to 5 were so limited, and the restrictions in notes 1(b) and note 2 were not present in the legislation when it was originally enacted in 1972. The extension in note 1(b) to cover loans of goods did not imply that only goods could be covered in the first place. Overall, as s.30 VATA 1994 referred to "goods and services", it was not material whether something constituted "goods" or "services" for its inclusion in Sch.8; it was whether it fell within the categories described.

HMRC raised a challenge to the finding that the digital editions were similar to the print editions on the ground that no reasonable Tribunal could have reached that conclusion on the basis of the facts that it had found. The judges reviewed the findings and concluded that this attack failed to reach the high threshold required by *Edwards v Bairstow*. The differences between the print and digital editions, both in terms of content and functionality, were not as significant as the similarities.

Having rejected (1) the FTT's conclusion that the fact that the digital versions are not goods precludes them from being newspapers within Item 2; (2) the FTT's conclusion that either or both of Article 110 of the PVD and the requirement for a strict construction precludes reliance on the "always speaking" doctrine; and (3) HMRC's challenge to the FTT's findings of fact, the remaining question was whether, on the basis of those findings, including that the digital versions are the same or very similar to the newsprint editions, the application of the "always speaking" doctrine leads to the conclusion that the digital versions are "newspapers".

Dictionary definitions were inconsistent and therefore not conclusive. It was necessary to consider not only whether the innovative product met the legislative purposes underlying the zero-rating of newspapers; it would also have to share the essential characteristics of newspapers. The FTT had decided that it did.

HMRC also argued that art.98 specifically excluded the application of lower rates to electronically supplied services, until it was amended by a Directive in 2018. The judges considered that this was irrelevant: art.98 had no application in this case, because zero-rating was permitted under art.110, and the zero rate was not a "reduced rate" within art.98.

Because the judges decided that the digital versions were "newspapers" within the meaning of the legislation, and therefore zero-rated under the statute, it was not necessary to consider the question of fiscal neutrality. The appeal was allowed.

Upper Tribunal: *News Corp UK and Ireland Ltd v HMRC*

Jim Burberry and Philip Munn discuss the above decision in an article in *Taxation*, and recommend making protective claims.

Taxation, 23 January 2020

HMRC have announced that they will appeal the *News Corp* decision to the Court of Appeal. Pending the outcome of the appeal, they clearly expect to receive claims from other taxpayers. The argument that an electronic "book" would also be covered by the decision, if it is upheld, is even stronger; "journals and periodicals" are part of the same item as "newspapers".

HMRC say that they will reject any claims made in reliance on the decision. "This approach will help to keep the handling of claims as simple as possible for both parties, minimising the time and resources spent on administering claims while protecting the revenue." The Brief sets out the conditions for making a claim (covered by SI 1995/2518 reg.37):

- The claim must be in writing;
- It must provide a full description of the supplies for which the claim is being made and which item of Group 3 Sch.8 VATA 1994 they are argued to fall in;
- It must explain the reasons for claiming that the supplies should be treated in the same way as those in the case;
- It must include a breakdown of amounts of overpaid VAT being claimed by prescribed accounting period and the method by which they have been calculated.

HMRC say that "a claimant must be able to give, on request, copies of documentation used in the calculation of a claim. If insufficient information is given in support of a claim it will be rejected and the organisation will need to resubmit its claim with the requisite information."

There have been many cases over the years since the 2009 "last chance to make historic reclaims" in which HMRC have argued that otherwise valid claims failed on the technicalities of the procedure. The points that people have failed to appreciate include:

- Failure to include all the requirements of reg.37 as set out above;
- Failure to lodge an appeal within 30 days of HMRC refusing the claim.

It is interesting that HMRC say they may ask for supporting documentation immediately, given that they are committed to refusing the claim on principle. It seems likely that they will test whether claims have been properly made in accordance with the statutory procedures. If they have not, then time (the four year deadline for reclaims) runs against the taxpayer until the deficiency is rectified.

Often claims made before 31 March 2009 were rejected, but no appeal was lodged; the claimants only revisited the matter once a test case had been won by another taxpayer several years later. In almost every case, the Tribunals have struck out such late claims – the claimant was held to have taken a decision not to pursue the matter, and could not reopen it.

Revenue & Customs Brief 01/2020

2.4.2 Budget change

The Budget on 11 March included the announcement that zero-rating would be extended to digital versions of books, newspapers, magazines and academic journals with effect from 1 December 2020. The law will probably attempt to exclude supplies which are in effect the provision of information to a limited audience; there used to be a distinction between (for example) investment circulars sent to clients on paper (zero-rated) and then faxed or e-mailed (standard rated). As the paper was always incidental to the information on it, it seems likely that such a supply will not be brought back into zero-rating.

The date is interesting: as the UK will still be in the transitional period on 1 December 2020, it appears that:

- either HMRC are accepting that the change does not breach the standstill provision in art.110, suggesting that digital newspapers were always covered by the zero-rating rule, or
- this is a breach of that standstill provision.

Budget Red Book 2.233

2.4.3 Food

The FTT has heard an appeal on the old question of whether something is zero-rated as "food" or falls within one of the excepted items, or one of the items overriding the exceptions. In this case, the issue was whether the product – "Nouri healthy balls" – should be standard rated as confectionery. The appellant had applied for a non-statutory clearance to confirm its view that the products should be zero-rated; they received an unfavourable answer on 23 March 2018, confirmed on review on 29 May 2018 and appealed on 19 June 2018.

The products are small balls made from dates, nuts and other natural ingredients with no added sugar. They are promoted as being vegan, gluten free and healthy but indulgent. At the time in question, they were produced in three flavours, matcha green tea, coconut and chia seeds and chocolate and hazelnuts. They were sold in packs of three balls and also in a "luxury box" of 16 truffles, also containing a fourth flavour not relevant to this appeal.

HMRC's Notice 701/14 stated that "confectionery includes chocolates, sweets and candies, chocolate biscuits and any other 'items of sweetened prepared food which is normally eaten with the fingers.' Items of sweetened prepared food don't need to have added sweetening if they are inherently sweet, for example, certain fruit and cereal bar products." The Notice contains a list of examples of items that are on each side of the line. Cereal and compressed fruit bars, unless they qualify as cakes, are standard rated.

The Tribunal sampled the products and described the experience. They examined the list of ingredients and nutritional information. Crucially, HMRC produced evidence of how the product was marketed – that contradicted efforts by the company to characterise them as something that would be eaten as part of a meal, rather than in the same way as sweets. They were presented as comparable to, but healthier than, ordinary chocolate truffles.

The judge noted the appellant's objection that that there are many posts on the company's Facebook and Twitter accounts and all the ones produced had been included by HMRC who had chosen them to make their point. That may be the case, but the screenshots we saw had a consistent message and the appellant had the opportunity to, but did not, include other posts and pictures which might have given a different view.

The judge referred to the principle set out by Lord Woolf in *Ferrero Rocher*: "The words in the statute must be given their ordinary meaning. What is relevant is the view of the ordinary reasonable man in the street." The Tribunal considered the various arguments in some detail, but came to "the short, practical answer to the short, practical question: 'are the products confectionery?' – yes."

The taxpayer tried the "Jaffa cake test" – producing a plate of various items, including the products, that had been left out for a week, and arguing that the Nouri balls had gone stale in the same way as cakes do. She argued that the products did not look "out of place" on a plate with cakes, and that they shared features with Pulsin' bars, which had succeeded in the Tribunal (TC06909). The Tribunal concluded that the well-informed ordinary person would form the impression that the products were not cakes.

An argument based on fiscal neutrality failed because the evidence was inconclusive. The trader provided a survey that only showed the confusion in the food market about what ought to be zero-rated – the same product was treated differently by different supermarkets, and similar products were treated differently in the same supermarket. It would be necessary to show that the appellant's products were effectively identical to something that was regarded as falling within the zero-rating provision as a matter of law, and "the appellant has not even begun to satisfy these requirements".

The Tribunal agreed with HMRC's classification of the products as confectionery, and dismissed the appeal.

First-Tier Tribunal (TC07570): *Corte Dilitto UK Ltd*

2.4.4 Review of food rules?

The Association of Taxation Technicians has called on the government to take the opportunity afforded by Brexit to review the current zero-rating rules for food. As illustrated by Tribunal decisions, many of the rules for food and drink derive from the old Purchase Tax regime, which was replaced with VAT when the UK joined the EU in 1973. As a result, they are often out of date and difficult to apply in the modern world. A clearer, more up to date set of rules would reduce confusion, and save both businesses and HMRC the time and costs associated with arguments over VAT treatment.

ATT Press release 13 March 2020

2.4.5 Zero rating for dispensing prescribed drugs

The Value Added Tax (Drugs and Medicines) Order 2020 adds "EEA country health professionals" and "approved country health professionals" to the list of practitioners entitled to treat supplies of drugs they prescribe as zero-rated for VAT. It partly comes into effect on 1 April 2020 and

fully at the end of the transition period for the UK's withdrawal from the EU (currently 31 December 2020).

SI 2020/250

HMRC have published a Brief explaining this change. The Regulations also provide for a further amendment at the end of the implementation period. This is as a result of changes introduced in *The Human Medicines Regulations 2012*. VAT zero rating is extended to private prescriptions issued by EEA and Swiss doctors for the first time subject to the same conditions as currently apply to UK prescriptions. HMRC have also issued a tax information and impact note on the changes.

Revenue & Customs Brief 2/2020

2.4.6 Women's sanitary products

The Spring Budget included the announcement that the reduced rate of 5% on women's sanitary products will be replaced by zero-rating on 1 January 2021. The ability to extend zero-rated is described as a benefit of leaving the EU. The removal of the 5% tax is estimated to save the average woman £40 over a lifetime.

2.4.7 Supplies to disabled persons

An engineer who was disabled after a serious accident in 1993 set up a business adapting and repairing personal transport devices for disabled persons. He did not do this with a profit motive; he registered for VAT in 2011, and reclaimed input tax on the basis that his supplies were zero-rated. He was selected for investigation in 2017; his records were deemed inadequate to support the zero-rating of his supplies, and he was assessed to disallow the input tax he had claimed. The amount was initially £30,586, later reduced to £28,134 as two periods were held to be out of time.

The problems were many:

(a) Input tax had been claimed on invoices to a third party;

(b) Input tax had been claimed on items where VAT had not been charged;

(c) Input tax had been claimed on non-recoverable items, such as fuel, business entertainment and food items;

(d) The necessary certificates for zero rating were not held;

(e) The necessary supporting documents required to submit repayment VAT returns could not be provided despite requests.

The judge noted that the trader felt that he had been victimised, and that HMRC had asserted that he was dishonest. However, HMRC had a duty to protect tax revenues, and dishonesty was no part of their statement of case: rather, in his zeal to assist his customers to obtain a VAT relief to which they would be entitled if they were disabled, the taxpayer had misunderstood what was allowable input tax for him to claim. In addition, he had a casual approach to record keeping, and was therefore unable to prove that he had complied with the regulations as he was required to do.

The appeal was dismissed.

First-Tier Tribunal (TC07498): *Dr Martin Osment (t/a Zippy Engineering Services)*

2.5 Lower rate

2.5.1 Chairlifts

A company operated an indoor snow dome and conference facility ("the Snow Dome"). This has lifts which are used to transport passengers to the top of the two indoor ski slopes. The primary retail shopping centre is in a separate building from the leisure complex. HMRC ruled that lift passes were not eligible for the lower rate of VAT and raised assessments for periods 1/6/2013 to 30/11/2014 (£156,160) and 1/12/2014 to 29/2/2016 (£138,555). The company appealed to the FTT (TC06308).

The company had started to account for lower rated VAT from 1 June 2013, shortly afterwards also claiming a repayment backdated to 1 April 2013 (£20,097). Group 13 ("cable-suspended passenger transport systems") had been introduced to Sch.7A with effect from 1 April 2013.

HMRC argued that the lift passes were excluded by Note 1, which provided that the lower rate would not apply to the transport of passengers to, from or within a place of entertainment, recreation or amusement, by the person who supplies a right of admission to, or a right to use facilities at, such a place.

The company argued that sale of a lift pass did not constitute a right to use the facilities. It was not mandatory to buy a lift pass to access the facilities. In correspondence the company had argued that Scotland's other snow sports resorts applied the lower rate to their lift passes, but at the hearing the company did not seek to rely on fiscal neutrality.

Judge Anne Scott examined the way in which the business operated. She noted that the company earned its revenue from the sale of lift passes. Customers were entitled to borrow skis, boots, snowboards, poles and helmets without charge, and those bringing their own equipment did not receive any discount. It would in theory be possible for someone with their own equipment to use the facilities without buying a lift pass and without using the lift, but this was not advertised.

The FTT judge noted that both parties concentrated on the nature of the supply of the lift pass. She concluded that the supply made by the appellant when selling a lift pass was access to the lift for the duration specified on the pass. Anyone could access the slope but someone purchasing a pass, in doing so, acquired an ancillary contractual right to use the slope provided they behaved safely. The wording of Note 1 then clearly applied: it was the appellant that supplied the right of admission to the place of amusement or recreation. It did not matter whether the price paid for that admission was included in the lift pass, or was not charged at all. The appeal was dismissed.

The company appealed to the Upper Tribunal, arguing that the FTT had erred in law in concluding that the company supplied a right to use the facilities at the snow dome. VAT disregarded supplies made for no

consideration, and there was no charge for admission. In addition, the principle of fiscal neutrality required that the indoor lifts should be treated in the same way as the lifts at outdoor resorts.

HMRC contended that the FTT decision had been correct, even though some of its reasoning was not supported. It would be artificial to divide up the company's supply, which was principally that of allowing the use of the facilities. If there was a supply within Item 1, it was excluded by Note 1, because it was ancillary to a provision of the facilities. It was irrelevant that some people could walk up the slope without paying; the case was concerned with the treatment of the consideration paid by those who did pay.

As regards fiscal neutrality, there had been no findings of fact about comparability of supplies in the FTT decision. An appeal to the UT could not succeed without such findings. In any case, HMRC contended that the supplies were not similar and not in competition with those of outdoor resorts.

The UT judges (Lord Tyre and Judge Andrew Scott) rehearse the facts and findings of the FTT at some length, but the decision is relatively brief. The judges agreed with the appellant that the key question was to consider what was supplied for consideration, and that was the lift pass. There was no doubt, as a matter of contract, that the customers were paying for the supply of transport: people were free to use the snow dome without it, but use of the lifts was absolutely conditional on holding a pass. That demonstrated the reciprocity between supply and consideration demanded by the precedent cases.

HMRC argued that customers were "really" paying for the facility of enjoying the ride down the snowslope after travelling up on the lift, but it was equally possible to characterise the customer's aim as to be able to ski the slope without the inconvenience of walking up. That analysis made it clear that what the customers were paying for was the transport, not the facilities. If anything, the supply of the facilities was incidental to the main supply of the transport.

The appeal was allowed; it was therefore not necessary to consider the fiscal neutrality argument, but the UT commented that if it had been necessary, there would have been insufficient findings of fact by the FTT to allow an appeal on that basis.

Upper Tribunal: *Snow Factor Ltd v HMRC*

2.6 Computational matters

2.6.1 Updated Notices

HMRC have updated the following Notices to reflect the revised treatment of single and multi-purpose vouchers from January 2019:

- Notice 727/2: Bespoke VAT retail schemes
- Notice 727/3: Point of sale VAT retail scheme
- Notice 727/4: Apportionment VAT retail schemes

- Notice 727/5: Direct calculation VAT retail schemes

2.7 Discounts, rebates and gifts

Nothing to report.

2.8 Compound and multiple

2.8.1 Books and courses

The *Metropolitan International Schools* (MIS) dispute continues its course through the courts, although it has probably now reached its final destination. Here is a brief history:

- in January 2000, HMRC agreed with the school a method to apportion fees for distance learning courses between standard rated education and zero-rated printed matter (about 25:75);
- in 2005, the case of *College of Estate Management* (*CEMA*) was decided by the House of Lords, leading HMRC to regard "courses with books" as likely to be a single supply of education (in that case, all exempt);
- in August 2009, HMRC sent MIS a letter stating an opinion that, in the light of *CEMA*, the company's supplies were all standard rated, and proposing to assess for output tax going back to April 2006 (the time limit at the time);
- the company appealed successfully to the FTT, which held that the supplies were all zero-rated;
- before that appeal was heard, HMRC accepted that withdrawing the letter with retrospective effect was unfair (i.e. they withdrew the assessment from 2006 to 2009);
- HMRC won an appeal to the Upper Tribunal, which held that the company was making a compound supply that was not simply printed matter;
- permission to appeal to the Court of Appeal was refused;
- the CA heard an appeal about whether the company could argue on the basis of "legitimate expectations" in the FTT, and held that it could not;
- HMRC served a winding-up petition in respect of unpaid VAT, but this was struck out as an abuse of process;
- at last, the company's application for judicial review of the decision to rescind the 2000 letter was heard by the Upper Tribunal.

The company argued that it was unreasonable for HMRC to apply a new basis of collecting VAT without giving a reasonable notice period, and also that the agreed method should be applied to the remainder of

contracts concluded before the 2009 letter was sent (the college agreed the prices for three-year courses at the outset).

The Upper Tribunal had to consider whether the application should proceed on the basis that the college had an arguable case with a realistic prospect of success. It was true that HMRC had appeared to make a clear, unambiguous and unqualified representation that it would apply the method in the 2000 letter even if the result was that the school paid less VAT than it would have done under the letter of the law. However, the 2000 letter also gave HMRC the right to review, amend or withdraw the agreement at any time. There was no representation that HMRC would apply the method after such an amendment or withdrawal.

The express power to terminate the agreement "at any time" was fatal to the company's case. Arguments based on proportionality and fairness were also rejected. The application for judicial review was refused.

Upper Tribunal: *R (oao Metropolitan International Schools Ltd) v HMRC*

2.8.2 Magazines and activities

A company sold activity boxes for children, treating them as mixed supplies containing zero-rated printed matter. HMRC initially argued that they were all wholly standard rated, but after a review conceded that the larger items containing books could be treated as mixed. They maintained that the smaller boxes, which contained a magazine, was a standard rated supply. The total assessed initially was just under £700,000 for periods from 01/14 to 07/17; this had not been revised for the review concession, but the Tribunal was asked to give a decision in principle.

The Tribunal reviewed the history of the development of the product, and also its composition. The smaller boxes had been developed to fit through a letterbox. The company carried out surveys of its customer base, and the results of one from August 2018 was produced in evidence: 161 customers responded out of 16,305 who received an online newsletter. This was considered a reasonable response according to industry standards, and highly likely to produce representative answers.

Of those who responded, 91.3% said that the magazine was "important" or "very important", and only 8.7% said it was "not at all important". There was a wide variety of responses to a question asking how much the magazine might retail for on its own; the average was £2.50, which was about half the price of the product as a whole.

The company also produced evidence that its turnover had increased substantially after introduction of the magazine. That was argued to show that the magazine was important to customers.

The dispute had started when the company's accountants asked HMRC to agree how the apportionment between SR and ZR elements should be carried out. The larger boxes contained only items bought in from third parties, so the apportionment was based on cost; the smaller box contained items produced in-house, so the apportionment was based on salaries and time spent. The result was an effective rate of 6.04% on the smaller box. HMRC ruled that the product was wholly standard rated, and extended their enquiry to the other products as well. This led to the assessments, a review, ADR, and a further review, and eventually to the Tribunal.

The Tribunal referred to the principles of compound and multiple supplies from *Card Protection Plan*: the starting point is that each supply should be treated as an independent supply, but if the essential features of the transaction show that there is a principal supply to which another supply is ancillary, there is a single supply for VAT purposes. A single supply should not be "artificially split": one should ask why, objectively, people are likely to want it. Other precedents considered were the 2017 FTT decision in *Harley-Davidson Europe Ltd* and the CJEU judgment in *Levob*. *Levob* provided an alternative test to *CPP*: there was a single supply where the components are so closely linked that they are not of benefit to the average consumer if they are supplied in isolation. The 12 principles cited in *Honourable Society of Middle Temple* were also quoted (see 2.3.3 above).

The Tribunal summed up the principles to apply by noting that the "typical consumer" to be considered is someone who receives the actual goods or services in question, and not merely a person who receives other goods or services from the supplier or who receives similar goods and services from other suppliers (the *Ice Rink* case). In the present case, this was a person who had received a free taster box and had signed up to subscribe for regular deliveries of the smaller product.

HMRC argued that the magazine (or "pamphlet") was obviously linked to the craft activities, in that it contained instructions on how to complete them. It was not sold separately during the period under review, and the fact that it was now so sold was irrelevant to the assessments.

The company relied on the results of its survey to show that the customers used the products at different times for different purposes, and both parts were significant to them. It would not be artificial to split them. HMRC's representative suggested that a 1% response rate was not enough to give a reliable result.

The judge noted that the instructions for the crafts were attached to the magazine, but were not part of it. HMRC had accepted that the larger products were mixed supplies, even though the books were "themed" with the craft contents. The smaller boxes had originally been sold without the magazine, and the magazine was now sold on its own, so it was clearly possible for each element to stand alone. It was not artificial to split them.

The decision went through the factors from *Middle Temple*, weighing each one, and came to the overall conclusion that the magazine was "an aim in itself" for the typical consumer. The judge (Marilyn McKeever) appeared keen to make it clear that this was a decision of fact:

"We have considered all the evidence, written and oral, examined samples of the Petite boxes and taken into account all the other circumstances of the case. We have weighed the various factors and principles which may be drawn from the authorities. We consider that the most important factors to which we should have regard are the 'principal/ancillary supply' test derived from *CPP* and the test from *Levob* that we should consider whether there is a single economic supply which should not be artificially split. We have also given appropriate weight to the other factors identified and set out in Middle Temple.

Having performed the required balancing exercise we conclude that the magazine is not ancillary to the supply of the craft activities but is a

valued resource in its own right and that it is not artificial to split the supplies."

The appeal was allowed.

First-Tier Tribunal (TC07505): *Dodadine Ltd*

2.8.3 A complex case

A company appealed against a decision that its supplies of occupational health services (such as medicals, heath surveillance, vaccinations, sickness absence management and drug/alcohol testing) constituted exempt supplies of medical services. It argued that it provided standard rated supplies of information and advice to employers. The dispute had been running for some 10 years.

Initially, HMRC believed that each individual supply was exempt healthcare. Following a presentation by the company's accountants, HMRC accepted that the company was making a single complex supply, but maintained that it was exempt. The company argued that it made a single complex supply to its corporate clients, and that fell outside the exemption.

Both parties also accepted that some services fell on the other side of the line: HMRC accepted that pre-employment medicals, pension scheme medicals, ergonomic assessments, laboratory services and administration charges were all standard rated; the appellants accepted that executive medicals were exempt.

Shortly before the hearing, the appellants changed their position. Their skeleton argument was filed and served on the basis that RPS was making separate single supplies which were all standard rated other than executive medicals and vaccinations. HMRC objected to this sudden change of position. The Tribunal adjourned the hearing with directions; by the time the hearing resumed, the appellants had reverted to their original position (single supply, standard rated).

The parties had agreed that the supply was a single, indivisible one (with the separate elements being ancillary to the main supply), and submitted that the Tribunal should therefore not consider that question. Due to the adversarial nature of the Tribunal process, the parties contended that the Tribunal could only consider the question that was in dispute between them. The Tribunal judge (Anne Redston) disagreed: she could not make a decision that she considered to be wrong in law, so she should consider and decide whether the company was making single separate supplies or a multiple supply. Because of the extent of the disagreement between the parties, this necessitated lengthy findings of fact – the decision runs to over 400 paragraphs.

Helpfully, the judge starts with a summary of the decision:

(1) where RPS provides an OH practitioner to deliver a range of services for a fixed price from an onsite or mobile clinic, this is a single indivisible economic supply of exempt services, being made up of elements which are so closely linked that it would be artificial to split them;

(2) otherwise, RPS provides separate single supplies on a bespoke basis. The overwhelming majority of these supplies are exempt, with ill-health

retirement medicals, medico-legal services, administration charges and training courses being standard rated.

12 We therefore substantially agreed with HMRC on classification, in that we found almost all the services to be exempt. We may have differed from HMRC on the classification of the following services, where they were supplied separately:

(1) ergonomic assessments and employment questionnaires/medicals given to new employees. These are exempt. HMRC had initially accepted they were standard rated, although by the end of the hearing, Ms Newstead Taylor submitted they were part of a single exempt supply; and

(2) training courses and medico-legal services are standard rated; HMRC's position was that they were part of a single exempt supply.

The judge noted that two of the company's witnesses were "partisan" and not entirely reliable: it seems that they knew what they needed to say to support the company's case. For example, one of them claimed that training staff on "manual handling" was to increase their efficiency, but the documentation all pointed to the purpose being to protect them from injury. The tender invitations prepared by clients suggested that the health of their workers, rather than profitability, was the main objective. This was also what the employers told their staff.

The decision examines the law on health and safety at work, and goes into detail about the requirements of clients from their supplier. Some of the clients were anonymised, with HMRC's agreement, because the nature of their requirements for OH services was argued to be potentially damaging to their businesses.

The judge explained why she considered that she had to examine the question of compound and multiple supplies, contrary to the views of both parties, and why she came to a different conclusion from both of them. She listed out a large number of supplies that she considered to be made separately and individually. The requirements of different clients were different: it was not possible to characterise most of the contracts as single, overarching supplies. The judge summed up this section by saying "Neither Counsel was able to put a coherent and consistent case for RPS making a single supply because it was not possible to fit the facts to that submission. In coming to that conclusion, we mean no disrespect: both Counsel were doing their best to put their client's cases."

If she was wrong on this question, or if she was wrong and she did not have jurisdiction to consider it, she would have decided that the company made single, overarching supplies of healthcare services, based on the aims of the customers in wishing to protect the health of their employees. The provision of information to employers was the result of the service, not its objective or fundamental nature.

The appeal was dismissed.

First-Tier Tribunal (TC07643): *RPS Health in Business Ltd and other*

2.9 Agency

2.9.1 Staff or services

A company provided services to Ayrshire and Arran Health Board. HMRC ruled that the business constituted taxable supplies of staff; the company argued that it was supplying exempt healthcare. The company appealed to the FTT.

The company had a contract to "provide staff to the NHS so that the NHS can meet their obligations in relation to the healthcare of inmates at HMP Kilmarnock". HMRC argued that it was clear that the obligation to provide healthcare rested with the NHS, and the appellant provided the staff to enable the NHS to fulfil that obligation. In support of their argument they cited Notice 701/57 section 6. The key point is that the distinction between taxable staff and exempt services is determined by who exercises direction and control over the health professionals.

The appellant argued that the contract reflected a supply of medical services. If it were merely a supply of staff, the supplier would not need professional indemnity insurance. The doctors did not work under the direction or control of the Board's management. It was the purpose of the exemption to reduce the cost of healthcare, which would be frustrated if VAT were imposed in these circumstances.

The judge asked for detailed submissions on the legal background for such contracts, in order properly to understand the background to the appeal. She concluded that the law "is decidedly convoluted and lacks clarity". In brief summary, Health Boards have an obligation "to provide or secure the provision of primary medical services as respects their area". It was explicitly contemplated that such provision could be either direct or through a third party provider.

Judge Anne Scott examined the background to the contract, including the tendering process. She considered the responsibilities of the company and the Board, and how the doctors worked in practice. In line with decisions such as *SecretHotels2*, it was necessary to consider the contract first, and then the commercial and economic reality of the situation. She summed up her findings by saying that "The reality is that the Appellant has had a free hand to decide what the GPs do, how they do it and when, and that is very clearly borne out by the Determination in the FAI [Fatal Accidents and Sudden Deaths Inquiry] and by the witness evidence. If the Appellant supplied staff only, then as Mr Simpson graphically put it, the Appellant's responsibility would stop at the prison gate. It most certainly did not."

The judge found that the Board exercised no control in relation to how the appellant delivered medical care in the prison. It appeared that the contract was largely ignored by the Board's management. The judge rejected HMRC's argument that the autonomy was limited to clinical autonomy exercised by the doctors, rather than economic autonomy exercised by the appellant. It was the appellant that decided on ways of working, training requirements, the provision of locums and all disciplinary matters.

HMRC's guidance was held to be irrelevant to a decision that was based on the findings of fact. The company provided exempt healthcare services, and was therefore not liable to register. The appeal was allowed.

First-Tier Tribunal (TC07557): *Archus Trading Ltd*

2.10 Second hand goods

2.10.1 Repossessions

A hire purchase company claimed repayment of £24m of output tax accounted for on sales of vehicles that had either been repossessed or voluntarily surrendered at the end of finance agreements. The claims related to the period from 1 July 2010 to 30 June 2014, and the FTT (TC06811) was asked to give a ruling in principle, with the amount to be settled separately if the ruling favoured the taxpayer.

The company had accounted for output tax on the full amount of the sales. It now contended that it should have been liable to a lower amount on one of two bases:

- either the margin scheme ought to apply to the sales; or
- if not, art.4(1)(a) of the Cars Order should take the supplies outside the scope of VAT as the sale of a repossessed item.

The second proposal was based on a contention that the 2006 restriction on this rule, brought in to prevent the double relief that was enjoyed in the *General Motors Acceptance Corporation* case, did not apply. That restriction was supposed to impose output tax on the full amount of any resale where the finance company was able to adjust the output tax on the first sale of the car as a result of the repossession (which this taxpayer did). The company argued that the restriction was only compatible with EU law if the margin scheme applied to the sale; if it did not, then it should be unenforceable.

The basis of the company's overall position that it must succeed on one or other argument to avoid double taxation. As the customers of its HP sales would not be able to recover VAT on the first sale to them, charging VAT again on the full proceeds of a second sale would result in a double charge. This would be contrary to art.1 PVD. It was common ground that all of the customers, for both the first and second sales of the vehicles involved in the appeal, would not be able to recover input tax on their purchases.

The company contended in the FTT that the margin scheme should apply because the customers "supplied" the car back to them at the end of the finance agreement. This was described as a "novel proposition" by the judge (Harriet Morgan). The consideration given by the company for this "supply" was the release from the obligation to pay the remaining amounts due under the original agreement, which were then used to reduce the consideration on that first supply under reg.38. The company also argued that this was logically consistent with art.14, which regarded the HP purchaser as having bought the car at delivery; if the end of the agreement did not involve a supply back to the company, it could not validly make a further supply to anyone else.

The company argued that its "margin" on the second sale was the difference between the amount that the customer had paid under the

finance agreement (as adjusted) and the amount received on the second sale at auction. This was normally negative, so no output tax would be due. The application of the margin scheme would therefore normally achieve the same result as the non-supply relief.

The judge set out an analysis of the way traditional HP and "PCP" sales work. PCP agreements involved lower monthly instalments and a large "balloon payment" at the end before the purchase of the car. Where a customer chose not to pay the "balloon payment", the contract provided for the company to sell the car as the customer's agent. Cars sold in this way were not included in the claim. Where a customer had paid at least half the total amount due under the agreement, it was possible to terminate voluntarily without incurring a cost (subject to any excess mileage and damage charges); where a customer defaulted on the payments, the company would repossess the car (a "forced termination").

The judge also included a numerical example of how the VAT accounting works:

- suppose the company pays £120 for a vehicle acquired from a dealer – that includes £20 of VAT;
- the company charges £120 of capital to the customer, receivable in 10 instalments, each including £2 of VAT;
- this involves a cash flow cost, in that the £20 of output tax is due to HMRC immediately on the sale, even though it will be collected from the customer later;
- if the customer terminates voluntarily halfway through the agreement, he has paid £50 of net capital plus £10 of VAT, so the company adjusts the output tax on the sale from £20 to £10.

Unfortunately, the judge's numerical example is not clear in relation to a forced termination – she says that "if the termination occurs on the customer's default and VWFS sells the vehicle for £30, VWFS makes a VAT adjustment under regulation 38 reflecting an amount equal to the sales proceeds of £30 as a reduction in the consideration for the HP supply. VWFS may be able to claim bad debt relief in respect of the remaining amount owed of £20". If the customer had paid half of the amount due, the £30 and the £20 here appear to be net amounts rather than gross, and the judge does not spell out the effect on the output tax.

As a preamble to considering the merits of the company's argument, the judge set out the history of the "desupply provision". She noted that it was introduced before the adjustment mechanism in reg.38: at that time, it was needed because otherwise the HP company would clearly have suffered double taxation. If it made the first sale for £120 (gross), received £60 before repossessing the car, and then made a second sale for £60, it would be liable for the full £20 on the first sale and £10 on the second. The *GMAC* case resulted from the introduction of the reg.38 mechanism without any restriction on the desupply rule: the courts held that the clear words of the law gave that company both reliefs at once – it was entitled to reduce the VAT on the first sale to £10, and to account for no VAT on the second. The purpose of the amendment in 2006 was to allow one relief or the other, which should produce a fair result.

HMRC argued that there was no question of double taxation in the circumstances put forward by the company. The company's position would result in it enjoying full relief for the VAT on the original cost of the car, but it would not charge output tax on the full amount received for the sale(s). The margin scheme should only apply if there was a supply for consideration by the customer to the HP company, which (according to HMRC) was not the case.

The CJEU had considered a similar situation in the later *GMAC* case (Case C-589/12) in which HMRC sought to deny a historic repayment on the basis that the operation of both reliefs together would provide a "windfall". The court refused to help the UK government: the reg.38 adjustment was based on a directly effective EU right, and the desupply rule was a provision of national law that the taxpayer was entitled to rely on. The fact that the national law gave an extra relief could not be a reason to deny a directly effective right. The judge interpreted this decision as confirming that the CJEU considered that the operation of both reliefs together would result in under-taxation.

The judge went on to examine CJEU decisions on the margin scheme, including *Commission v Ireland* (Case C-17/84) and *Jyske Finans v Skatteministeriet* (Case C-280/04). These decisions confirmed that the scheme was intended to prevent double taxation where a dealer acquired goods for sale from someone who could not themselves recover VAT on an earlier purchase; but also confirmed that the scheme was an exception to the normal rules of VAT, and therefore had to be applied only to the strict circumstances prescribed by the Directive.

The judge sought to illustrate her view that the company would not suffer double taxation was set out in the following continuation of her numerical example:

The VAT effects if the scheme applies to a resale and if it does not apply are best illustrated by an example as follows:

(1) A financier purchases a car from a car dealer for £100 plus VAT of £20.

(2) The financier agrees to provide the car to the customer under a HP transaction under which the customer is to pay a capital amount for the car of a total of £120 due in 10 equal instalments of £12 (plus interest costs and related fees). This represents the capital amount of £100 and VAT of £20 to be collected by the financier at £2 per instalment.

(3) At the outset the financier accounts for the VAT of £20 charged on its purchase of the car as input tax and for output tax of £20 in respect of the HP supply on the full amount of capital instalments due of £100.

(4) The financier has borrowed £120 to fund the total amount it pays for the vehicle of £120 (including VAT of £20). As noted, it recovers the output tax of £20 from the customer only over time when the capital instalments are paid.

(5) The customer terminates the HP transaction voluntarily at a point when it has paid £60 of the instalments due, comprising £50 representing the capital amounts and £10 representing output tax for which the financier has accounted on the HP supply.

(6) The financier's VAT account is adjusted under regulation 38 by treating the unpaid capital amount of £50 as a reduction in the consideration for the HP supply. On that basis it is liable to account for output tax of £10 only in respect of the HP supply on the reduced sum of £50. The financier, therefore, receives a refund of £10 of VAT overcharged on the HP supply. At that point the customer's irrecoverable VAT cost is fixed at £10.

(7) The financier takes back possession of the car and sells it at auction to a third party purchaser for a VAT inclusive price of £60 which includes VAT of £10. As established in the cases, this is a separate supply of goods for VAT purposes. Assuming the margin scheme does not apply, the financier accounts for output tax on the supply of £10, which it has to pay to HMRC. The purchaser at auction correspondingly has an irrecoverable VAT cost of £10.

(8) Overall, the financier incurs recoverable input tax of £20 (on its purchase of the vehicle) and accounts for output tax of £20 (£10 on the HP supply and £10 on the sale at auction). Correspondingly this gives rise to irrecoverable VAT costs of £20 in the hands of the consumers (£10 for the customer and £10 for the purchaser at auction).

(9) In cash terms the financier has received £120 in respect of the transactions undertaken which equals its original cash outlay of £120 (disregarding subsequent finance charges). It receives (a) £60 from the customer in respect of the HP supply (being the amount paid up to the date of termination), (b) £10 in respect of overpaid VAT (as a result of the VAT adjustment on termination to reflect that £50 (and the related VAT) is no longer due) and (c) £50 on the sale at auction (£60 of the net sales proceeds received less £10 of output tax which the company has to account for to HMRC).

If VWFS' approach is instead applied, under the margin scheme the finance company would not be liable to account for VAT on the auction sale at all or for a minimal amount of VAT only.

(1) The financier again sells the vehicle at auction for £60 (that being the auction price regardless of any VAT charge).

(2) The profit margin under the scheme is the difference between (a) the purchase price, being the amount the financier paid for the vehicle and (b) the selling price, being the amount it receives on the sale at auction. The selling price is, therefore, £60.

(3) On VWFS' analysis the customer supplies the vehicle to the financier in return for consideration equal to the instalments which are no longer due from the customer. I take that to be the purchase price. (I note that VWFS argues that the value of that consideration should be taken to be equal to the actual sums paid by the customer to the date of termination. I have addressed that argument below.) It is not clear to me whether, on VWFS' argument, that amount is to include the VAT element of the instalments or not. I have set out the position in each case.

(a) If the purchase price is £60 (including the VAT element of the instalments), the profit margin is zero so that no VAT charge is due on the sale.

(b) If the purchase price for the purposes of the scheme is £50 (leaving the VAT element of the unpaid instalments out of account), the profit margin is £10 (£60 received at the auction sale less £50). The resulting VAT is £1.67.

(4) The overall result in the scenario in (3)(a), therefore, is that the financier incurs recoverable input tax of £20 only and accounts for output tax of £10 only on the HP supply and no VAT on the repossession sale. In cash terms the finance company would receive £130 in respect of the transaction undertaken which exceeds its original cash outlay of £120 (disregarding finance charges). As before it receives £60 from the customer in respect of the HP supply and £10 in respect of overpaid VAT. However on the auction sale it receives an increased amount of £60 as it does not have to account for VAT out of the sales proceeds.

(5) In the scenario in (3)(b), the result is the same except that the financier is liable to account for a total of £11.67 of output tax and in cash terms realises £1.67 less overall.

The fallacy in the company's argument is identified as the proposition that there is unrelieved VAT that needs to be taken into account on its second sale. Although the consumer has suffered irrecoverable VAT, it is effectively reduced by the reg.38 adjustment; and the original cost of the car is effectively a cost component of both of the company's sales, relief for which would be double counted on the company's approach.

The judge then considered in detail whether the margin scheme could apply to the repossession and resale of cars. This depended on the repossession constituting a "supply" by the customer surrendering the car. The judge examined art.14 PVD in detail and also cases including *Mercedes-Benz* (Case C-164/16). In her view, there was no separate transaction on repossession: it was simply an exercise of rights arising out of the original contract. The commercial and economic reality of the situation was that there was no supply by the customer. The company's arguments that it provided consideration to the customer for the return of the vehicle were likewise unconvincing. That meant that the terms of the PVD did not bring the resale within the margin scheme.

At the conclusion of 246 paragraphs, the FTT judge held that the company could not enjoy the desupply rule if it had made adjustments under reg.38, and could not use the margin scheme. It had correctly accounted for output tax on the full amount of resales, and its appeal was dismissed.

The company appealed to the Upper Tribunal, where it came before Mr Justice Zacaroli and Judge Timothy Herrington. It only pursued the argument that the margin scheme should apply to the second sale. It was common ground that this required the return of the vehicle to VWFS to constitute a supply of goods (within art.14 PVD) for consideration (as required by art.2 PVD).

Both parties agreed that the supply by VWFS at the outset of the finance agreement was within art.14(2)(b) PVD; the essence of the appeal was VWFS's argument that the return was a supply of goods within art.14(1) ("the transfer of the right to dispose of tangible property as owner"). The company's representative argued that art.14(1) effectively required the expression "supply of goods" to be read as meaning "the transfer of the right to dispose of tangible property as owner" wherever it appeared in the

PVD. This would bring the return of the car at the end of the finance agreement within art.14(1), by operation of what the judges described as mathematical logic, or the continuation of a "fiscal fiction" that the right to dispose as owner had been transferred to the lessee at the outset.

They did not accept this logic. Art.14(1) gave one example of something that is to be regarded as a supply of goods; art.14(2) gave three more. They were separate provisions and did not interact in the way the appellant contended. This was made clear by the opening words of art.14(2): "in addition to the transaction referred to in para.1".

The judges accepted that it was possible that, during the currency of the agreement, the contract restricted some of VWFS's rights – the company could not "dispose of the goods as owner". However, on repossession it did not reacquired those rights by transfer from the lessee, but simply as a result of the contractual restrictions lapsing.

The company also argued that the FTT had erred in its conclusion that no consideration was given for the return of the car. The UT held that there had been no error. It was necessary to analyse a transaction in accordance with its contractual basis, while paying attention to the commercial and economic reality. The company argued that there was consideration for the same reasons that the CJEU imputed consideration to the voucher scheme in *AstraZeneca*: the choice exercised by the lessee to return the vehicle in return for not having to pay the outstanding instalments was similar to an employee choosing to receive vouchers instead of some salary. The judges disagreed. The reality was that the lessee received nothing of value. The reduction in liability was matched by the reduction in the availability of the car.

The judges considered that the appeal still rested on the argument that VWFS suffered double taxation if it accounted for VAT in full on the second sale. This was not put forward as a separate reason for allowing the appeal, but the company's representative argued that it constituted the background against which the PVD should be construed. The company argued that there was irrecoverable VAT "embedded in the vehicle" when it was returned to VWFS, and the whole scheme of VAT required that the company should obtain relief for it – if not by deduction, then by operating the margin scheme.

The judges disagreed. It was true that the original customer could not recover VAT, but that did not mean that it was "embedded in the car". Rather, that VAT charge was related to the use of the car during the currency of the contract, which was treated as a supply of goods in accordance with art.14(2)(b) but was more akin to a supply of services. It was apparent that, if VWFS received half the value of the car from the HP lessee before repossession, and then sold the car a second time for half its original value, it would have received total sales proceeds of the full original price of the car; but, on VWFS's argument, it would only have to account for output tax on half of that. That could not be right.

For all these reasons, the FTT had come to the correct decision, and the appeal was dismissed.

Upper Tribunal: *Volkswagen Financial Services (UK) Ltd v HMRC*

2.11 Charities and clubs

2.11.1 Guidance for charities

HMRC have updated their detailed guidance notes on how the tax system operates for charities. This mainly focuses on direct tax obligations and reliefs, but also makes some references to VAT. It has been updated to update references to the Charities Act 2011; detailed consideration of the background to that Act was part of a recent Upper Tribunal case (*Eynsham Cricket Club*) which turned on the difference between a charity and a community amateur sports club.

www.gov.uk/government/publications/charities-detailed-guidance-notes

2.12 Other supply problems

2.12.1 Updated Manual

The *VAT Assessments and Error Correction Manual* guidance on transfers of a going concern has been updated to include updated contact details for returns with a due date on or after 1 April 2009.

VAEC3520

2.12.2 Student article

In an article aimed mainly at exam students, Edd Thompson reviews the TOGC rules.

Taxation, 30 January 2020

2.12.3 Updated Notice

HMRC have updated their Notice *Business promotions* from the May 2012 version. The main change concerns the new VAT treatment of face-value vouchers from 1 January 2019. Other changes include clarification on the meaning of ‘gift’ and disposals of obsolete stock.

The following comments on multi-purpose vouchers are a reminder of how complex the rules became in 2019:

9.6 Input tax deduction

The consideration for the issue or transfer of a multi-purpose voucher is disregarded for VAT purposes so there is no output tax to account for on the issue or transfer. This means that the issue and transfer of a multi-purpose voucher in isolation is not regarded as a supply which would permit the deduction of input tax.

Where the issue or transfer of multi-purpose vouchers is done in order to facilitate a different supply, or is a necessary part of a different supply, VAT incurred in relation to the entire activity may be deductible as input tax (where, of course, it is a taxable activity). The extent of this will depend on individual circumstances, an important factor is whether the

issue or transfer of multi-purpose vouchers is subsumed within a wider commercial activity.

For example in the case of a retailer that issues its own multi-purpose vouchers, so they are used later to purchase goods or services from that retailer, the VAT incurred in relation to the issue of the multi-purpose vouchers is attributable to the supply of those goods or services. Where a voucher is not redeemed, the VAT becomes an overhead cost.

A business which supplies promotional or marketing services, and ancillary to this is the issue or transfer of multi-purpose vouchers, may be able to attribute the VAT it incurs to those promotional or marketing services. A trade organisation which supplies a vouchers management service to its members, issuing vouchers on their behalf, may be able to attribute the VAT it incurs to those membership services.

Input tax that relates to a number of activities may need to be apportioned using a fair and reasonable method using similar principles to those set out in section 32 of Notice 700.

Notice 700/7

3. LAND AND PROPERTY

3.1 Exemption

Nothing to report.

3.2 Option to tax

3.2.1 Circular rules

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 FTT judge (TC06539) 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.

The taxpayer appealed to the Upper Tribunal, where it came before Lord Ericht and Judge Dean. They reviewed the facts and the law, and examined the circularity of the law, in detail. They found no fault with the FTT's reasoning or decision: the FTT had applied the test (of the transferor's intention or expectation at the time of the grant) correctly, by reference to the appellant's knowledge of the facts of the transaction and not by reference to his knowledge of the statutory provisions. He had issued an invoice showing that the transaction was exempt, and could not therefore have intended or expected the land to become a capital item in the hands of the purchaser.

The appeal was refused.

Upper Tribunal: *Moulsdale v HMRC*

3.2.2 Updated Notice

HMRC have updated their Notice *Opting to tax land and buildings* with a new address for the Option to Tax Unit.

Notice 742A

3.3 Developers and builders

3.3.1 Zero-rating certificate penalty

A rowing club issued a zero-rating certificate in relation to the construction of a building to be used by itself and other sports clubs in the local area and also to provide a gym facility for which it would offer membership to non-club members. HMRC ruled that it had done so incorrectly, and charged a penalty under s.62 VATA 1994. The club's initial appeal included the submission that the certificate had been correctly issued, but this was withdrawn after the CA decision in *Longridge on the Thames*. Instead, it argued that it had a reasonable excuse for issuing the certificate.

In the FTT (TC06803), the club argued that it had taken considerable care in deciding to issue the certificate. It had a number of financial and tax professionals as directors and members of the committee that made all the relevant decisions; further advice was taken, including counsel's opinion; the club was aware of the *Longridge* case, which at the time was progressing through the courts with HMRC appealing against decisions in the taxpayer's favour. The certificate was issued in November 2013.

The club treasurer, who was a corporate tax partner in a firm of accountants, set out in some detail the grounds for believing that the club had acted reasonably. It had relied on a Tribunal decision that had not been overturned; it was difficult to see what it could have done differently, because if it had not issued the certificate and the CA had found for Longridge, it would have ended up incurring a significant amount of irrecoverable VAT.

HMRC argued that it was not reasonable to issue the certificate when it was known to be contrary to HMRC's settled policy in the area. They suggested that the club should have approached HMRC, who could have taken protective action and stood the case behind *Longridge*. The club had used Longridge's own counsel, who was likely to give them the opinion they wanted. Even so, he put caveats in his opinion that the club did not follow up. The club asked its accountants for a second opinion; the accountants suggested two options, and recommended one that would have disclosed the situation to HMRC at an early stage. The club chose the other option.

Judge Anne Fairpo set out the test for a reasonable excuse from *Clean Car Company* (VTD 5695): "a reasonable excuse should be judged by the standards of reasonableness which one would expect to be exhibited by a taxpayer who had a responsible attitude to his duties as a taxpayer, but who in other respects shared such attributes of the particular appellant as the tribunal considered relevant to the situation being considered."

On this basis, she considered that the club did not have a reasonable excuse. Given the awareness that counsel's opinion depended on *Longridge* succeeding on appeal, and the uncertainty that entailed, a reasonable person would have taken one of the options that would have notified HMRC of the situation, rather than waiting to see if HMRC objected. The appeal was dismissed.

The club appealed to the Upper Tribunal, where it came before Judges Swami Raghavan and Kevin Poole. They considered that it was necessary

to extract in more detail the correspondence and advice that were given in the run up to the issue of the certificate than had been given in the high level summaries in the FTT decision.

This more detailed recording shows that the advice was taken at various stages and on different points in relation to the construction project. The second Baker Tilly report was obtained after the opinion from Longridge's counsel had explained the possible application of the FTT decision in that case. BT had put forward two possible structures:

- Option 1, which was to issue the ZR certificate, which had the benefit of simplicity but required the agreement of the building contractor and ran the risk of a later challenge by HMRC;
- Option 2, which was to enter into a lease-and-leaseback arrangement with a trading subsidiary, which would enable the subsidiary to recover input tax charged by the builder (and to make a zero-rated grant of a long lease for use for a RCP) – that would be more complicated, but the builder would charge VAT, and it would be more likely to be examined earlier by HMRC, leading to earlier certainty.

The club treasurer gave evidence that Option 1 was selected because Option 2 appeared complicated and possibly contrived.

The club's appeal was based on the following grounds:

(1) the FTT was wrong to characterise the second Baker Tilly report as making a clear recommendation to advise HMRC of the position at the earliest opportunity (failure to comply with which recommendation necessarily rendered Marlow's actions unreasonable);

(2) whether (1) is correct or not, the FTT was wrong to regard Marlow's failure to approach HMRC as necessarily depriving Marlow of any reasonable excuse, because any such approach before issuing the certificate could not have resulted in an appealable decision, and any approach to HMRC after issuing the certificate could not affect the reasonableness or otherwise of issuing the certificate in the first place.

The UT considered (2) first. The question of whether the club could have obtained an appealable decision was a matter of law, on which the FTT could have made an appealable mistake. The club pointed out that an unregistered entity could not obtain an appealable ruling; HMRC responded that their Charities Division would, to assist traders, provide binding letters to charities on their right to issue certificates, and these could be produced in evidence if a dispute followed. Redacted examples were shown to the UT. However, they would only do this if the supply had commenced, because the courts would not consider theoretical questions.

The UT set out the dilemma that this presents to a taxpayer: "If Marlow thought, knowing its view of the law was different from HMRC, that it ought to be able to issue a certificate, it would not be able to get an appealable decision before the supply commenced. However, if Marlow had decided, despite its view that the supply was zero-rated, not to issue a certificate and to then pay standard rate VAT it was not at all clear how Marlow could then go about recouping that VAT given, as noted above, it

is a pre-condition for zero-rating that the zero-rating certificate was issued before the supply was made."

As the club could only have obtained an appealable decision after the supply commenced, and as the certificate had to be issued before the supply was made, the issue of obtaining an appealable decision could not be relevant to a reasonable excuse for issuing the certificate. HMRC's concessionary practice of allowing ZR for certificates issued after the supply had commenced would rely on the supplier adjusting output tax was also not relevant, because the application of a concession would not be within the jurisdiction of the FTT.

Concluding that an appealable decision could have been obtained was an error of law by the FTT. The UT could then remit the case to the FTT or could re-make the decision. The judges decided that their detailed examination of the correspondence enabled them to remake it, applying the procedure for consideration of reasonable excuse given in *Perrin*:

(1) First, establish what facts the taxpayer asserts give rise to a reasonable excuse (this may include the belief, acts or omissions of the taxpayer or any other person, the taxpayer's own experience or relevant attributes, the situation of the taxpayer at any relevant time and any other relevant external facts).

(2) Second, decide which of those facts are proven.

(3) Third, decide whether, viewed objectively, those proven facts do indeed amount to an objectively reasonable excuse for the default…. In doing so, it should take into account the experience and other relevant attributes of the taxpayer and the situation in which the taxpayer found himself at the relevant time or times. It might assist the FTT, in this context, to ask itself the question "was what the taxpayer did (or omitted to do or believed) objectively reasonable for this taxpayer in those circumstances?...

The key issues, according to the UT, where the significance of the advice given taking account of the context in which it was sought, and whether the club should have taken the option suggested by Baker Tilly which it was said would have elicited certainty in HMRC's view sooner, and/or sought advice from HMRC.

Baker Tilly's first report clearly stated that the supplies of building services would be standard rated. However, this was called into question by the *Longridge* FTT decision; counsel's opinion was based on the information available at the time, and although there were points of difference between Longridge and a members' club, this did not appear to be relevant to the *Longridge* decision.

HMRC argued that the advice was taken in order to mitigate penalties, rather than out of a genuine attempt to establish the liability of the supply. The club denied this; it was clear from the correspondence that the treasurer was unaware of how a s.62 penalty operated, appearing to believe that it would be charged in addition to collecting the VAT (as with the CT penalties he was more familiar with).

The club argued that Baker Tilly's second report did not express an unreserved recommendation to adopt Option 2. The committee had valid

reasons for preferring the simplicity of Option 1, which also avoided the need to consider various SDLT and charity law issues.

The UT set out a number of principles at the start of its discussion:

- the fact that the committee had some expertise in tax was relevant in considering the standard of reasonable care to be expected;
- the mere taking of legal advice could not automatically confer a reasonable excuse, because each case would have to be considered on its facts;
- the motivation behind taking the advice was relevant, in that the taxpayer must genuinely be trying to establish the right thing to do, but "mitigating a penalty" was not necessarily fatal because avoiding a penalty suggested that the taxpayer was doing the right thing.

The UT accepted that there were various caveats and limitations in counsel's opinion, but, read as a whole, it was clear advice on which the club was entitled to rely. The club had attempted to implement the limitations in the advice, in that:

- the certificate was only issued in respect of the proportion of the building occupied by the club for RCP;
- other points were covered by a report to the AGM in July 2013 that showed an intention by the club to meet the objectives that would make the opinion applicable.

The fact that *Longridge* was decided against the taxpayer at the Court of Appeal could not be counted against there being a relevant excuse at the time the certificate was issued. It would not have been wildly optimistic at that point to expect the FTT decision to survive (it was upheld by the Upper Tribunal).

Most significantly, the UT did not think that there would have been any point in approaching HMRC after receiving the advice and before issuing the certificate. The fact that HMRC were appealing the *Longridge* decision made their answer predictable, but it could have been no more than their view of the law, which was at that time questionable because of the very decision they had lost. HMRC's view would have been no more reliable than that of a professional adviser. In *Greenisland FC*, the Upper Tribunal had "given short shrift" to an argument that the taxpayer should have obtained HMRC's advice "in any event" – Notice 708 contains no such suggestion.

In conclusion, the judges decided that the committee acted reasonably in seeking advice from professionals and not asking HMRC, and in issuing the certificate, even though that was incorrect. The appeal was allowed. Although that represented a windfall for the club, that was inherent in a scheme which, while it charges a penalty of the amount of tax that ought to have been charged, allows the taxpayer to escape the penalty charge where it has a reasonable excuse.

Upper Tribunal: *Marlow Rowing Club v HMRC*

3.3.2 Residential conversions

A sole trader supplied building services to a property dealing company he owned. He treated various supplies as eligible for the reduced rate;

HMRC raised best judgement assessments for periods from 12/14 to 03/17 totalling £59,184 on the basis that the standard rate should have applied.

The company acquired two-storey residential properties with a view to converting them into houses in multiple occupation (HMOs). Initially it acquired terraced properties, but then saw the potential for extra profit in acquiring semi-detached properties with land to the side on which extensions could be built. Planning permission was sought for a separate dwelling while the extension was being built; the owner had informed HMRC of this "phased approach" at an initial meeting. The appeal concerned 25 properties, all of which had been extended; 14 had been converted into two or more separate dwellings.

HMRC considered that the input tax claim, in relation to purchases of £100,000 of materials, was more likely to relate to the construction of extensions than to conversions to HMO use. An expert witness told the Tribunal that very little work was usually required to carry out such a conversion (often little more than installing locks on the bedroom doors).

HMRC's approach was as follows:

- as there was no evidence of multiple occupation, none of the supplies was eligible for the reduced rate;
- construction of extensions could be zero-rated from the date that planning permission was granted for construction of a new dwelling (14 cases), but was standard rated up to that point;
- those properties that had been extended without conversion into two or more dwellings (11 cases) were subject to standard rated VAT.

Because the records were not adequate to allocate supplies accurately to particular properties, various estimates had been made in arriving at the amount of the assessment. The amount relating to residential conversions under Sch.7A Group 6 was estimated at zero; the Tribunal held that this should be amended to £1,000 per property, to reflect the minimal alterations necessary, but otherwise was to best judgement.

None of the supplies could qualify for the reduced rate under Group 7, because the empty property condition was not satisfied – the director had explained that he let the properties as soon as he acquired them in order to maximise cash flow. It was therefore only possible to qualify under Group 6 on conversion services, not under Group 7 which extended to renovations.

It was possible that services in a conversion that results in a new dwelling separate from the HMO could qualify under Group 6, but this would only qualify once planning permission had been granted. The liability had to be determined at the time of the supply, and by the existence or absence of consent at the time. Similarly, the zero-rating of the construction of a new dwelling in an extension would require contemporaneous planning consent. It would be reasonable to apportion the expenditure on a straight line basis to before and after the planning permission was granted.

The appeal was allowed in part.

First-Tier Tribunal (TC07524): *Gareth Bertram*

3.3.3 Updated Notice

HMRC have updated their Notice *VAT on buildings and construction* to clarify the relevant criteria for the two main types of non-residential conversion:

5.3 Non-residential conversion

A 'non-residential conversion' takes place in 2 situations. The first is when the building (or part) being converted has never been used as a dwelling or number of dwellings for a 'relevant residential purpose', and it is converted into a building 'designed as a dwelling or number of dwellings', or intended for use solely for a 'relevant residential purpose'.

The second situation requires that in the 10 years immediately before the sale or long lease, the building (or part) has not been used as a dwelling or number of dwellings or for a 'relevant residential purpose' and it is converted into a building either 'designed as a dwelling or number of dwellings', or intended for use solely for a 'relevant residential purpose'.

Examples of a 'non-residential conversion' into a building 'designed as a dwelling or number of dwellings' include the conversion of:

- a commercial building (such as an office, warehouse, shop)
- an agricultural building (such as a barn)
- a redundant school or church

The conversion of a garage, occupied together with a dwelling, into a building designed as a dwelling is not a non-residential conversion.

The term 'garage' not only covers buildings designed to store motor vehicles but also buildings such as barns, to the extent that they're used as garages.

But if it can be established that the garage was never used to store motor vehicles or has not been used as a garage for a considerable length of time prior to conversion, its conversion into a building designed as a dwelling can be a non-residential conversion.

Notice 708

3.3.4 Domestic reverse charge procedure

The Budget confirmed that the Domestic Reverse Charge on construction services will be introduced as planned on 1 October 2020. This was delayed for a year from 1 October 2019 because of Brexit and a lack of preparedness among those affected. At this stage, it does not appear that the problems with the latest set of rules and guidance have been addressed, but there may be more awareness in the industry by October.

A small change has been made to the DRC Notice, updating the October 2019 version to add clarification that Reverse Charge Sales List needs to include 'the relevant period' of the reverse charge sales.

Another small change has been made to reflect that businesses can submit details of their Reverse Charge Sales List (RCSL) returns using Making Tax Digital for VAT up to Friday 28 August 2020. Businesses may be liable to a penalty if they fail to submit their RCSL, send it in late or make mistakes.

Notice 735

3.4 Input tax claims on land

3.4.1 DIY claims – time limit

HMRC refused a claim for £25,276 on the grounds that it was made out of time. Planning permission had been granted in February 2012; the schedule of 327 VAT invoices started in March 2012 and finished for the most part in November 2015. The building was fit for habitation in June 2015 and was occupied in August 2015. However, snagging continued into the following year, and the owners did not apply for a completion certificate until December 2016. The council responded in February 2017 that the electrical installation certificate was not valid, because it had to be registered online. As their electrician had retired, this led to delays and the paperwork was not regularised until April 2018. The DIY claim was made in July 2018, within 3 months of the council's completion certificate, but well over the time limit based on completion of construction and on occupation.

The judge (Michael Connell) considered the regulations and a number of previous cases on the same issue. He commented that "Unfortunately the provisions of regulation 201 VATR 1995, although clearly worded, can lead to a misunderstanding as to what is required by HMRC as evidence that a building has been completed for the purposes of the VAT DIY regulations." The appellants had been trying to comply with what they thought the requirement was; however, the certificate itself was neither necessary nor sufficient evidence of the date of completion for the purposes of the regulations. That was found by weighing all the evidence available. The date of occupation and the date of the last invoice were clear indications that the property had been complete over two years before the date of the claim.

The appeal was dismissed.

First-Tier Tribunal (TC07489): *Satish Chander Arora and another*

The same issue was considered in relation to another building project, in this case involving two houses constructed by brothers in the grounds of a house belonging to their father. The appeal concerned only one of the brothers, whose claim had been refused for being out of time; the paperwork for the other brother's claim had been lost, but the judge (Robin Vos) commented that the decision might also be relevant for that claim.

The date of occupation was 1 March 2017. At that stage, the property did not have a permanent electricity or water supply. Instead, temporary supplies were being provided from the father's house. The evidence was not clear, but on the balance of probabilities the judge concluded that the water supply was not connected until after August 2018. A certificate of completion had been issued on 19 February 2018, and the claim was submitted on 8 May 2018.

The Tribunal noted that HMRC's manual states that claims may exceptionally be accepted outside the time limit where there is a reasonable excuse for the delay, including compassionate reasons, negligence of a professional advisor or circumstances outside the claimant's control, such as difficulty and obtaining invoices or completion certificates. However, the UT in *Asim Patel* had stated that the statutory

time limit was mandatory, and in any case a concession could not be enforced by the FTT. The question therefore was when the building was complete.

The judge commented on the impossible position that the legislation puts a claimant in. Only one claim is permitted, which cannot be made before the building is completed, and cannot be made more than three months after it is completed; it appears that the completion certificate is essential to a claim, but HMRC may say that it was issued after the building was completed. The judge concluded that the wording of the legislation suggested that other documentation or evidence could be used to establish a completion date if there was no certificate of completion, but if there was one, the date on it was the date to use. The claim had been made within the required period, and the appeal was allowed.

First-Tier Tribunal (TC07504): *Liam Dunbar*

The same time limit issue arose in a case involving a property in Scotland. Although the point was not raised by either the appellants or HMRC, the judge observed that Building Regulations operate differently in Scotland. It is an offence to occupy a building before the "Notification of Acceptance" is issued; this was not done until 10 April 2018, and the claim was submitted on 4 May.

HMRC refused the claim on the grounds that the building had been occupied by several short holiday lets starting in July 2017; it was therefore both "completed" more than 3 months before the claim, and had been constructed for a letting business rather than non-business use.

The judge accepted that a claim could not properly be made before 10 April 2018, because of the legal difference from England (where, in his view, the completion date would have been in March 2017). On the balance of probabilities, he was satisfied that there had always been an intention to occupy the building as a private holiday home, and the letting was something that had arisen out of necessity when circumstances changed.

The appeal was allowed in principle, and the parties were left to agree the amount of the claim.

First-Tier Tribunal (TC07553): *Simon and Joanne Cotton*

Yet another appeal concerned the question of whether the claim was submitted more than 3 months after the completion of the house. The claim was for £14,032; the claimants (a married couple) had followed HMRC guidance and had not been aware of reg.201 until the proceedings started. The husband (P) pointed out that the purpose of the legislation was to allow claims by DIY builders, and suggested that the scheme should not be operated in such a way as to deny valid claims. HMRC's representative submitted that the three month time limit for making a claim was mandatory, that the Tribunal could not extend the time, and so the only issue for the Tribunal was whether the dwelling was completed earlier than three months prior to the claim being submitted.

The building project had started in 1998. In 2010, P attended a VAT seminar, from which he understood that he had an unlimited time to complete the project, but that a completion certificate had to be submitted with the claim. The couple moved into the property in 2010, and carried

on working on it for the next 7 years. The Tribunal records the progress of the work; it was only on the installation of new windows in October 2016 that the couple considered that they could apply for a completion certificate. There were delays, for reasons beyond their control, in obtaining gas, electricity and energy performance certificates, and the completion certificate was only issued in February 2018. The claim was submitted to HMRC on 27 March 2018.

Correspondence followed through 2018, leading to refusal of the claim on 20 September, confirmed on review on 12 February 2019. The review officer stated that the earlier conclusion was reached on the basis that the more relevant factors to demonstrate completion were when the works had been completed in accordance with the planning permission and to make the building functional. Neither occupation nor a Certificate of Completion were conclusive. The review officer held open the possibility of HMRC extending the time in which a claim could be made if there was a reasonable excuse for the delay in making the claim, but made it clear that could be considered by the original officer only, and not at the Tribunal.

The judge (Jane Bailey) noted that earlier Tribunal decisions were not binding, but that the reasoning could be informative. She also accepted the appellant's argument that such decisions were fact-sensitive, so a decision that completion had occurred at a particular stage in another project did not necessarily mean that it occurred at the same stage in this one.

The judge described the circumstances of four older precedents before commenting "It seems that at some time since 2016, HMRC changed their practice, described in *Morris*, of treating the date on the Completion Certificate as the date on which the building was completed. That change has resulted in a surprising number of reported decisions on this issue within the last year."

As the Tribunal had noted in *Farquharson*, there are difficulties for a DIY builder (and for HMRC) in correctly identifying the date of completion if – as suggested in *Hall,* and argued for by HMRC in this appeal – it is a matter of fact and degree when a building is completed, and the date of completion can be different in each case. It would also be difficult to provide documentary evidence of completion if, for example, it was determined to be at a point where no third party documentation would usually be issued. For example, in the present case, it might be argued that the home was completed when the couple finished installing the en suite bathroom (and for the first time had the washing facilities normally expected in a home). The judge could not see what document the couple might be expected to provide to support a DIY claim for that date.

Other cases referred to by the judge (but not all cited in the hearing) included *Fraser*, *Arora*, *Dunbar*, and *Cotton* (decision issued after the hearing of this case). She concluded that there were two main lines of authority. On the one hand, *Fraser* and *Arora* regarded "completion" as an ordinary term and which place focus upon a variety of factors, including occupation and the homeowner's subjective view, to determine when that has occurred. This approach depends heavily on the facts of the appeal, as determined by the Tribunal and can make it difficult for a DIY housebuilder to understand when a DIY claim should be made.

On the other hand, there are the decisions in *Farquharson* and *Dunbar*, which interpret "completion" in the context of reg.201 and the requirement that a valid claim be supported by a completion certificate or other documentary evidence. This interpretation enables the regulations to be interpreted in a consistent manner which can be easily understood and applied by all taxpayers.

HMRC argued for the first of these approaches, inviting the Tribunal to conclude that the building was completed either in 2010, when it was occupied, or in 2016, when the windows were installed. The judge understood the appellants' approach to be the second, to rely only on the issue of the certificate. However, she held that reg.201 did not give a special definition to "completion", so it had to be interpreted in accordance with its ordinary meaning: it was not essential for a certificate to have been issued in order for a building to be complete. Rather, she considered that for a dwelling to be complete, it must be finished in accordance with the plans for which planning permission was given, and that the dwelling must be able to fulfil its intended purpose. The primary purpose of a dwelling is to function as a safe, hygienic and habitable home.

In earlier cases, the factors considered relevant were the date of occupation, the dates of the invoices, and the DIY builder's own understanding of when the dwelling was complete. The first two were not particularly helpful, and the third was difficult to determine with any precision. The judge considered that the more useful factors for determining the date of completion are when the relevant building has been built in accordance with the relevant planning permission, when it meets the requirements of the Building Regulations and when it is compliant with all other legal obligations for a dwelling.

The planning permission was essentially complied with in this case on completion of the windows in 2016. However, the dwelling must not only be safe, hygienic and habitable but should be demonstrably so. The judge summed up: "Therefore, we conclude that the dwelling was not complete until Mr and Mrs Proffitt were issued with an electrical certificate, a gas safe certificate, and (in this case) a Completion Certificate. Those certificates demonstrated that the dwelling was safe, hygienic and habitable, meeting certain minimum standards. We conclude that a DIY builder should not be able to make a DIY claim in respect of a dwelling said to be lawfully completed until that dwelling can be demonstrated to finished to an equivalent standard to that which a commercial housebuilder would be obliged to meet."

This was not quite the same as the conclusion in *Farquaharson* that the date depended only on the certificate, even though the result was the same; the certificate was one of the factors, and in this case happened to be a significant one.

If that conclusion was wrong, the judge would have found that the building was completed in 2016. The delay until the claim was submitted was due to factors beyond the claimants' control, and appeared to fit exactly the definition of "reasonable excuse" in HMRC's manual. Although the Tribunal had no power to extend the time for a claim or to enforce what was effectively a concession within HMRC's discretion, the

judge would have expected HMRC to reconsider their decision in the light of the Tribunal's view that an extension should have been granted.

The appeal was allowed on the basis of the legal position; a further ground of appeal on the basis of misdirection was not considered further because it was not necessary (and the Tribunal had no jurisdiction, following the Upper Tribunal's decision in *Noor*).

First-Tier Tribunal (TC07614): *Neil Proffitt*

The Tribunal allowed a further appeal in yet another case on the same issue, concerning claims by two brothers for £31,170 and £25,019. The judges reviewed similar precedents and came to a similar conclusion: that in principle completion of a building can pre-date the issue of the certificate of completion. In this case it did so, but nevertheless the claim was made within three months of that earlier date.

The judge (Richard Chapman) listed 11 principles underlying his conclusion that the date of completion was a matter of fact and degree. The last of these was "Finally, in response to the argument that HMRC's own guidance treats the time limit as running from the date of the document being used as completion evidence, we repeat our comment that this guidance does not have the force of law. Further, for the reasons set out above, the guidance is incorrect."

In this case, HMRC argued that the buildings were complete either when they were occupied, in December 2012 and March 2013, or when the works were completed in accordance with the plans in May 2017. The judge disagreed: the works were not complete until December 2017. He was not sure when in that month they were complete, but as the claim was made on 28 February 2018, it was within the time limit.

This conclusion was based on the fact that one brother did not complete a disabled access ramp until that month: the ramp had been a requirement of the local authority before a certificate could be issued, so the building was not complete without it. The other brother was still carrying out landscaping works that were required on the original plans. The fact that invoices predated the works did not prove that the works were still in progress in December.

HMRC submitted to the Tribunal that a decision in the appellants' favour on the time limit should only lead to an adjournment while they considered the other aspects of the claims. The judge took into account that the decisions were solely based on the time limit, but decided that the additional cost and delay of a further dispute would be disproportionate. There was no explanation for the fact that HMRC had not considered other aspects of the claims; in accordance with the overriding objective of the Tribunal to deal with cases fairly and justly, the judge allowed the appeal in full.

First-Tier Tribunal (TC07619): *Paul Wedgbury and another*

3.4.2 DIY claims – planning consent

The occupants of a timber-framed mobile home applied for planning permission to alter and extend it. In the course of the work, the mobile home was completely demolished, and on completion, the occupants made a DIY claim. HMRC refused the claim on the basis that the works were

an alteration or extension of an existing building, as stated in the planning permission. The claimants appealed.

In their skeleton argument, HMRC argued that, if the result was a new building, it was not in accordance with the planning permission and therefore failed on a different ground. The claimants objected to HMRC raising this as an argument at the hearing, as it had not been stated as a reason in their original refusal of the claim. They accepted that, if it was allowed as a matter of procedure, it would defeat their appeal.

The judge concluded that HMRC should be allowed to advance this alternative argument. It was clear that the works did not, as a matter of fact, amount to the construction of an extension; the resulting structure was a new dwelling. The skeleton argument had been issued over six months before the hearing. It was not necessary to conclude on the lawfulness of the building itself, but it was not constructed in accordance with the consent, and the claim therefore had to be refused.

First-Tier Tribunal (TC07513): *John Watson and another*

HMRC refused a claim in a situation in which the planning consent had changed during the course of the project from "extension" to "demolition and construction". As a result, there were different reasons for different parts of the refusal:

- up to the date of the change of the consent, HMRC ruled that the project did not qualify – the claimants argued that the VAT should be recoverable based on the fact that the eventual result was a qualifying project;
- after the date of the change, HMRC ruled that the builders should have zero-rated supplies of services and building materials.

The judge examined various precedent cases in some detail, extracting some principles and disagreeing with others. In essence, however, he agreed with HMRC: up to the date of the change, the builders were right to charge VAT, and it could not be recovered because the project had to be considered in the light of the planning consent in force at the time the supply was made; and a claim under s.35 could not succeed for VAT that should not have been charged. The condition for making a direct claim from HMRC was that the "normal route" (claiming from the builder, who would claim the overcharged output tax back from HMRC) had to be excessively difficult or practically impossible.

The appeal was dismissed.

First-Tier Tribunal (TC07579): *Gavin Franks and another*

Another case involving a change of planning consent was also a refusal on the grounds that the work was not carried out in line with the planning consent in force at the time. The consent had been given for an alteration of an existing building; in the course of the project, an engineer advised that the building was unsound and should be demolished completely. There was no doubt that the result was a completely new building; the council had observed that a new planning application should have been made, but they allowed the building to be regarded as lawful because it had been constructed in line with the original drawings.

The judge (Anne Scott) said that she had no choice but to apply the law, even if that seemed unfair to the claimant. She had no discretion, and dismissed the appeal.

First-Tier Tribunal (TC07561): *David Stewart*

4. INTERNATIONAL SUPPLIES

4.1 E-commerce

4.1.1 VAT MOSS exchange rates

HMRC have published the usual table of exchange rates to be used in MOSS returns for the quarter to 31 December 2019.

www.gov.uk/guidance/vat-moss-exchange-rates-for-2019

4.1.2 Reduced rates for electronic publications

From 18 December 2019, Germany introduced a new reduced VAT rate of 7% for certain electronically supplied services.

The reduced rate applies to the following transactions that are in electronic form:

- printed books, brochures, leaflets and similar printed matter;
- newspapers, journals or periodicals;
- children's picture, drawing or colouring books;
- printed music;
- maps and hydrographic or similar charts – including atlases, wall maps, topographical plans and globes;
- recordings of a book being read.

The reduced rate does not apply to:

- publications that mostly include:
  - video content;
  - audible music;
  - advertising – including travel;
- media deemed harmful to young people;
- products subject to the information requirements under section 15 (1) to (3) and (6) of the Youth Protection Act (Jugendschutzgesetz).

Favourable tax treatment also applies to databases containing a large number of electronic books, newspapers, periodicals, or their parts.

Queries to Poststelle@fa-h-no.niedersachsen.de

Other countries that have also introduced reduced rates for electronic publications include:

- Slovenia, 5% from 1 January 2020;
- Sweden, 6% from 1 July 2019;
- Portugal, 6% from 7 June 2019;
- Belgium, 6% from 1 April 2019;
- Ireland, 9% from 1 January 2019.

www.gov.uk/guidance/changes-to-the-vat-moss-rate-for-other-countries

4.2 Where is a supply of services?

Nothing to report.

4.3 International supplies of goods

4.3.1 Chains

The Value Added Tax (Place of Supply of Goods) (Amendment) Order 2019 was laid before Parliament on 20 December 2019, to take effect from 1 January 2020, to implement the "quick fix" in relation to chain transactions.

SI 2019/1507

The Value Added Tax (Amendment) (No 2) Regulations 2019 was laid and took effect on the same dates as the above order, to implement the quick fix in relation to making it compulsory to record the customer's VAT number and to file a Sales List in order to secure zero-rating of despatches.

SI 2019/1509

On 20 December, HMRC published guidance on the implementation of the new EU rules on chain transactions.

1. Chain transactions

A chain transaction occurs where there are a number of businesses successively buying and selling the same goods but the goods themselves are transported directly from the original supplier and delivered to the final purchaser.

There is no limit to the number of businesses that can be in the chain but it must consist of at least 3 businesses which include the:

- original seller;
- original buyer;
- final buyer who purchases the goods.

Where the goods supplied by the original seller in the member state of origin are transported from that member state and delivered to the final customer in the member state of destination there must be an intra-community supply. The Court of Justice of the EU has ruled that only one transaction in a chain can be treated as the intra-community supply. In a simple chain consisting of 3 businesses, this could be either the:

- supply by the original seller to the original buyer;
- onward supply by the original buyer to the final purchaser.

The new chain transaction rules set out how to determine which supply is to be treated as the intra-community supply. The principle holds good for a chain of any length, irrespective of the number of intermediary buyers.

The new rules make express provision as to which supply is to be treated as the intra-community supply and, in most cases, will achieve the same end result as the UK's current policy does.

The new rules do not affect chain transactions that do not involve a cross-border movement of the goods. In those cases, normal VAT accounting rules will apply in the member state where the goods are located.

1.1 Overview

The new rules provide a simple approach to determining which supply in a chain is the cross-border intra-community supply. The default position is that the intra-community supply is the supply to the person in the chain (the intermediary operator which may be the original buyer or a subsequent buyer in the chain) who arranges for the goods to be moved from the member state of origin to the member state of destination.

All supplies leading up to and including the intra-community supply are to be treated as taking place in the member state of origin and all subsequent supplies are to be treated as being made in the member state of destination.

If that intermediary operator is VAT registered in the same member state as the supplier, then, subject to certain conditions, the onward supply by the intermediary operator can be treated as the intra-community supply.

The businesses involved may not be established or have a fixed establishment in either the member state of origin or the member state of destination but the normal VAT registration rules and reporting requirements will apply to the supplies made by the parties in the member state where the supply takes place.

The new rules are set out in part 4 of the Value Added Tax (Place of Supply of Goods) Order 2004 (SI 2004/3148) and take effect from 1 January 2020.

For more details on the VAT treatment of the supply that is deemed to be the intra-EU supply, read information about the single market (VAT Notice 725).

1.2 Intermediary operator

This legislation defines an intermediary operator as the business in the chain that transports or arranges for the transport of the goods across the EU border.

The intermediary operator cannot be the original supplier. Where the original supplier arranges the cross-border transport, then the normal rules for accounting for intra-community supplies of goods will apply.

Where the final customer arranges for the transport of the goods to itself, the rules will apply and the final customer can be seen as an intermediary operator for the purposes of applying them.

1.3 Intra-community supply

The intra-community supply is deemed to be the supply to the intermediary operator.

If that intermediary operator is VAT registered in the member state of origin, the intermediary operator can opt to treat the onward supply made

by it as the intra-community supply, provided that the intermediary operator supplies its VAT number to its supplier and, in that case, the supply to the intermediary operator will be a normal business to business supply in the member state of origin.

1.4 Final customer

A final customer who otherwise meets the conditions can apply the rules as though they were the intermediary operator. In such a case, the intra-community supply will be the supply made to the final customer and the final customer must account for acquisition tax on the supply in the destination member state.

If the final customer notifies its supplier of a VAT registration number in the member state of origin, the intra-community removal will become a deemed supply of own goods. Read Notice 725, section 9 for more information.

1.5 Business establishments

It is irrelevant to the operation of these rules whether or not the original supplier, the original buyer (or any other intermediaries in the chain) or the final customer are established or have a fixed establishment in either the member state of origin or the member state of destination.

All parties are required to keep to the relevant VAT registration rules and accounting requirements that apply in relation to making the relevant supplies.

1.6 Triangulation

The chain transaction rules can operate in conjunction with the triangulation rules, as long as the triangulation criteria are met.

1.7 Zero rating

Subject to certain conditions being met, a cross-border supply can be zero-rated as a supply in the member state of dispatch. The new rules make some changes to the zero rating conditions.

2. Zero-rating for intra-community supplies

The intra-community supply of goods between businesses is almost always zero-rated for VAT in the member state of origin and taxable as an acquisition by the customer in the destination member state.

Member states are entitled to set conditions to prevent possible evasion, avoidance or abuse of the VAT system and to ensure the correct and straight forward application of this zero rating provision.

The UK, along with most other member states, applies a condition that requires the customer to be VAT registered in the destination member state and the supplier to record that number. This helps make sure that the VAT is not lost where, for example, the goods are supplied to a non-VAT registered person. The UK decided that this was vital in the provisions of the Principal VAT Directive.

In a number of cases, the Court of Justice of the EU concluded that these requirements were not formal conditions with the force of law, meaning that there was some uncertainty as to their status.

2.1 Overview

The new rules add additional formal conditions that must be legislated for, so that for an intra-community supply of goods to be zero-rated, the:

- customer is VAT registered in a member state other than the member state of origin;
- customer has provided the supplier with that VAT number;
- supply is reported on an EC Sales List.

In addition, Article 45a of Council Implementing Regulation 282/2011 sets out a list of documentary evidence and conditions whereby it can be presumed that the goods have been transported across an EU border. As the Implementing Regulation is directly applicable, no further legislation is required to implement it into UK law – it will apply in the UK from 1 January 2020. Read VAT Notice 725 the single market.

2.2 Conditions

VAT number

The requirement for the supplier to obtain the customer's VAT registration number is currently set out in Notice 725 paragraph 4.3 which has force of law. As this is now a legal requirement set out in the Value Added Tax Regulations 1995, the notice will be revised. The other requirements in that paragraph will remain, including the requirement that the VAT registration number be shown on the sales invoice including the 2-letter country prefix code.

Fall-back use of VAT number

While the legislation requires a customer's VAT registration number to be known and disclosed, it does not require that number to be issued by the destination member state. Read the fall-back requirements in Notice 725 paragraphs 7.7 to 7.9.

EC Sales List

There is no change to the general requirement to submit EC Sales Lists. However, submission of an accurate EC Sales List will become a requirement for zero rating a cross border supply within the EU from 1 January 2020. If a supply is not correctly reported on an EC Sales List then any zero rating of the supply becomes invalid and will be cancelled. The effective date of cancellation will be the date of the original supply. Any additional VAT due on the supply may be liable to a penalty and interest.

If the EC Sales List is corrected at a later date, zero rating can be reinstated from that date as long as all the other conditions for zero rating are met. You may still be liable for interest.

If there was a reasonable excuse for the failure to submit the EC Sales List or the failure to provide the correct information, then zero rating will not be cancelled.

Normal penalties for non-submission, late submission and errors on EC Sales Lists are unchanged.

Notice 725, paragraph 17.12 explains penalties.

2.3 Removal evidence

Current requirements

Notice 725, paragraph 4.3 (which has force of law) includes a requirement that you get and keep valid commercial evidence that the goods have been removed from the UK within the time limits set out at paragraph 4.4.

Notice 725, section 5 sets out a list of documents, a combination of which must be used to provide clear evidence that a supply has taken place and that the goods have been removed from the UK. The responsibility is on the business to prove to HMRC that the conditions have been met. Businesses which have difficulty gathering the information required by the new rules can continue to rely on these rules.

New simplification rules

The effect of the new rules is that, where certain conditions are met, it is presumed that the goods have been transported from the member state of origin. This presumption can be challenged by HMRC. If the relevant conditions are met, it is for HMRC to prove that the goods have not been transported from the member state of origin.

Article 45a of Council Implementing Regulation 282/2011 sets out the conditions under which the goods can be presumed to have been removed. The Implementing Regulation is directly applicable, so no further legislation is required to implement it into UK law.

Presumption

The presumptions are met where the supplier confirms the dispatch or transport which was issued by 2 different parties that are independent of each other, of the vendor and of the acquirer and is in possession of one of the following:

- at least two items of non-contradictory acceptable evidence from list A;
- any single item from list A together with any single item of non-contradictory acceptable evidence from list B.

In addition, where the acquirer arranges the transport of the goods, the supplier must be in possession of a written statement from the acquirer, stating that the goods have been dispatched or transported by the acquirer, or by a third party on behalf of the acquirer, and identifying the destination member state of the goods.

That written statement should state:

- the date of issue;
- the name and address of the acquirer;
- the quantity and nature of the goods;
- the date and place of the arrival of the goods;
- in the case of the supply of means of transport, the identification number of the means of transport;
- the identification of the individual accepting the goods on behalf of the acquirer.

The statement must be provided by the 10th day of the month following the supply.

<u>Acceptable evidence</u>

List A: Documents relating to the dispatch or transport of the goods, such as:

- a signed CMR document or note;
- a bill of lading;
- an airfreight invoice;
- an invoice from the carrier of the goods.

List B: The following documents:

- an insurance policy with regard to the dispatch or transport of the goods or bank documents proving payment for the dispatch or transport of the goods;
- official documents issued by a public authority, such as a notary, confirming the arrival of the goods in the destination member state;
- a receipt issued by a warehouse keeper in the destination member state, confirming the storage of the goods in that member state.

www.gov.uk/government/publications/changes-to-vat-for-intra-eu-chain-transactions-and-zero-rated-goods

There is a useful article about chains and call-off stock, from a UK perspective, by Angela Lang-Horgan in *Taxation* of 27 February 2020. She makes the following points about these new rules:

In a simplified form, businesses should apply the following checklist to establish how their supplies need to be invoiced in a chain transaction scenario:

1) Is there a single transport?

2) Who transports the goods?

3) Have the requirements for zero rating of the IC supply been met?

[She then examines each of these in more detail, before making the following observation.]

Businesses are not obliged to follow the new provision though. According to HMRC, taxpayers can continue to operate on the basis of VAT Notice 725, section 5 (tinyurl.com/vj583ok). However, complying with the new EU rule has a significant advantage: it protects a business's zero rating because it contains a presumption that the goods have been dispatched or transported to another EU member state if the documents required by Art 45a are in the possession of the business. Unless fraud or similar has occurred, it seems unlikely that the presumption will be rebutted by the tax authorities. It should also not be too onerous to follow the new rules. The documents listed in Art 45a are similar to the proofs mentioned in *VAT Notice 725*, section 5.

Taxation, 27 February 2020

4.3.2 HMRC guidance on call-off stock

There was no Statutory Instrument for the call-off quick fix in time for its implementation on 1 January 2020. Instead, it was confirmed in the Budget that the law would be changed in the FA 2020, with retrospective effect to 1 January. There has been no announcement about a transitional period or a "soft landing", which is unsatisfactory: anyone applying "the current law" up to Royal Assent to the Finance Act could be held to be doing the wrong thing.

In December, HMRC published draft guidance on the new rules for call-off stock as they will be applied in the UK:

1. Call-off stock

Call-off stock refers to goods transported by a supplier from a Member State of origin to a Member State of destination. At the time of the transport of goods, the supplier already knows the identity of the person to whom these goods will be supplied (called-off) at a later stage and after they have arrived in the Member State of destination. That person is referred to in this guidance as 'the customer'.

Member States have taken different approaches to how call-off stocks are accounted for and these changes are intended to provide for a common approach.

The current approach normally gives rise to a deemed supply in the Member State of origin and a deemed intra-community acquisition in the Member State of destination by the supplier, followed by a 'domestic' supply to the customer in the Member State of destination when the goods are called-off. This means the supplier has to become VAT registered in the Member State of destination.

The new rules avoid this by allowing the intra-community supply of the goods to be treated as occurring when the goods are supplied to the customer in the destination Member State. This is subject to certain conditions.

There is no obligation on a business to structure transactions so as to meet the conditions and fall within the new rules. Businesses who do not meet the conditions and so do not fall within the new rules should continue with the current VAT accounting mechanisms for EU cross-border transactions.

The UK's current policy approach allows the customer to account for the acquisition when the goods first arrive into the UK and before being called-off. This removes the need for the EU supplier to register for VAT in the UK.

2. Overview

To avoid the need for the supplier to register for VAT in the Member State of destination, Article 17a of Directive 2006/112/EC sets out the new rules which permit the intra-community supply of the goods to be treated as occurring when the goods are called-off and the final supply is made to the customer.

That means that the physical movement of the goods from the Member State of origin to the Member State of destination does not give rise to an intra-community supply. The goods that are held as call-off stock in the

Member State of destination are considered, for VAT purposes, to still be within the scope of VAT in the Member State of origin.

The intra-community supply is when the goods are called off by the customer. At that point, the normal VAT accounting rules for a cross border sale of goods apply, that is the customer accounts for acquisition tax.

Businesses must comply with a number of conditions if they want to take advantage of this simplification. These are set out below.

The rules include situations when call-off stock treatment is deemed to be terminated. Termination of treatment prior to the goods being called off may give rise to a requirement for the supplier to register for VAT in the Member State of destination and to bring the goods to account as an acquisition of own goods.

The force of law conditions in Notice 725 will be modified to apply to call-off stock arrangements. In the meantime, some parts of this guidance have force of law.

3. Force of law amendments

Paragraph 4.4 of Notice 725 is amended as follows:

These two paragraphs, including the, bullets have force of law.

Where goods are removed from the UK under call-off stock arrangements, the time limit for getting valid evidence of removal is 3 months from the time the goods leave the UK.

In all other cases, the time limits for removing the goods and getting valid evidence of removal will begin from the time of supply. For goods removed to another Member State the time limits are as follows:

- 3 months (including supplies of goods involved in groupage or consolidation prior to removal)
- 6 months for supplies of goods involved in processing or incorporation prior to removal.

4. Conditions

In order for the new simplified rules for call-off stock arrangements to apply, certain conditions must be met. The key conditions are that at the time of removal of the goods from the Member State of origin to the Member State of destination by or under the directions of the supplier:

- a call-off stock agreement is in place with the customer;
- the supplier is removing the goods to the Member State of destination with the intention of supplying those goods to the customer there after their arrival in the Member State of destination;
- the supplier does not have a business establishment or other fixed established in the destination member State;
- the customer is VAT registered in the Member State of destination and the supplier knows the customer’s identity and VAT registration number;
- and the supplier records the removal of the goods in the register referred to in the “prescribed records are maintained” section below;

- and the customer's VAT registration number in the Member State of destination is reported on the supplier's EC sales list.

5. Call-off stock agreement

A call-off stock agreement is a contract between a supplier and its customer, which entitles the customer to call the stock off – that is, to take ownership of the goods.

For the purposes of applying the new rules, it is recommended that the contract also provides that:

- the supplier will remove the goods from the Member State of origin to the Member State of destination;
- the goods are to be located in the Member State of destination when they are to be called-off.

A contract that simply provides for the goods to be made available on the demand of the customer but does not set out how that is to be achieved or where the goods are to be stored before they are made available does not provide evidence that the conditions for the new simplified rules are met.

Contracting parties are recommended to have an express provision in the contract to state whether or not it is a contract to which the parties wish Article 17a of Directive 2006/112/EC to apply.

6. Established and business establishment

For the purposes of these rules a business is said to be established if:

- the business is registered in a Member State under similar arrangements to registering at Companies House in the UK;
- the business (whether or not related to the call-off stock arrangements) is conducted from premises through the presence of the means to conduct that business;
- the warehouse where the call-off stock is to be located is owned (or rented) and directly run by the supplier with his own employees.

A VAT registration does not of itself constitute being established or having a fixed establishment.

Ownership of the warehouse which is operated by an independent third party does not of itself constitute being established or having a fixed establishment.

7. Prescribed records are maintained

As a condition of the application of the new simplified rules, the supplier must record in a register (the Call-off Stock Register) the transfer of stock to the Member State of destination under the call-off stock arrangements.

When the goods are physically removed to the Member State of destination, a record must be made of the transfer of the goods. The Call-off stock Register must also be kept up to date, and it must record when goods are called off.

The information that must be contained in the Call-off stock Register is set out in Article 54a of Council Implementing Regulation 282/2011 (the "Implementing Regulation"). The Implementing Regulation is directly

applicable, so no further legislation is required to implement it into UK law – it will apply in the UK from 1 January 2020.

The Implementing Regulation requires the supplier's Call-off Stock Register to record:

a. the Member State of origin and the date of dispatch or transport of the goods;

b. the VAT registration number of the customer in the Member State of destination;

c. the Member State of destination, the VAT registration number of the warehouse keeper, the address of the warehouse at which the goods are stored upon arrival and the date of arrival of the goods in the warehouse;

d. the value, description and quantity of the goods that arrived in the warehouse;

e. the VAT identification number of the taxable person substituting for the customer, where the Substitution Rule conditions are satisfied;

f. the date on which the goods are called-off by the customer in accordance with the conditions for the simplified treatment the taxable amount, description and quantity of the goods so called-off by the customer and the customer's VAT registration number in the Member State of destination;

g. the taxable amount, description and quantity of the goods affected by a relevant event and the date of the relevant event;

h. the value, description and quantity of the returned goods and the date of the return of the goods as referred to as Returned Goods.

The Implementing Regulation requires the customer's Call-off Stock Register to record:

a. the VAT registration number of the supplier of the goods subject to the call-off stock arrangements;

b. the description and quantity of the goods intended for him;

c. the date on which the goods intended for him arrive in the warehouse;

d. the taxable amount, description and quantity of the goods supplied to him and the date on which the customer's intra-community acquisition of the goods is made;

e. the description and quantity of the goods, and the date on which the goods are removed from the warehouse by order of the supplier;

f. the description and quantity of the goods destroyed or missing and the date of destruction, loss or theft of the goods or the date on which the goods were found to be destroyed or missing.

Where the customer is not the warehouse keeper, so will not necessarily have access to all the information, their Call-off stock Register does not need to contain the information referred to in points (c), (e) and (f).

The following sentence has the force of law.

A supplier which dispatches goods from the UK must preserve the records it keeps in the Call-off Stock Register for 6 years.

The following sentence has the force of law.

A customer which calls-off goods in the UK must preserve the records it keeps in the Call-off Stock Register for 6 years.

Contracting parties are recommended to set out in the contract(s) how they intend to fulfil the record keeping requirements, including how the necessary information is to be communicated between the parties.

If you fail to make or retain the required records, you may be liable to a penalty.

8. EC Sales List

When call-off stocks are sent from a Member State of origin to a warehouse or a customer's storage facility in a Member State of destination, this must be recorded in the supplier's EC Sales List.

The information that must be supplied on the EC Sales List is:

- the customer's country code;
- the customer VAT Registration Number;
- the call-off stock indicator.

If there has been a change in the intended customer during a period under the substitution rule. The supplier must record the following information on its EC Sales List for that period:

- the original customer's country code;
- the original customer's VAT Registration Number;
- the new customer's country code;
- the new customer's VAT Registration Number;
- the call-off stock indicator for a change in intended customer.

If call-off stocks are returned to the Member State of origin without being called-off under the rules for returned goods. Then the following information must be recorded in the supplier's EC Sales List for the period in which the goods were returned:

- the customer's country code;
- the customer VAT Registration Number;
- the call-off stock indicator for returned goods.

No values should be entered on an EC Sales list where the entry relates to call-off stocks.

9. Calling-off

The treatment described below applies subject to meeting conditions that:

- the supply is made within 12 months of the arrival of the goods in the Member State of destination;
- there has not been a prior relevant event.

When the goods are called-off by the customer the supplier makes the supply of the goods to the customer for VAT purposes. This supply should be treated as giving rise to the intra-community transaction at that

time. This means that the supplier makes a supply of the goods in the Member State of origin and the customer acquires the goods for VAT purposes in the Member State of destination.

The normal time of supply and VAT accounting rules as set out in Notice 725 will apply.

This includes the requirement to make the normal EC Sales List declaration for such a supply.

In addition, the Call-off Stock Register should be updated to record the call-off of the goods by the customer.

10. Events which trigger an 'acquisition of own goods'

10.1 12-month rule

Stock is permitted to be held in the Member State of destination pending call-off for up to 12 months from arrival into the Member State of destination. For all practical purposes, the date of arrival into the warehouse can be used as that date.

Where stock, for example commodities, is handled on a last-in first-out basis then this can be treated as though first-in, first-out were in operation and the Call-off Stock Register can be maintained on that basis.

If 12 months pass from the date of arrival of the goods in the Member State of destination without the goods being called off by the customer there is deemed to be:

- a supply by the supplier of the goods in the Member State of origin;
- an acquisition by the supplier of the goods in the Member State of destination (an acquisition of own goods).

Any subsequent supply of the goods by the supplier will be in the Member State of destination (businesses should confirm the treatment with the relevant authorities in the Member State in question).

The deemed supply and deemed acquisition occur on the day after the 12-month period ends. The normal time of supply and VAT accounting rules as set out in and Notice 725 will apply.

This includes the requirement to make the normal EC Sales List declaration for such a deemed supply.

10.2 A relevant event

A relevant event is:

a. the supplier no longer intends to supply the goods to the original customer;

b. the supplier intends to supply the goods to the customer in a place other than the Member State of destination;

c. the supplier establishes a business establishment or other fixed establishment in the destination Member State;

d. the customer ceases to be VAT registered in the Member State of destination;

e. the supplier removes the goods from the Member State of destination other than to return them to the Member State of origin;

f. the goods are destroyed, lost or stolen.

Where a relevant event occurs, there is deemed to be:

- a supply by the supplier of the goods in the Member State of origin;
- an acquisition by the supplier of the goods in the Member State of destination (an acquisition of own goods).

Any subsequent supply of the goods by the supplier will be in the Member State of destination (businesses should confirm the treatment with the relevant authorities in the Member State in question).

The normal time of supply and VAT accounting rules as set out in and Notice 725 will apply.

This includes the requirement to make the normal EC Sales List declaration for such a deemed supply and acquisition.

10.3 Substitution rule

The substitution rule permits the supplier to decide not to supply the call-off stock to the original customer but, instead, to supply it to a different customer ('the substitute customer') without triggering an acquisition of own goods by the supplier under the rules for relevant events.

Certain conditions apply:

- the supplier must decide not to supply the goods to the original customer and at the same time decide to supply them to the substitute customer;
- the substitute customer must at that time be registered for VAT in the Member State of destination;
- the supplier must include the substitute customer's VAT registration number in its EC Sales List;
- the supplier must record the intention to supply goods to the substitute customer in the Call-off Stock Register.

The introduction of a substitute customer does not change the application of the 12-month rule which applies to the goods and not to the customer.

The substitution can be in respect of the whole amount of the goods held, or in respect of part of the goods.

Example

A customer's business is taken over by another taxable person. That person may become the substitute customer where the conditions are met.

There are several call-off customers for the same type of goods and the stock when initially sent is allocated appropriately to each customer in the Call-off Stock Register.

However, one customer requests call-off for an amount greater than that recorded in the Call-off Stock Register.

The substitute customer rules will, where the conditions are met, apply to any additional stock that is called off by a substitute customer in these circumstances.

10.4 Returned goods

Call-off stock may be returned to the Member State of origin by the supplier without giving rise to an acquisition of own goods by the supplier under the 12-month rule or the relevant events rule.

This is conditional on:

- the goods being returned to the Member State of origin by or under the direction of the supplier during the 12 month period beginning with their arrival in the Member State of destination;
- the Call-off Stock Register being updated accordingly.

It is not necessary for the goods to be returned to the premises of the supplier as the goods may have been sold to another person in the Member State of origin.

Where this is the UK, as the goods are still considered to be within the scope of UK VAT, any supply to another UK business that involves the goods being transferred back to the UK will simply be a UK domestic supply.

In addition, the return of the goods must be reported on an EC sales list by the supplier.

www.gov.uk/government/publications/changes-to-tax-rules-for-call-off-stock-arrangements-between-member-states

On call-off stock, Angela Lang-Horgan highlights the following as differences between the regime in the UK before and after the change:

The main differences between the call-off stock rules applicable before 1 January 2020 and after 31 December 2019 are as follows.

- *Time limit for removal*. Previously none, now 12 months from the time of arrival of the goods in the stock.
- *Tax point of IC supply and corresponding IC acquisition*. Previously when the goods arrived in the stock, now when the goods are removed from it. Declaration of IC supply in the EC sales list of the country of dispatch needs to follow in parallel.
- *Compliance*. Although at first sight this seems to be insignificant, complying with the stipulated reporting requirements is now a substantive precondition for the new simplification rule to apply.

Note in particular that the supplier must:

- record the removal in the country of dispatch and the customer must record the arrival of goods in the country of arrival ‘as soon as practicable’ after dispatch or arrival in a special national register for call-off stock movements (the particulars of which are listed in the new Art 54a); and
- mention the VAT identification number of the intended acquirer of the goods in their EC sales list when the goods are dispatched, albeit without declaring the value of the goods.

Further, under the new rules a customer can be substituted after the goods have arrived in the stock, although stringent preconditions apply. In addition, it is now finally clarified that a UK VAT-registered supplier can benefit from the simplification as long as they are not also UK established.

Although in principle goods destroyed or stolen before removal from the stock cannot benefit from the simplification and can thus trigger a VAT registration and be subject to VAT, a large majority of the EU VAT Committee (an advisory committee which consists of representatives of the member states and the EU Commission) agrees that up to 5% of the stock value or amount at the time of the loss shall not disapply the simplification.

Taxation, 27 February 2020

HMRC have updated their Notice *The single market* with information about these changes to call-off stock arrangements from 1 January 2020.

Notice 725

4.3.3 Budget announcements

One of the most significant statements in the 11 March Budget was confirmation that from 1 January 2021 postponed accounting will apply to all imports of goods, including from the EU. This means that import VAT will be accounted for on the next VAT return (when it will normally be offset against an input tax claim), rather than paid at the point of entry or accounted for through duty deferment. This means that:

- Businesses that have dealt only with the EU since 1993 will see no change in their VAT cash flow – it will be the same as it was under acquisition accounting;
- Businesses that import goods into the UK from outside the EU will see a significant cash flow advantage – they will no longer have to pay the money to HMRC and claim it back later.

Although this is mainly a timing difference, it is a very significant one – the Budget Red Book shows the effect as government "expenditure" of £3.5 billion in 2020/21, followed by a further deficit of £180 million in 2021/22, with reversing differences of £910 million and £295 million in the following 2 years. Very few figures in the Red Book are anywhere near that size.

The government will carry out a review of the VAT and excise treatment of goods crossing UK borders after the EU exit transition period (through an informal consultation).

Budget Red Book 2.233/1.71

The CIOT has welcomed the government's confirmation at Spring Budget 2020 that 'postponed accounting' for VAT will apply to all imports of goods from 1 January 2021. This means VAT-registered UK importers will account for import VAT as an entry in the VAT return, rather than paying up front at import, or by using a monthly deferral account. Postponed accounting will not apply to customs or excise duty. The government had planned to introduce postponed accounting for VAT in the event of a no-deal Brexit.

CIOT Press Release 11 March 2020

4.3.4 Brexit position

On 27 February 2020, the UK government published a position paper outlining its priorities and approach for negotiations on its future

relationship with the EU. The UK is looking to finalise a Comprehensive Free Trade Agreement with zero tariffs and quotas on goods, based on existing EU models such as Canada, Japan and South Korea. This would be supplemented by a range of other international agreements e.g. on fisheries, nuclear cooperation, law enforcement and judicial cooperation. This would be supported by various technical and other processes for instance on data protection adequacy, financial services equivalence and civil judicial cooperation. Central to the UK position is the rejection of the EU's proposals on level playing field, centralised governance and enforced dynamic alignment with EU rules, regulations and institutions, including the Court of Justice.

Negotiations were supposed to start on 2 March 2020 and were considered to be subject to a tight timetable, with the prospect of an exit without a deal on 31 December 2020 if no agreement could be reached – in practice, there would have to be significant progress by early summer. That process has been derailed by the Coronavirus pandemic, and it remains to be seen where and when it will be picked up again.

On 18 March 2020, the European Commission's UK Task Force (UKTF) published its proposed draft legal text for an 'ambitious and comprehensive' future partnership agreement between the EU and the UK. The draft 'translates into a legal text the negotiating directives approved by Member States in the General Affairs Council on 25 February 2020, in line with the Political Declaration agreed between the EU and the UK in October 2019'.

The UK has been working on its own separate proposals, based on elements of existing precedents in the EU's agreements with Canada, Japan and South Korea. However, the EU proposal goes into far more detail than those agreements, in particular in the imposition of "level playing field" rules that would presumably affect VAT among many other areas of the economy.

https://ec.europa.eu/ireland/news/future-eu-uk-partnership-european-commission-publishes-draft-legal-text_en

4.3.5 Theft from warehouse

A Bulgarian business entered 13 containers of plywood into a customs warehousing procedure on 16 March 2017. One of the containers was stolen on its way to the warehouse, together with the vehicle transporting it. The warehousekeeper was issued with a penalty and an assessment to pay the value of the goods as well. The company appealed, arguing that it was subject to force majeure and could not be held responsible or liable.

The court confirmed that, in accordance with precedent case law, the liability of a warehousekeeper for breaches of customs processes is strict; it depends only on the objective fact that the goods have been removed from supervision, and it not dependent on any standard of conduct of the authorised person.

The Bulgarian authorities argued that requiring a payment of the value of the goods was equivalent to "seizing them and disposing of them for the benefit of the State", given that this was impossible because the goods were missing. The CJEU rejected this analogy: the requirement to pay the value was a penalty, and as such it had to be effective, proportionate and

dissuasive. The court ruled that a penalty of this size was disproportionate, regardless of the fact that it was payable in addition to the administrative penalty for the breach of procedures.

CJEU (Case C-655/18): *Teritorialna direktsiya 'Severna morska' kam Agentsiya Mitnitsi, successor in law to Mitnitsa Varna v Schenker EOOD*

4.3.6 Adequacy of evidence

A UK company bought consumer goods in the UK and sold them through the Chinese equivalent of eBay to middle-class purchasers in China who were concerned about the quality of goods they could purchase locally. The company claimed a repayment of £48,474 in its VAT return for 01/17 on the basis that it was making zero-rated exports, and this triggered an enquiry. During the visit, the company's director explained that the Chinese authorities required purchases of goods from overseas suppliers to be below a certain value, as a result of which the Appellant had incorrectly described and undervalued the goods on the export shipping documents. The director also explained in his witness statement that he "sometimes" entered deliberately vague or even misleading descriptions of the goods on the customs declaration form CN23 "in order to reduce the possibility of theft in transit".

HMRC extended their enquiry and eventually raised assessments for £152,181 for periods from 07/15 to 07/17. The trader appealed to the Tribunal, which noted that the documentary evidence did not link the goods for which input tax was claimed to any particular export sale. Judge Kevin Poole quoted the relevant sections of Notice 703 on direct exports, which have the force of law:

A supply of goods sent to a destination outside the EC is liable to the zero rate as a direct export where you:

- *make sure that the goods are exported from the EC within the specified time limits (see paragraph 3.5)*
- *obtain official or commercial evidence of export as appropriate (see paragraphs 6.2 and 6.3) within the specified time limits*
- *keep supplementary evidence of the export transaction (see paragraph 6.4), and*
- *comply with the law and the conditions of this notice*

Section 6.5 contains the required contents of export evidence, again having the force of law:

The evidence you obtain as proof of export, whether official or commercial, or supporting must clearly identify:

- *the supplier*
- *the consignor (where different from the supplier)*
- *the customer*
- *the goods*
- *an accurate value*
- *the export destination, and*

- *the mode of transport and route of the export movement.*

The company's representative argued that the documents and supporting commercial evidence, taken in the round, were sufficient to satisfy the requirements of the legislation and Notice 703. The judge agreed that there was no requirement for all the mandated information to be included on a single document, but it was simply not possible, on the basis of the evidence before the Tribunal, to link up the various pieces of that evidence in a way which satisfied the requirements of the Notice. As the Upper Tribunal had concluded in the 2013 case *Arkeley Ltd (in liquidation)*, "the evidence of export must read as a whole clearly and correctly identify all the matters specified in paragraph 6.5". In this case, it did not. The appeal was dismissed.

First-Tier Tribunal (TC07520): *A & S Import and Export Trading Ltd*

4.3.7 Article

In an article in *Taxation*, Sam Brodsky examines the VAT treatment of private jets and yachts imported into the Isle of Man. This has been subject to a review by the Treasury after the "Paradise papers" suggested that the local procedures were being used for tax avoidance. The writer describes the local registration processes as "more user friendly" than the UK's, in spite of the theoretical union for VAT purposes between the Isle of Man and the UK.

Taxation, 12 March 2020

4.4 European rules

4.4.1 Report on double taxation

The EU VAT forum sub-group has published a report on prevention and solution of VAT double taxation disputes, which notes that the EU does not currently have a measure for the economic or quantitative impact of VAT double taxation/non-taxation. The only available indicator is the number of cases on related matters that reach the CJEU. While a number of tools are available to businesses and tax authorities to address cross-border VAT disputes, none of them provide a solution for all cases.

The report recommends:

- in the short term, better communication and dialogue between tax authorities and between tax authorities and taxpayers;
- in the medium term, upgrading the existing tools, such as the pilot for EU VAT cross-border rulings and SOLVIT online service; and
- in the long term, explore a comprehensive legal framework for a mechanism involving taxpayers and member states to prevent and/or solve VAT double taxation situations.

The EU VAT forum offers a discussion platform where business and VAT authorities meet to discuss how the implementation of the VAT legislation can be improved in practice.

ec.europa.eu/taxation_customs/sites/taxation/files/01-2020-executive-note-eu-vat_forum.pdf

4.4.2 Speech by Commissioner on EU taxation policy

On 5 March 2020, the European Commissioner Paolo Gentiloni, in his speech on 'Making Tax Work For All', set out his priorities for taxation. These included continuing to address tax fraud, evasion and avoidance, and removing obstacles to facilitate cross-border work, such as reducing double taxation, enhancing cooperation and simplifications to VAT compliance. He had intended to host a high-level conference on 'Making Tax Work – Fighting tax evasion and ensuring Compliance' on 20 April (probably now postponed), and has invited ideas from citizens, businesses, academics, policy makers and politicians. On that basis, the Commission hoped to finalise an Action Plan for June 2020, setting a roadmap of initiatives to make taxation easier for taxpayers and to make life harder for tax cheats.

ec.europa.eu/commission/presscorner/detail/en/speech_20_398

4.4.3 Simplified VAT rules for SMEs

ECOFIN has formally adopted amendments to the VAT directive and administrative cooperation regulation introducing simplified VAT rules for SMEs trading across borders from 1 January 2025.

The Directive has been published in the Official Journal. It amends the PVD as regards the special scheme for small enterprises and Regulation (EU) No 904/2010 as regards the administrative cooperation and exchange of information for the purpose of monitoring the correct application of the special scheme for small enterprises. Member States are required to implement it in their domestic legislation by the effective date. The purpose of the new measures is "to reduce the administrative burden and compliance costs for small enterprises and help create a fiscal environment to facilitate their growth and the development of cross- border trade".

Directive (EU) 2020/285

4.4.4 Payment service providers

ECOFIN has formally adopted VAT directive amendments requiring payment service providers to keep records of cross-border e-commerce transactions, and amendments to the administrative cooperation regulation introducing enhanced sharing of payment information between EU tax administrations and law enforcement bodies to tackle VAT fraud. The new measures will apply from 1 January 2024.

The Directive has been published in the Official Journal. It inserts new articles 243a to 243d in the PVD. Member States must implement it in their own legislation.

Directive (EU) 2020/284

The Commission has published a survey to gather views from businesses in the payments industry on the implementation of these rules.

https://ec.europa.eu/eusurvey/runner/VATPaymentDataSurvey

4.4.5 Administrative cooperation on fraud

A further measure to strengthen administrative cooperation in order to combat VAT fraud has been published in the Official Journal. This is a Council Regulation, to take effect from 1 January 2024, establishing a mechanism for collecting, storing and sharing information about payments for online supplies. The Commission shall develop, maintain, host and technically manage a central electronic system of payment information ("CESOP") for the purpose of investigations into suspected VAT fraud or in order to detect VAT fraud. The Regulation contains rules about how it may be accessed and monitored.

Council Regulation (EU) 2020/283

4.4.6 Action against fraud

The Fiscal Action Unit of the Portuguese National Republican Guard, under the direction of the Central Public Prosecutor's Office, has carried out operation Netto Price, which helped to dismantle an organised crime group (OCG) that obtained illegitimate tax advantages of at least €5m through a scheme based on fraudulent invoices. The OCG issued large numbers of false invoices in order to obtain undue deductions and VAT refunds. The investigation, which lasted for two years, allowed police to identify a network operating in Portugal, Germany, Latvia and the UK. Due to the complexity of the investigation, Europol assisted the Portuguese authorities by providing digital forensic support experts. On the day the operation was closed down, the authorities exercised 108 search warrants in Portugal, 7 in the UK, 6 in Germany and 2 in Latvia.

www.europol.europa.eu/newsroom/news/network-defrauding-least-€5-million-dismantled-in-portugal

Europol supported the National Organised Crime Agency of the Czech Police in a Joint Investigation Team with the Slovak National Criminal Agency in close cooperation with the Czech Financial Intelligence Unit and the Financial Administration of the Czech Republic to arrest 23 people suspected of tax evasion through employment agencies. The joint investigation revealed that the criminals used employment agencies to send foreign workers to manufacturing companies in Czechia. The owners of these agencies created a large group of companies to provide false invoices and evade VAT and income tax. This criminal activity has been ongoing for a considerable length of time and the damage caused exceeds €7.2 million

https://www.europol.europa.eu/newsroom/news/scammers-arrested-after-evading-%E2%82%AC72-million-in-tax

4.4.7 Portuguese rules for medical care

The Advocate-General has considered a case in which a Portuguese commercial company ran five healthcare institutions for profit. It had opted for inclusion in the normal VAT taxation regime, but the Portuguese tax authority decided that it was not entitled to do so, because it had concluded a number of operating agreements with public bodies that brought it within the mandatory exemption of healthcare services. An assessment was raised for over €2m of overclaimed input tax.

The questions for reference noted that:

- more than 54.5% of revenue, including sums invoiced to the relevant user-beneficiaries, comes from State bodies and public health subsystems, at the prices stipulated in the agreements concluded with them;
- more than 69% of users are beneficiaries of public health subsystems or receive services provided within the framework of agreements concluded with State bodies;
- more than 71% of medical services are carried out under agreements concluded with public health subsystems and with State bodies; and
- the activity carried out is of significant general public interest.

There were also questions about the operation of the special rules introduced by Portugal under article 391, allowing an option for taxation.

The Advocate-General observed that it is the nature of the services and the conditions under which they are provided that determines whether they are exempt within art.132(1)(b) PVD. This means that individual services are exempt or not; it is not relevant to consider what proportion of services provided by the entity as a whole are covered by the particular conditions. He recognised that this conclusion, which would make the business partially exempt, would impose an administrative burden in having to decide which supplies were exempt and which were taxable, but he considered that to be the correct answer.

The company argued that the question of whether its supplies were made "under social conditions comparable to those applicable to bodies governed by public law" was something that the Portuguese court should determine, and was not admissible in the CJEU. However, the A-G considered that it was a proper question and guidance should be given: in his view, where an entity provides medical services under a health insurance scheme which is compulsory or is one of the alternative insurance schemes from which the insured person is obliged to choose, and this scheme is intended to satisfy basic medical care needs, there is a significant probability that such services would fall within the exemption.

The A-G also noted that art.133 allows, but does not require, Member States to impose conditions relating to non-profit status on some of the exemptions, including art.132(1)(b). Portugal had not done so, so that provision was not relevant.

The remaining questions concerned the rarely visited rule in art.377 which allows some Member States (including Portugal) to exempt some hospital care that would not be exempt under art.132(1)(b), and the related rule in art.391 that then allows taxpayers to opt to tax such supplies for a period of five years. The A-G pointed out that the option in art.391 only applied to transactions that were exempt because of art.377 – not to supplies that were mandatorily exempt under art.132. The principles of legitimate expectations, fiscal neutrality, equality and non-discrimination did not affect this conclusion. The taxpayer could not insist on its transactions being taxable if they were properly exempt within art.132(1)(b).

CJEU (A-G) (Case C-211/18): *Idealmed III – Serviços de Saúde SA v Autoridade Tributária e Aduaneira*

4.5 Foreign refund reclaims

Nothing to report.

5. INPUTS

5.1 Economic activity

5.1.1 Investment activity

The FTT has considered the unusual situation of an "old-fashioned" English limited partnership, which is a business structure that predated the creation of LLPs. A limited partnership is not treated as a body corporate, whereas a LLP is one; it may have a number of limited partners who are not liable for all the debts of the firm, but it must have at least one general partner with unlimited liability. In this case, the general partner was itself a limited company, which is permissible – the debts of the limited partnership could make the general partner insolvent, but could not (in normal circumstances) then be collected from the shareholders of the general partner. For VAT purposes, only the general partner is treated as carrying on the business, and is therefore registered as a sole trader (see Notice 742A para.7.4).

The appellant was the general partner of MSSLP, an investment fund. It held (on behalf of the fund) shares in an Isle of Man company, HPH. HPH in turn held shares in a number of companies or special purpose vehicles, each of which held an underlying asset such as a commercial property. Some of the SPVs received taxable income in the form of opted rent.

The appellant was in its turn owned by MCP, a LLP. The LLP was contracted to provide advisory, property management and administrative services (all standard rated) to the fund; these services were provided under contract directly to each of the SPVs in return for fees payable directly by the SPV to the LLP.

The appeal concerned inputs incurred by the general partner in:

- setting up the fund and attracting investors;
- operating the fund including audit costs, overheads and due diligence for making new investments.

The appellant was registered as a VAT group with the LLP; HPH and the SPVs formed a separate VAT group.

HMRC issued a decision in 2015 (confirmed on review) that the appellant was not entitled to recover input tax on either the set-up or the operating costs. The company appealed.

It was agreed that the appellant VAT group made no exempt supplies. The appellant argued that:

(1) the activities of the Fund should be treated as the activities of its general partner, i.e. the appellant;

(2) the activities of the appellant as general partner, including those of the fund and those of the LLP should be treated as activities of a single entity for VAT purposes, namely the group; and

(3) the group actively managed its investment in the SPVs and made only taxable supplies, so it should be entitled to full recovery of its input tax.

As all the activities of a VAT group are regarded as activities of a single entity, the company argued that it should not be treated separately as "the LLP providing taxable services" and "the general partner holding investments", but as a single entity that both provided taxable services and held investments. With no separate activity of holding investments, and no exempt supplies, there should be no input tax restriction.

HMRC argued that the proper analysis was to consider the link between costs and economic activities. In their view, the split in the group's activities meant that input tax recovery should be restricted. The group provided finance to HPH and the SPVs for no taxable consideration, and that was a non-economic activity.

In HMRC's view:

- VAT on overheads was in principle recoverable, but had to be apportioned between economic and non-economic activities;
- VAT on purely investment activities such as setting up and dissolving the fund and attracting investment were not recoverable at all, because they were linked only to the non-economic activity.

HMRC countered the argument that the appellant managed the investments by pointing out that HPH had that role – the appellant was a shareholder in HPH, but HPH was in the position of holding company actively managing its subsidiaries.

Among the many precedents cited, HMRC referred to the opinion of the A-G in Case C-85/11 *Commission v Ireland*:

"The forming of a VAT group results in the creation of a single taxable person for VAT purposes which is in all aspects comparable to a taxable person consisting of only one entity. Regardless of its nature as a special scheme, VAT grouping neither introduces limitations nor broadens the rights of a taxable person as defined in Article 9 of the VAT Directive… The establishment of a VAT group initiates the tax liability of the VAT group, and terminates the separate tax liability of those of its members who were taxable persons for VAT purposes before joining the group. The VAT treatment of the group's transactions, both to and from entities outside the group, is comparable to VAT treatment of a single taxable person operating individually. Transactions between the individual members of the group, and which remain therefore within the group, are considered as having been carried out by the group for itself. Consequently, a VAT group's internal transactions do not exist for VAT purposes. When a VAT group acts in accordance with the rules of the VAT regime, the right of the persons belonging to the VAT group to deduct VAT for purchases is not expanded. This right continues to be applicable only to those supplies that are made for the activities subject to VAT by the VAT group. Nor are the members of the VAT group entitled to deduct VAT on supplies made for VAT exempted activities."

The judge (Rachel Mainwaring-Taylor) set out the arguments of the parties at length, but her discussion is very brief. Her summation of the principles of holding company input tax deduction is succinct and unhelpful to HMRC – in effect, she has completely rejected their traditional line on the matter.

66. The VAT rules around holding companies' costs are the subject of a body of case law. It is established that the mere acquisition and holding of shares in other companies does not amount to a business activity (see Polysar) but the provision of management services to subsidiaries may do (see Cibo) if such services are provided for consideration.

67. The mere holding of shares does not constitute economic activity (Polysar).

68. The exploitation of tangible or intangible property for the purpose of obtaining an income therefrom on an ongoing basis is regarded as an economic activity (Article 9(1)).

69. The provision of management services for consideration to subsidiaries constitutes economic activity (Cibo).

70. The Appellant does not carry out either of the above activities directly itself.

71. The SPVs may be exploiting tangible property for the purpose of obtaining an income but their actions are not attributed to the Appellant as they are in a separate VAT group.

72. The LLP provides investment and administrative services to the Appellant as general partner of the Fund but these are disregarded for VAT purposes as intra-group supplies.

73. The LLP provides management services to HPH and the SPVs via an agreement with the Appellant, supplemented by tripartite DOAs between the LLP, the Appellant and each of HPH and the SPVs. Consideration is payable by the SPVs and HPH under the DOAs.

74. Supplies made by the LLP are deemed to be made by the Appellant as the representative member of the Group.

75. For the purposes of the VAT rules, due to the existence of the Group, the Appellant is engaged in an economic activity (the provision of management services to its subsidiaries) and makes taxable supplies in the form of these services.

76. Costs incurred by the Appellant, or deemed to be incurred by the Appellant as representative member of the Group, in the course of the furtherance of this business are therefore recoverable as input tax.

77. Are the costs in question incurred for the purpose of the business carried on by the Appellant? The economic activity in this case is the provision of management services for consideration. It does not seem to me that the Appellant carries out a separate investment business, distinct from its activities as active holding company for HPH and the SPVs; its activities (and that of the Fund on behalf of which it acts) are acting as holding company and it provides management services for consideration to all of its subsidiaries. The Set-up Costs are incurred for the purpose of subscribing for shares in or providing loans to HPH and the SPVs with the intention of providing the advisory services to them. On this basis, there appears to be a direct and immediate link between the Set-up Costs and the economic activity carried out.

78. It is accepted by HMRC that the Operating Costs are recoverable as input tax to the extent that they relate to the economic activity undertaken. Since the Tribunal has not found that separate economic and non-

economic activities are undertaken here it must follow that these costs are recoverable in full.

The appeal was allowed in full.

First-Tier Tribunal (TC07514): *Melford Capital General Partner Ltd*

5.2 Who receives the supply?

5.2.1 Holding company and subsidiary

A company, AIS, held the shares in a subsidiary, HFIM, which provided regulated investment services. The same person was the director of both companies. There was a management agreement in place, stating that AIS supplied management services to HFIM; HMRC argued that as Mr Patel was a director of both AIS and HFIM, any services which he provided to HFIM were in his capacity as a director of HFIM and so were not provided by AIS. This conflicted with the Management Agreement and so effectively amounted to an argument that the Management Agreement did not govern the relationship between AIS and HFIM.

On the basis that AIS was not carrying on any taxable business, HMRC raised assessments to deny AIS's input tax claims from 09/13 to 09/16, amounting to £21,637; they also denied a repayment claim of £2,400 for 12/16, and issued a decision to cancel the company's registration with effect from 30 June 2017. A "careless behaviour" penalty was charged in November 2017 amounting to £4,868.

The judge (Judge Richard Chapman) rejected the argument that the management agreement did not govern the relationship between the companies. The fact that the same person was a director of both AIS and HFIM meant that he owed duties to both AIS and HFIM. However, this did not define the work which he was doing or which company he was doing it for. He said that his work for HFIM was as a result of his service contract with AIS and there was no evidence to contradict that.

The problem was that HFIM had become involved in litigation in the Seychelles which resulted in operations being effectively suspended from 2011 to 2017. HMRC relied on various e-mails and other documents to submit that during this period, AIS did not provide any services to HFIM. Again, on the basis of the director's witness evidence, the judge rejected this argument. There was no dispute that HFIM was trading, at least for the purposes of dealing with its litigation and continuing to comply with regulatory obligations; on the balance of probabilities, the director was acting on behalf of AIS in carrying out work for HFIM.

The input tax all related to accommodation costs. From 08/13 to 12/16, the invoices were all issued to HFIM. The director claimed that this was an administrative mistake, and produced a letter from the licensor to confirm this. The judge accepted this as evidence that the invoices should have been addressed to both companies. The rent was paid by both companies from time to time; the director stated that, when HFIM paid it, it was on behalf of AIS, and this was accounted for in the books of the two companies.

The reasons for HMRC's decisions were "not a picture of clarity", but were summarised by the judge as:

(1) The accommodation costs did not relate to a supply to AIS or paid for by AIS.

(2) The accommodation costs were not invoiced to AIS and there was insufficient alternative evidence to allow the input tax.

(3) AIS did not make (and did not intend to make) any taxable supplies.

The judge concluded that HMRC had taken a decision not to accept alternative evidence to support a deduction in the absence of "proper" VAT invoices held by the claimant, under SI 1995/2518 reg.29.

The judge referred to the precedent of *Airtours* for the principles of identification of the recipient of a supply in a tripartite situation. The recipient of the supply is to be identified by reference to the contractual documentation unless this does not reflect the economic reality. The circumstances in which a contract does not reflect the economic reality of a transaction are not restricted to situations of artificiality or sham (FTT decision in *American Express Services Europe Ltd*, also citing the CJEU judgment in *Newey*). The judge found as a fact that the accommodation was supplied to both AIS and HFIM, both as a matter of contract and commercial reality. However, this was not sufficient on its own for the appeal to succeed as HMRC refused to accept AIS's evidence of the supplies.

The precedent of *Scandico* showed that a decision on alternative evidence had to be judged on the evidence that was provided to HMRC at the time the decision was made, not evidence provided later. The test was whether the decision was reasonable or unreasonable, rather than whether the Tribunal would have come to a different decision. At the time the decision was taken:

- the only invoices shown to HMRC were made out to HFIM;
- the payments shown to HMRC had been made by HFIM;
- the only evidence of inter-company accounting was an assertion by the director;
- a licence agreement provided to HMRC conflicted with the invoices and payments, and only related to part of the period.

The judge therefore concluded that the decision had been a reasonable one.

In deciding whether the decision to cancel the registration was correct, the judge accepted the director's evidence that genuine management supplies were provided, even while the level of HFIM's activities was greatly reduced. There was genuine consideration in the form of inter-company accounting. There was also an intention to make further taxable supplies in the future. The judge also noted that HMRC did not explain why the cancellation took effect from 30 June 2017. There was no suggestion that this was a date agreed between the parties and on HMRC's own case the cessation of business was long before 30 June 2017. The appeal against the decision to cancel registration was allowed, but this was of no assistance in the appeal against disallowance of the input tax.

Turning to the penalty, this was calculated on the "careless, prompted" scale with only 50% mitigation of the maximum for quality of disclosure. The penalty explanation letter said the following:

Telling: The inaccuracies were not disclosed at the start of the compliance check, and you did not tell us everything about the extent of the inaccuracies as soon as you could.

Helping: Several requests had to be made to obtain all of the relevant information from you, because you did not answer my questions in full at the outset.

Giving: Relevant information was only given in response to specific, detailed request. You did not respond to all of my requests for information on time.

The director's only defence against the penalty was to argue that there had been no error in the returns. He did not put forward any reasonable excuse or special circumstances. The judge saw no reason to disturb the penalty. As the assessments had been held to be correct, the potential lost revenue was established; it was clear that the disclosure was "prompted"; and the judge agreed with HMRC's assessment of the taxpayer's level of cooperation.

The appeal was allowed only in respect of the registration decision.

First-Tier Tribunal (TC07525): *Alternative Investment Strategies Ltd*

5.3 Partial exemption

5.3.1 Special methods and supplies "outside EU"

The *Value Added Tax (Miscellaneous Amendments, Revocation and Transitional Provisions) (EU Exit) Regulations 2019 (Appointed Day No 1) (EU Exit) Regulations 2020* make technical amendments to ensure that partial exemption methods that give credit for input tax attributed to supplies to non-EU customers do not apply to customers in the UK (which is, of course, now "non-EU").

SI 2020/513

5.4 Cars

Nothing to report.

5.5 Business entertainment

5.5.1 Blocking order: input tax on food

A company provided "support services" to companies in order to promote their products and their brands. It produces films, videos and television programmes for which it acquires goods and services of various kinds. These include catering services to meet the food needs of participants in

the programmes and promotional films. Third party caterers invoice the company, which charges the cost on to its clients; the invoices describe the supply as a single "film production/filming service", which includes the catering as an unspecified cost.

The company appears to have made an additional reclaim for input tax on these catering expenses; this led to a tax audit, whereupon the tax authority in Portugal concluded that it had incorrectly deducted input tax on what it regarded as blocked "entertaining" expenditure. An assessment was raised with interest.

The company appealed, and the Portuguese court referred questions on the application of art.168 and art.176 PVD to this situation. The court recited the usual precedents on the absolute right of a trader to deduct input tax on all the cost components of taxable output supplies, and the restriction on a Member State's power to restrict deductions: derogations from the right to deduct VAT are only permitted in the cases expressly provided for by the provisions of the VAT Directives. One such derogation is in art.176(2), which contains a standstill clause allowing the retention of input tax blocks that were in force at the time of the country's accession.

The court stated that the referring court was responsible for determining exactly what the Portuguese law blocked in 1986 on accession, or in 1989 when the Directive took full effect, and also to consider an amendment in 2005 which appeared to allow 50% of input tax incurred on food in certain circumstances. The referring court should also determine whether the category of expenditure on which input tax was blocked could be identified with sufficient certainty; if not, the provision would be too general in scope and could not be given effect.

The court's judgment was that art.176 did appear to authorise the block in this case. The fact that the cost was incurred in the course of making taxable supplies was irrelevant: it was the point of art.176 that it allowed blocking of input tax that would otherwise be allowed. The amendment in 2005 did not wholly invalidate the block, and the category of expenditure appeared to be identifiable with sufficient certainty.

CJEU (Case C-630/19): *PAGE International Lda v Autoridade Tributária e Aduaneira*

5.6 Non-business use of supplies

5.6.1 No connection to business

An individual appealed against the disallowance of input tax on legal fees incurred in quarters 06/17 to 12/17 in relation to a dispute over a freezing order imposed on his assets by HMRC following the issue of personal liability notices for £8.7m in July 2015. These in turn related to the individual's alleged involvement in companies based outside the EU that had been issued with civil evasion penalties for failing to account properly for import VAT on goods imported into the UK. The PLNs were the subject of separate appeals. In the meantime, the freezing orders and penalties have been increased, so that the prohibition on moving the appellant's assets stood at £22.75m from August 2018.

The individual was registered for VAT as a sole trader in relation to a property holding business with opted rental income. He said that he also provided consultancy services through the sole trade, but no output tax invoices were raised in the relevant period for that activity because of the time spent on the PLN litigation.

The Tribunal accepted that the freezing orders had an impact on his sole trade, even though they did not prevent him continuing to collect rent. He had to abort the purchase of two properties in August 2015 because the freezing order did not allow him to enter the necessary arrangements.

The trader relied on the recent Court of Appeal decision in *Praesto Consulting* as support for the deduction. Looked at "in the round", the restrictions imposed by the freezing orders provided the necessary link between the sole trade and the legal costs. Alternatively, they should be regarded as overheads incurred in attempting to make more capital available for the business, as in *Kretztechnik*.

The Tribunal was not persuaded. The legal costs were incurred purely in attempting to show that there was no link between the appellant and the companies that were the subject of the evasion penalties. The purpose of the legal fees was not in order to allow him to continue to rent the properties that he owns or to invest in more rental properties. There was no nexus with what the sole proprietorship continued to invoice, to adopt the terminology used in *Rosner*. The legal supplies to the appellant and the economic reality of the sole proprietorship illustrated that the advice was in respect of the alleged activities of others, as opposed to those of the sole proprietorship.

The appeal was dismissed.

First-Tier Tribunal (TC07621): *Parul Keshavlal Malde*

5.7 Bad debt relief

Nothing to report.

5.8 Other input tax problems

5.8.1 MTIC decision: mobile phones

A long-running dispute, which proceeded through the lower levels to the Court of Appeal in late 2016, returned to the FTT in 2018 for directions and has now been heard again by the Upper Tribunal, still arguing about procedural matters rather than the substantive evidence.

The company was denied input tax in relation to purchases of mobile phones and denied zero rating on the sale of mobile phones. HMRC alleged that the invoices purporting to support the purchase did not comply with reg.14, because they did not adequately describe the goods: they had evidence that there were not enough of these phones available on the market at that time to fulfil these transactions, so the invoices could

not be accurate. If they could prove that on the balance of probabilities, it would not be necessary to allege fraud, knowledge or means of knowledge. HMRC also alleged that the transport documents supporting the supposed despatches to other member states were unreliable, partly because they were issued by a company that was involved in a number of other frauds. Once again, they argued that they did not need to show bad faith by the company, only that the documentation did not satisfy the statutory requirements.

A dispute followed about the admissibility of some of HMRC's evidence, in particular witness statements from two officers. The company claimed that these witness statements implied that the company was involved in a fraud; if HMRC wished to allege that, it should plead it fully with evidence, and if it did not wish to do so, it should not make prejudicial statements of this kind. The First-Tier and Upper Tribunals agreed that the witness statements should be struck out, at least to the extent that they referred to fraud.

The Court of Appeal agreed with the earlier Tribunals in relation to the input tax side, where the witness statement did no more than refer to criminal convictions of certain employees of counterparties. The judge could not see its relevance to a dispute about the invoices. However, he considered that the statement about the despatches (with some passages excised) was relevant to the reliability of the documentation, and should therefore be considered by the Tribunal.

He described his judgment as "taking the short route": rather than considering very detailed arguments of the two counsel about the rightness or wrongness of the principles of the Upper Tribunal judge's conclusion, he considered that it would be appropriate for the case to proceed to a full hearing where the evidence could be tested. Underhill LJ and Arden LJ agreed.

The case came before Judge Tony Beare in April 2018 for directions (TC06481). He accepted an application from the appellants to bar HMRC from taking further part in the proceedings in relation to the input tax matter, and summarily allowed that appeal. However, he refused a similar application in relation to the despatch side, and made a number of directions about the provision of arguments and evidence for a substantive hearing.

In relation to the input tax dispute, the judge considered that he was bound to follow the principles of the CJEU decisions in *Mahageben* (Case C-80/11), *David* (Case C-142/11) and *Stroy Trans EOOD* (Case C-642/11). These cases showed that a trader could not be denied a deduction on the mere grounds that the supply did not take place; the trader should have either known or had the means of knowing that this was so. If HMRC were not prepared to argue that, it would deprive the CJEU decisions of meaning. HMRC could not rely on a string of domestic precedents that indicated the contrary conclusion, because the CJEU had primacy.

The judge noted that the CA had expressed the view that the facts should be established by a substantive hearing, rather than by the appellant applying for a barring order of this type. The appellant had chosen not to follow that course, but even so, the case law led the judge to the inevitable conclusion that HMRC stood no reasonable prospect of success on the basis of the case they were prepared to put forward.

Turning to the export issue, the judge noted that both sides wished to rely on *Teleos* (Case C-409/04), but did not agree on the principle it established. The appellant argued that it was simply an application of *Kittel*, but HMRC argued that it was subtly different. It was a two-limbed test, requiring the First-tier Tribunal to conclude both that the supplier acted in good faith and that the supplier has taken every reasonable measure in its power to ensure that the supply it was effecting did not lead to its participation in the relevant fraud.

The FTT judge appeared to accept HMRC's argument. The claim that the appellant had not taken every reasonable step did not amount to an allegation of dishonesty, and was a separate test. It could not be determined without a full hearing at which the evidence would be examined to determine whether the appellant had satisfied these obligations, and whether the goods were actually exported.

HMRC appealed against the FTT decision to summarily dismiss their case on the input tax side. The company cross-appealed the other part of the FTT decision. The case came before The Hon. Mr Justice Marcus Smith and Judge Thomas Scott in the Upper Tribunal, sitting in July 2019, and the decision was released on 30 December.

In relation to the input tax appeal, the company raised a preliminary objection that HMRC had changed their argument: they had introduced an assertion that no supply had taken place, when previously they had only asserted that the invoices did not comply with the regulations. The Upper Tribunal rejected this objection. HMRC had from the outset made it clear that they did not believe that the telephones described in the invoices had been supplied. The FTT had made an error of law in concluding that the existence of the goods was irrelevant if the claimant had no actual or constructive knowledge of the fraud; that error of law led to permission being granted for an appeal.

The UT did not agree with the FTT's interpretation of the decisions in *Mahageben* and *Stroy Trans*. The judges were satisfied that there was no right to deduct based only on paperwork; there must have been a supply. There were also later decisions of the CJEU that were relevant (Case C-459/17 *SGI and Valeriane SNC* and Case C-712/17 *EN.SA Srl*) and which post-dated the FTT decision. Both of these cases made it clear that the good or bad faith of a claimant was irrelevant if there had not been a supply: there was no right to deduct in respect of fictitious transactions.

The FTT had relied on a statement in *Mahageben* that "the right to deduct can be refused only where it can be established, on the basis of objective evidence, that the taxable person concerned knew, or ought to have known, that the transaction relied 35 on as a basis for the right to deduct was connected with fraud committed by the issuer of the invoice or by another trader acting earlier in the chain of supply." The Upper Tribunal agreed that this appeared to lead to the FTT's conclusion, but suggested that it had to be read in its context. In that case, there was no question that the supplies had taken place; the only question was whether the claimant knew or ought to have known that there was a fraud further up the supply chain. The *Stroy Trans* decision was similar, in similar circumstances, as emphasised by the CJEU in the *SGI* decision.

For these reasons, HMRC's appeal in relation to the input tax dispute was allowed.

Turning to the zero-rating dispute, the Upper Tribunal summarised the company's contentions as relating to the burden of proof. If the tests in *Teleos* were the same as those in *Kittel*, it would be for HMRC to prove that the company should have known that the documents were fraudulent. As HMRC had not pleaded actual or constructive knowledge of fraud, their case had no reasonable prospect of success.

The Upper Tribunal summarised the FTT's decision on this issue as involving an acceptance of the basic argument that *Teleos* was merely an interpretation of *Kittel*, but nevertheless concluding that HMRC might satisfy the burden of proof in a substantive hearing. The UT disagreed with this: *Teleos* was not the same as *Kittel*, and the burden of proof under *Teleos* falls on the company, not on the tax authority. If the FTT had not fallen into this error, the UT would still have agreed with the conclusion; however, it dismissed the company's appeal on the grounds that the FTT had come to the right answer for the wrong reason.

The judge summed up the difference between the cases as follows:

'We do not consider that *Kittel* and *Teleos* can be equated. *Kittel*, as we have described, is relevant where the existence of a supply has been established, such that the right to deduct input tax on the part of the supplier exists, but where, nevertheless, in view of the supplier's actual or constructive knowledge of a fraud on the revenue authority, it is appropriate that the right to deduct input tax be removed. Since this is, in effect, a derogation from the taxpayer's entitlement, it is easy to see why the burden of proof must rest on the taxing authority.

'By contrast, where an entitlement to zero-rate does not strictly exist because, by reference to the objective circumstances, supplies did not leave the Member State of origin for another Member State, one can see a strong case for saying that the tax underpaid should be paid, whatever the supplier's understanding. That was recognised by both the Advocate General and the CJEU in *Teleos*. However, both the Advocate General and the CJEU considered that the strict legal position should be subject to what we call a defence, where the supplier can demonstrate that the supplier took "every reasonable measure in his power to ensure that the intra-Community supply he was effecting did not lead to his participation in such evasion".

'We consider that it is an essential part of the CJEU's reasoning that the burden of proof rests on the supplier in this regard, and that this is an essential difference between *Kittel* and *Teleos*.'

HMRC's appeal was allowed, and the company's appeal was dismissed. Maybe one day this case will proceed to a substantive hearing.

Upper Tribunal: *Infinity Distribution Ltd (in administration) v HMRC*

5.8.2 Missing trader decision: cars

A LLP appealed against seven decisions, one denying input tax of £876,000 on *Kittel* grounds and six denying zero-rating of sales on *Mecsek* principles. The denial of input tax related to 66 transactions between 11/13 and 08/14, and the output tax decisions related to about £450,000 on 54 transactions in the same period. The company was involved in buying and exporting high value cars.

The business commenced in 2010 as a limited company, and was transferred to a LLP in early 2013. It grew very quickly to have turnover of over £10 million. Several visits were carried out, and several returns subjected to extended verification. The judge reviewed the investigations that continued up to the issue of the assessments in 2015 and 2016, before setting out in detail the relevant legislation and CJEU precedents. The issues before the Tribunal were:

(1) was there a tax loss;

(2) if so, did the tax loss result from fraudulent evasion;

(3) if so, were M&M's transactions which were the subject of appeal connected with that fraudulent evasion;

(4) if so, did M&M know or should it have known that its transactions were so connected, and, in respect of the *Mecsek* decisions, did M&M take every reasonable step within its power to prevent its own participation in that fraud.

The burden of proof rested with HMRC, and the standard of proof was the balance of probabilities.

By the time of the hearing, the appellant had accepted that there was a tax loss in each of the transaction chains, but was unable to confirm that the losses arose from fraud rather than from some other reason.

HMRC invited the judge to draw adverse inferences from the appellant's failure to call any witnesses from its counterparties. The appellant's representative responded that HMRC had also declined to bring forward witnesses who had dealt with the business in its earlier period (when it appears that no significant problems were found). The judge agreed that it might be appropriate to draw adverse inferences against the trader, subject to strict conditions, but accepted HMRC's reasons for not bringing the earlier witnesses.

The Tribunal examined the evidence in relation to all of the counterparties involved in the relevant transactions, and concluded that, in each case, they were involved in fraudulent evasion. The judge expressed reservations about a few detailed matters, but concluded that HMRC had satisfied the balance of probabilities on the overall conclusion in each case.

Before examining "means of knowledge" and the conduct of the trader in relation to export sales, the judge considered a general complaint from the appellant about HMRC's conduct in the contacts maintained in the period leading up to the disputed transactions. The trader argued that HMRC should have given them more explicit warnings about particular counterparties, or could have done more to prevent the counterparties from carrying out VAT fraud. The judge considered that he had no jurisdiction to consider HMRC's conduct; he could only consider the evidence of whether the trader knew or ought to have known of the connection with fraud.

However, a fourth claim in this area did carry some weight: that HMRC had provided the LLP with a template to use when carrying out due diligence. This would be considered as part of the examination of whether the trader "knew or ought to have known", as it related to the adequacy of its own procedures.

The judge also considered the credibility of the appellant's main witness at length. Given that he had been arrested and interviewed under caution in 2009 in relation to VAT fraud (although no charges were brought), the judge did not consider it plausible that he repeatedly denied being aware of the existence of VAT fraud in the motor trade before the first VAT visit in 2011.

After detailed consideration of the due diligence carried out, the judge concluded that it was inadequate. The LLP was simply going through the motions of obtaining a narrow range of information and were not applying any critical thought to the information that was then received; factors which the appellant submitted supported this level of due diligence (namely trust in its counterparties and approval from HMRC) did not in fact do so.

After just under 500 paragraphs of detailed examination, the judge came to the conclusion that all of HMRC's decisions were justified. On the balance of probabilities, the director not only had the means of knowing, but actually knew that he was not operating in a genuine commercial market. The appeals were dismissed.

The decision concluded with an award of costs to HMRC. As some of the appeals had been opted out of the costs regime by the taxpayer, the award of costs related only to 6.88% of the amount under appeal. HMRC were invited to apply for costs on this basis.

First-Tier Tribunal (TC07601): *M&M (Cambridge) LLP*

5.8.3 *Kittel* attack rejected

In TC06412, the appellant applied for a decision summarily allowing part of its appeal on the basis that the officer's assessment could not be to best judgement because the officer had not formed the necessary view that the counterparty's defaults were fraudulent, and HMRC had not produced sufficient evidence to show that they were. The application for a summary decision came before Judge Mosedale, who considered the arguments in detail and refused the application. She also refused most of the company's application for further disclosure of documents by HMRC, but allowed one small part of the application. She issued directions for the case to proceed towards a full hearing.

That substantive hearing finally took place in October 2019 before Judge Sarah Allatt. The total amount of input tax denied was £597,172 in relation to 389 transactions in scrap metal purchased from two different suppliers (one supplied 383 times, the other just 6) in 07/13 to 01/14. In that period there were a total of 8,084 purchases with total input tax of £21,339,520.

The business was established in 1976 and still owned by the founder. It employed over 200 people. It dealt with around 3,000 suppliers and customers; terms were agreed on individual transactions rather than on the basis of ongoing contracts.

The company appealed on the grounds that the decision was not competent or made to best judgement; HMRC had not proved fraud by the counterparties; and in the case of the 6 transactions bought from one supplier, there was no link between the appellant and the alleged fraudulent supplier, which was two steps up the supply chain. Overall, the

appellant neither knew nor had the means of knowing of any connection with fraud.

The judge commented on the witness evidence of the HMRC officer who had carried out much of the investigation into the appellant. She highlighted contradictions and inconsistencies; many of his assertions were inaccurate or irrelevant. By contrast, an officer who gave evidence about the main counterparty was said to be "straightforward and truthful". The directors of the counterparty had been subject to disqualification or imprisonment in 2016. They had run a succession of "phoenix" companies that went into liquidation without paying HMRC, including the one that traded with the appellant. A third officer, who investigated the company at the end of the transaction chain for the 6 purchases, was described as "honest but defensive".

The Tribunal also heard evidence from the chief finance officer of the appellant, who was clear and impressive, as well as the owner and the man in charge of the ferrous metal division. They explained how the business operated and what due diligence was carried out. The finance officer explained that she understood MTIC fraud, but that HMRC had never raised the issue of phoenix companies in meetings with the company.

The judge considered that HMRC had not provided any evidence that the company at the end of the transaction chain was a fraudulent defaulter. It had been deregistered because of HMRC suspicions that it might be involved in fraud, but there was no direct evidence. Even so, in case there was a connection with fraud somewhere in that chain, the Tribunal considered evidence of a connection between the 6 deals and the company up the chain. HMRC had found similar weights and types of metal being sold by the defaulter to the intermediary, but the Tribunal noted that the purchases by the appellant were some weeks later. Although the similarity in quantities was persuasive of a link, the judge considered that the timing was more persuasive – particularly as there had been a much faster turnaround at other times. The Tribunal decided that the transactions were not linked.

Turning to the other counterparty, the Tribunal was satisfied that it did carry out an intentional default; even though that took place after many of the transactions in dispute, it satisfied the first of the *Kittel* tests. The judge summarised HMRC's argument as an attempt to show that the appellant carried out weaker due diligence on these two counterparties than on other transactions, and an attempt to show that the appellant knew about the history of defaults by the owners of the counterparty. HMRC had failed to make out either of these cases. That meant that they had not succeeded in showing actual knowledge.

Turning to "means of knowledge", the judge considered competing criticisms by HMRC and justifications by the appellant of the due diligence that was carried out. It is an interesting balancing exercise; it also includes a review of the procedures that the company had introduced to try to prevent fraud, for example requesting photo ID from traders selling lead, long before it became a legal requirement. The totality of the evidence pointed to a company that did its best, engaged with the process and HMRC officers, and went about its ordinary course of business. Even had the due diligence been more thorough, it would not have revealed

anything that would have indicated a fraud. The most that would have been revealed would have been businesses operating with commercial uncertainty. However, due to the history that the appellant had in dealing with either the specific business, or knowing that the individual behind the business has long-standing in the industry, this would not have been a significant indicator of fraud.

The first two grounds of appeal were considered only briefly, but were decided in HMRC's favour. It was clear that the assessments were raised on the basis of HMRC's belief that the returns were inaccurate, and that was all that was required for them to be "competent" within s.73. Although the decision letter which set out the reasons for the assessment contained – putting it in the best possible light – a number of exaggerations by the officer concerned, this did not mean that the assessment was not to best judgement. It did not rely on factors that were irrelevant.

Accordingly, the appeal was allowed on the basis that HMRC had failed to prove that the company knew, or ought to have known, of a connection with a fraudulent tax loss. "To RHJ Ltd these transactions were in the ordinary course of its business, there was nothing in the transactions themselves that were suspicious. RHJ Ltd did not have the means of knowledge to uncover the history of the Cooper family businesses and further due diligence would not have revealed conclusive indicators of fraud."

First-Tier Tribunal (TC07571): *Ronald Hull Junior Ltd*

Gary Brothers and Charlie Tateson examine this decision and the principles of the *Kittel* line of cases in an article in *Taxation*.

Taxation, 5 March 2020

5.8.4 Missing trader decision: telecommunications services

HMRC assessed a company to £2,381,076 in denied input tax on 18 transactions in electronic communications services. Due to illness, the hearing of the appeal was spread out over 5 days in May 2018, December 2019 and February 2019 with written submissions in March and May 2019. The director of the company accepted that its transactions were connected with a fraud, but claimed that he was an innocent dupe who neither knew nor had the means of knowing what was going on.

Judge Cannan examined the history of the business and its links with the fraudulent parties. He considered the director to be an honest and reliable witness. However, the transactions had lacked commercial rationale; the judge concluded that the director did not know of the connection to fraud, but should have asked more questions that would have led him to the answer. He therefore had the means of knowing, and his appeal was dismissed.

First-Tier Tribunal (TC07565): *The 3p Telephone Company Ltd*

5.8.5 Missing trader decision: software

A company that had been in business since 2000 was denied input tax deductions in 03/15, 06/15 and 09/15 totalling £216,848 on the grounds that there was a connection to missing trader fraud. The main disputed

transactions related to purchases of software that were claimed to have been sold on to a customer based in Hong Kong. The company appealed, arguing that HMRC had not proved a link to fraudulent evasion, and also that it neither knew nor could have known of such a link.

Judge Malek heard evidence from several HMRC officers and from the director of the company, whose reliability was not "wholly satisfactory". The evidence of the officers was accepted as establishing, on the balance of probabilities, that there were tax losses and they resulted from fraudulent evasion by defaulting counterparties. The judge examined a number of criticisms of the director's conduct and, while rejecting some of them as "not convincing", he accepted that there was enough to show that the director ought to have known about the connection with fraud. It was not necessary to consider the question of actual knowledge.

First-Tier Tribunal (TC07533): *Pyramid Distribution Ltd*

5.8.6 New refund bodies

The Value Added Tax (Refund of Tax) Order 2020 specifies four new non-departmental public bodies eligible to claim VAT refunds under s.33E VATA 1994 in respect of cost-sharing arrangements or contracted-out services, and comes into force on 1 April 2020.

SI 2020/185

6. ADMINISTRATION AND PENALTIES

6.1 Group registration

Nothing to report.

6.2 Other registration rules

6.2.1 Unrealistic extrapolation

Between December 2009 and August 2013, HMRC seized a number of packages of hand rolling tobacco either addressed to or belonging to an individual who lived in a caravan in Morecambe, Lancashire. They concluded that he was selling the tobacco and was therefore liable to registration for VAT. He admitted to selling a small amount of tobacco to family and friends, but nothing like the amount required to exceed the VAT registration threshold.

HMRC's initial decision was based on an extrapolation from two seizures on consecutive days (4 and 5 December 2009). These two days were used to extrapolate a daily average turnover of £2,050. This would have put him over the VAT registration threshold after 34 days. The turnover over a longer period was calculated by averaging 7 seizures between December 2009 and August 2013, which gave an average daily sale of £1,046 and a turnover over the period from 1 March 2010 to 22 August 2013 of £1.3m. This was the basis for an assessment to VAT and a penalty of a similar amount.

The appellant's representative put forward three main arguments to undermine the "best judgement" of the assessment:

- the lack of appropriate storage facilities for that quantity of tobacco;
- the lack of working capital to fund such a venture;
- the lack of sufficient demand in the local area.

The officer was aware of the appellant's circumstances but had not asked questions about any of these points. The officer's background at HMRC was in the investigation of MTIC fraud relating to mobile telephones.

The judge pointed out that "best judgement" had no relevance to a registration decision in Sch.1. Nevertheless, and in spite of the lack of evidence produced by the appellant about what had actually taken place, the judge concluded that the evidence did not support HMRC's conclusion. The extrapolation based on the first two seizures, assuming that they would produce a daily average of sales, when there were only five more (smaller) seizures over the next three and a half years, was not credible.

HMRC might want to consider whether the individual should have been registered from a later date; however, his appeal against registration with effect from 1 March 2010 was allowed.

First-Tier Tribunal (TC07515): *Christopher Kendrick*

The case is discussed in an article in *Taxation* by Neil Warren. He notes that the trader was in the wrong, but HMRC's decision was nevertheless wholly unrealistic. The trader's personal circumstances, and the likelihood of him being able to sell the calculated amount of tobacco in his local area, should have alerted HMRC to the flaw in their argument.

Taxation, 19 March 2020

6.2.2 Compulsory registration

An individual appealed against decisions that he should have registered for VAT from 1 August 2010, together with assessments to VAT and income tax on undeclared turnover and related penalties. As is often the case, the Tribunal began with a consideration of the procedural failures in the appeal – HMRC had made several decisions, but the trader had only appealed within the correct time limit against one of them. HMRC had raised no objection, but only the Tribunal could formally accept a late appeal; the judge considered the correspondence and concluded that the Tribunal had already accepted the irregularities "unless HMRC had further objections", and decided that it would be inappropriate to re-open that question.

The decision then examines in detail the procedure for investigating and assessing a fish-and-chip shop. HMRC placed considerable reliance on data from a supplier, which the trader disputed related to him. The officer had decided that 50% of sales were suppressed and had applied that uplift to the figures recorded by the trader, resulting in an EDR of 1 August 2010. The trader disputed the figures and therefore the conclusion drawn from them.

After recounting the submissions, the judge concluded that "the evidence presented by both parties is rather sparse". The judge pointed out areas in which each party could have strengthened their case by inclusion of better supporting evidence (if, of course, it supported their case). After further discussion of the law, the judge concluded that the trader's declared turnover was not credible in the light of the results of invigilation, and dismissed all the appeals.

First-Tier Tribunal (TC07517): *Tahsin Dagdelen*

6.2.3 Updated Notice

HMRC have updated their Notice *Who should register for VAT* to remove references to temporary arrangements for advanced notification of UK VAT registration, which were to have applied in the event the UK left the EU without a deal.

Notice 700/1

6.2.4 Article

In an article in *Taxation*, Neil Warren examines practical situations in which clients might seek to "back-pedal", including retrospective deregistration (only possible if the client has ceased trading), retrospective joining or leaving the flat rate scheme, or applying an option to tax or special method of partial exemption from an earlier date than has been agreed with HMRC.

Taxation, 6 February 2020

6.3 Payments and returns

6.3.1 Deferral of payments

HMRC have announced that VAT payments may be deferred by businesses that are struggling to cope with the impact of Covid-19. VAT returns must still be submitted on time. The relaxation does not apply to VAT MOSS liabilities.

The guidance states:

If you're a UK VAT registered business and have a VAT payment due between 20 March 2020 and 30 June 2020, you have the option to:

- *defer the payment until a later date*
- *pay the VAT due as normal*

It does not cover payments for VAT MOSS or import VAT.

HMRC will not charge interest or penalties on any amount deferred as a result of the Chancellor's announcement.

HMRC will continue to process VAT reclaims and refunds as normal during this time.

<u>If you choose to defer paying your VAT</u>

If you choose to defer your VAT payment as a result of coronavirus (COVID-19), you must pay the VAT due on or before 31 March 2021.

You do not need to tell HMRC that you are deferring your VAT payment.

<u>Payments made by Direct Debit</u>

If you normally pay by Direct Debit you should contact your bank to cancel your Direct Debit as soon as you can, or you can cancel online if you're registered for online banking.

<u>After the VAT deferral ends</u>

VAT payments due following the end of the deferral period will have to be paid as normal. Further information about how to repay the VAT you've deferred will be available soon.

<u>If you're in temporary financial distress because of COVID-19</u>

If you are experiencing financial difficulties more help is available from HMRC's Time to Pay service.

Although this policy does not apply to import VAT, on 10 April HMRC announced that duty deferment account holders who would be unable to pay on 15 April should contact HMRC to discuss further deferment terms; and importers not using deferment accounts should also contact HMRC if they were in financial difficulties.

"HMRC will consider this request and decide whether or not to agree an additional time to pay. The decision will be taken on a case-by-case basis and could be refused. If the request is approved the conditions, including the length of time offered, will depend upon the importer's individual

circumstances and may require the holding of a guarantee for the period of the time extension."

www.gov.uk/guidance/deferral-of-vat-payments-due-to-coronavirus-covid-19

6.4 Repayment claims

6.4.1 *Fleming* claims

A company made a claim for repayment of £233,302 relating to the period 1 June 1988 to 30 September 1996 on 30 March 2009. HMRC rejected the claim on 4 December 2009 on the basis that there was no evidence to support it. Further evidence was provided as part of a request for a review of the decision, but HMRC upheld their original decision on 1 February 2010. The company appealed on 25 February 2010; the appeal was stayed behind various other appeals, and in the intervening period the amount concerned was reduced to £183,677.

The claim related to incentive payments received in respect of company cars – an "*Elida Gibbs* claim". The judge (Jonathan Cannan) reviewed the history of such claims, including the agreement of HMRC to accept estimated figures in certain circumstances on the basis that it was reasonable for detailed evidence not to have been kept to support a claim.

Nevertheless, HMRC did not accept that this company had established the basis for a claim. It needed to show that it had accounted for output tax on incentive payments; it needed to provide some evidence of the number and cost of vehicles purchased, the proportion of them that were non-commercial, and which manufacturers supplied them (because not all manufacturers paid bonuses).

The main evidence for the taxpayer was the witness statement of two employees who had worked in the transport and business support services departments. A key question was whether cars were bought directly from manufacturers, or through dealers. If they were bought from manufacturers, it was more likely that bonuses would have been treated as discounts (reducing irrecoverable input tax rather than accounting for output tax). The witnesses' recollections were not sufficiently reliable to satisfy the balance of probabilities, so the judge concluded there was not enough evidence to support a finding that the company had probably paid output tax.

That was enough to determine the appeal against the appellant, but the judge went on to conclude on the other factual issues. There was very little evidence in relation to whether the company would have paid output tax if it had bought cars from dealers and received the bonuses from manufacturers; the judge stated that "it is unlikely that a large business such as the appellant would not have declared the output tax".

On the other hand, the calculations that were then used to produce the repayment claim were too speculative to satisfy any level of proof. The judge was not satisfied as to the amount that might have been overpaid, and could not conclude that there was any minimum amount that he could be so satisfied by.

The appeal was dismissed.

First-Tier Tribunal (TC07585): *Brammer UK Ltd*

The same issue arose in another appeal before the same judge (covering both *Elida* and *Italian Republic* claims, because the business was a motor dealer). The claim was brought by the former owner of the business after it had been liquidated in October 2004. It was accepted that any rights to claim had been assigned to him on liquidation, and he was entitled to make the appeal.

In this case, the judge was satisfied that there would have been eligible vehicles, and although there were difficulties in establishing facts after so many years, he could come to a minimum figure for vehicles eligible for the claim. The company had claimed £310,000 on the basis of 316 eligible vehicles per year and a bonus rate of 10%; the judge concluded that there must have been at least 111 eligible vehicles, but the bonus rate was probably lower (HMRC argued that it would have been in the range 5 – 7%).

The consequences of the findings on the quantum of the appeal were left to the parties to agree; if they could not agree, they should return to the Tribunal for further directions.

First-Tier Tribunal (TC07575): *Ian Workman*

6.5 Timing issues

Nothing to report.

6.6 Records

6.6.1 Exemption from MTD for VAT

HMRC have created new guidance on when and how businesses can apply for exemption from digital reporting and record-keeping under MTD. This information was previously contained in separate HMRC guidance on when businesses must sign up for MTD. The guidance states:

You're automatically exempt from Making Tax Digital for VAT and do not need to apply if:

- *your taxable turnover has not been above £85,000 since April 2019*
- *you're already exempt from filing VAT Returns online*
- *you or your business are subject to an insolvency procedure*

You can still sign up voluntarily.

You can apply for an exemption if it's not reasonable or practical for you to use computers, software or the internet to follow the rules for Making Tax Digital for VAT.

This could be because:

- *of your age, a disability or where you live*
- *you object to using computers on religious grounds*

- *of any other reason why it's not reasonable or practical*

HMRC will consider each application on a case by case basis.

www.gov.uk/guidance/apply-for-an-exemption-from-making-tax-digital-for-vat

6.6.2 Digital links

HMRC have confirmed an extension to the deadline for implementing digital links for MTD for VAT in light of the impact of coronavirus (COVID-19). All businesses now have until their first VAT return period starting on or after 1 April 2021 to put digital links in place. This is to help businesses focus on doing the business they can and manage the COVID-19 challenges. The CIOT and ATT welcomed this relaxation.

www.tax.org.uk/media-centre/press-releases/press-release-tax-institute-welcomes-delay-making-tax-digital-'phase-two

6.6.3 MTD surveys

Taxation magazine carried out a survey of readers to assess their experience of MTD. The results have not yet been published. The survey will probably not be affected by late entries but is at www.surveymonkey.com/r/Y6TG76P.

Taxation, 19 February 2020

Results of a survey conducted by the CIOT and ATT about MTD strengthens the tax bodies' shared view that the project is far from achieving its goals. The survey results have led the two organisations to call jointly for a comprehensive review of the roll out of MTD before HMRC advance plans to roll out digital reporting obligations more widely.

- Nearly 90% of respondents say that MTD has not reduced errors;
- The costs of MTD compliance have far exceeded government estimates;
- Just 14% of respondents say there has been an increase in productivity in their organisation as a result of MTD.

The online survey was open to businesses and agents with an interest in MTD. The questions explored opinions about the implementation of MTD and the future of the whole MTD programme. There was a total of 1,091 responses. The survey found that the costs of complying with MTD have so far been significantly above HMRC estimates, and that generally it is not reducing mistakes.

www.tax.org.uk/media-centre/press-releases/press-release-survey-results-contradict-government-claims-realising

6.6.4 MTD review by HMRC

HMRC have published a review of the introduction of MTD for VAT, and a report on the progress towards introducing MTD for other taxes. While recognising that there have been some difficulties, the report suggests that HMRC regard the introduction as a success, and they appear to believe that the great majority of "customers" view it in the same way.

www.gov.uk/government/publications/making-tax-digital-review

Before the Budget, the CIOT made representations to the Treasury to:

- carry out a thorough review and evaluation of the roll out of MTD for VAT, in accordance with its tax consultation framework; and
- undertake further consultation around MTD, before making any commitments to the extension of MTD to other taxes or businesses.

This followed the results of the recent CIOT/ATT survey, which found MTD for VAT has not brought about a reduction in errors and has increased compliance costs beyond government estimates.

The CIOT welcomed the announcement that the government would publish an evaluation of the introduction of MTD for VAT. This release was issued before the report itself was published, and therefore does not reflect the difference in tone between the results of the HMRC review (overwhelmingly positive) and the CIOT.ATT survey (rather more negative).

CIOT Press Release 13 March 2020

6.7 Assessments

6.7.1 Assessment by refusal of input tax

A company appealed against a refusal of input tax of £758,000 for its period 07/06. There was a preliminary issue: the appellant argued that HMRC had never issued a formal assessment, and were therefore unable to collect any money. The FTT (TC04888) would have no jurisdiction to consider the matter, and should strike the case out. The judge examined a number of precedents, and was satisfied that the Tribunal did have jurisdiction over whether an assessment existed, and that HMRC's actions in this case constituted the making of one.

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

The company appealed to the Upper Tribunal. The grounds of appeal appeared to be directed at the factual findings of the FTT, so the UT began with a detailed explanation of the circumstances in which an appellate Tribunal would overturn findings of fact. It rejected the view of the company's counsel that it should remit the case to the FTT for reconsideration if it found errors within it, unless it could conclude that the decision would have inevitably been the same without the errors. The FTT decision was 100 pages long with 374 paragraphs. If everything was subjected to detailed analysis, it might be possible to discover some errors or lack of clarity; such errors would only undermine the decision if the UT was satisfied that the matter was material to the overall factual conclusion.

The judges (Mr Justice Roth and Judge Jonathan Richards) went on to consider the 36 detailed criticisms of the FTT's findings. They examined

them at length, and concluded that only one of them had any substance to it. In the context of the decision as a whole, that one matter was not particularly significant. There was no reason to overturn the FTT's findings of fact.

The UT was also satisfied that the FTT had been correct to conclude that the letters sent by HMRC to the taxpayer constituted an "assessment". It appeared that the company had never paid the tax, even though there had not been a formal agreement of "hardship", but HMRC appeared willing for the Tribunals to entertain the appeal in spite of non-payment. The UT concluded that the FTT did have jurisdiction to hear the appeal, and the UT had jurisdiction as well. The appeal was dismissed again.

The company appealed further to the Court of Appeal, now only arguing the ground that HMRC had not issued an assessment. The court noted that there was no statutory definition of "assessment", and no particular formality required by either statute or regulations. It was in general a legal act on the part of HMRC constituting its determination of the amount of tax that had been due. A notification of an assessment could be contained simply in a letter and could be contained in more than one document. The question whether an assessment had been made or not was to be determined on an objective analysis. The decision-maker's subjective state of mind could not alter that objective fact. Further, the test was how the document or documents said to have recorded an assessment were to be understood by the reasonable reader.

In the present case, the reasonable reader would have understood HMRC's letters, read together, as recording and notifying a determination of the amount of VAT assessed as being due. On an objective analysis, they had recorded an assessment of the VAT due and had simply not been a correction of the figures set out in the VAT return which had been submitted by the taxpayer. The letters had constituted a legally valid assessment within s.73 VATA 1994.

The court was critical of HMRC's processes and suggested that these should be reviewed so that taxpayers always had complete clarity over what was due and payable.

Court of Appeal: *Aria Technology Ltd v HMRC*

6.7.2 Best judgement

A takeaway food outlet appealed against an assessment for £23,555, reduced on review to £15,865, in relation to the period from 07/14 to 01/18. The assessment was based on a "best judgement" estimate of the underpaid VAT arising from failing to categorise zero-rated items correctly.

The company had agreed that an adjustment was appropriate, but claimed that this was only agreed for one year; HMRC had applied the same uplift to the whole of the four year period. The director, who presented the appeal in person in the absence of his accountant, argued that his company "is one of the very few restaurant/takeaway businesses in Londonderry that actually pay VAT. A very significant number of them are over the threshold and yet HMRC do not do anything to help tax compliant traders compete on a level playing field." The director wanted to bring this into the appeal, but the judge said he had no jurisdiction to "engage in a roving

inquiry as to the tax position of other takeaway businesses". It could only decide the present appeal by the present appellant.

The judge went on to note that HMRC had not alleged any dishonesty. This was a case of careless record-keeping rather than conscious wrongdoing. The director had taken responsibility for the VAT accounting in the middle of the period under assessment, and his evidence therefore suffered from a lack of contemporary knowledge or reliable documentation to displace the figure that HMRC had used.

The judge reviewed the history of the enquiry and the dispute, and concluded that the first hurdle for a best judgement assessment – that the returns were not accurate – was cleared by the director's agreement that 14% was too high a proportion of zero-rated sales, and 7% was a fairer estimate. It was then not possible for the director to displace the resulting application of that figure to earlier years, because the evidence required was insufficient.

The appeal was dismissed.

First-Tier Tribunal (TC07537): *2 Strand Road Ltd*

6.7.3 Late registration and penalties

A hairdresser appealed against an assessment for VAT of £67,807 for the period from 1 March 2008 to 31 August 2015, a belated notification penalty for the period up to 15 May 2014, and related income tax assessments and penalties. She had owned the salon since 1983; she had been registered for VAT from 24 October 1998, but deregistered on 16 January 2008. HMRC investigated this in March 2011, as the self-assessment returns suggested that she was still trading with turnover above the registration threshold.

A questionnaire was returned covering the period from April 2009 to March 2011. Turnover was stated to be below the threshold, and no further action was taken. A further questionnaire sent in April 2013 also claimed that turnover was below the threshold for the years to 31 October 2011 and 2012.

In the course of further enquiries, HMRC alleged that the trader's diary had been amended to remove bookings, and the receipts in the accounts were incomplete. They also alleged that wages had been paid out before receipts were recorded, suppressing the VATable turnover.

The decision records the trader's account of how she tried to deal with the investigation. There were reasons for alterations to the diary – some customers did not actually receive the treatments they had booked for, and some staff members recorded "invisible" clients to give themselves less to do. She had attempted to reconcile the diary with the bankings, which she was sure were accurate, and had therefore amended the diary to match. This had led HMRC to suspect that her records were not accurate.

The trader argued that the assessment was not raised to best judgement, in that there was an inconsistency of method and a refusal to take additional information into account. She also questioned the arithmetical accuracy of the assessment. However, she did accept that she should have re-registered for VAT (or not deregistered).

The judge considered the discussions that had taken place between the taxpayer and HMRC officers in detail. He noted that her accountants had prepared a single period VAT return for the period from March 2008 to August 2015 showing turnover of £210,096; there was no explanation for the discrepancy between that and the accounts for the same period, which showed turnover totalling over £500,000. This clearly justified HMRC's belief that the return was inaccurate, so a best judgement assessment was appropriate.

The judge noted that HMRC had applied different methods to the periods November 2012 to August 2015 (extrapolating turnover from wages using an industry average for that ratio) and March 2008 to October 2012 (adding wages to declared turnover, on the basis that the bankings were simply net of wages). The judge did not consider that the second of these approaches was justified or reasonable based on the figures and the evidence, and directed that HMRC should revisit the assessment to apply the "turnover/wages" method. Further, HMRC should revisit the whole assessment to consider whether the right ratio had been used.

The behaviour of the trader had been careless rather than deliberate. The penalties and income tax assessments were also to be reviewed in accordance with the rest of the decision, and one of the income tax penalties was assessed out of time. The appeal was allowed in part.

First-Tier Tribunal (TC07521): *Brenda Crutchley*

6.7.4 Not best judgement

Another case involving a takeaway restaurant involved an assessment for 16 periods from 06/11 to 03/15. The decision records the methodology of such an investigation, including making undercover visits, observing the till, writing up notes in the toilet, and "planting" particular banknotes in payments for test meals in order to trace them in the till afterwards during unannounced inspections at close of business.

The decision considers the "long stop" time limit: as the assessments were raised more than four years after the end of the first period concerned, some periods could only be included if there was deliberate conduct leading to a loss of tax. HMRC put forward several grounds for alleging deliberate conduct, but these were based on objective factors such as the surprisingly high ratio of recorded card sales to cash sales, and the fact that the till had no battery so its memory was erased when it was unplugged. The required test, for which the burden of proof lay with HMRC, was to show that the appellants had subjectively decided to make returns knowing they were inaccurate. HMRC tried to draw inferences from the fact that the traders chose not to give evidence to the Tribunal, but the judge did not consider that there was enough to support a finding of deliberate conduct. The assessments for periods before 09/12 were therefore out of time.

Turning to the "short stop" of 12 months or 2 years, HMRC were relying on information about rental income to justify a delay in raising an assessment on undeclared turnover. This was a completely separate matter and could not justify extending the normal 2 year deadline. Assessments for periods before 09/14 were therefore also out of time.

The judge also considered that the method used by the officer in raising the assessments lacked logic or common sense. She had used a ratio of card to cash sales of 37:63, when the evidence pointed to something closer to 50:50, which she admitted was normal. The ratio was so out of line that it could not be regarded as reasonable. Further, the result was a turnover that did not appear credible, and would have required 27 to 43 extra daily sales.

The judge recalculated the assessments for the two years that he considered to be in time, and discharged the rest. The appeal was allowed in (large) part.

First-Tier Tribunal (TC07523): *Wei Xian Peng and Qian Hong Peng*

6.7.5 More lack of judgement

A trader was assessed to VAT for the years 2012/13 to 2016/17. She had run a corner shop selling food and some other goods during that period; when she moved away and ceased trading in 2016 she thought she no longer needed the records so she disposed of them, which made it difficult to argue against HMRC's assessments. These were based on figures supplied by the present owner: HMRC took the current turnover, rounded it down to £200,000, then reduced it progressively for the retail price index over the period in question. They then applied the flat rate scheme percentage of 4% to the resulting turnover to arrive at a VAT liability of £27,325. This appeared to be based on total turnover for the five years of £683,138.

The trader (who was only 20 when she acquired the business) accepted that she should have been registered for VAT, and regretted that she had not taken advice or asked HMRC for information. However, she considered that the basis of the assessment was flawed. The new owner said that "£3,000 was a good week and £1,000 was a bad week"; the figure of £200,000 for a year's turnover was not justified. Various other elements of the new owner's figures had been changed with the effect that the assessment was increased. The FRS should not have been applied to a business with a turnover alleged to be greater than £150,000, and it should not be imposed on a trader who would probably have made a significant proportion of zero-rated sales. The trader's accountant produced figures for similar clients showing that their net VAT liability for a year was substantially below 4% of turnover.

The judge concluded, quite briefly, that the assessment had not been raised to best judgement. He quoted from *Van Boekel*: best judgement requires an "honest bona fide judgment by the Commissioners on the material before them of the amount of tax due" and that the "Commissioners will fairly consider all material placed before them and, on that material, come to a conclusion which is reasonable and not arbitrary as to the amount of tax which is due." In this case, that would require a consideration of the nature of the appellant's business, the known facts about the trading conditions including the date of commencement, the existence of any competitors, the split between standard and zero rated supplies, the split between card and cash sales and any other special factors brought out in the enquiry. "A blanket approach can never be a best judgment assessment."

The judge made various findings on the basis of the appellant's accountant's representations, and reduced the assessment from £27,325 to £4,255. Although no appeal had been made against penalties, the judge commented that this should be resolved without recourse to the Tribunal; the appellant had done everything she could to resolve the issue once she became aware of it. Her ignorance of the law and her failure to take advice could be characterised as "careless behaviour", and she should be given the maximum discounts for cooperation, disclosure and assistance.

The appeal was allowed in (large) part.

First-Tier Tribunal (TC07528): *Sital Khimji*

The case is discussed in an article in *Taxation* by Neil Warren. He is concerned that such a case should ever have proceeded as far as the Tribunal, and relieved that the Tribunal restored some element of sanity to the amount assessed.

Taxation, 19 March 2020

6.7.6 Yet more lack of judgement

HMRC assessed a filling station to £686,054 of underpaid VAT for the periods from 08/15 to 10/17 on the basis of estimated underdeclared sales. The company denied that it had omitted any turnover, and argued that underdeclaration on this scale would have had to depend on the participation of the public (agreeing to pay in cash, when debit cards had become more normal) and all the employees in the filling station. The ratio of diesel sales to unleaded petrol sales claimed by HMRC was not supported by any statistical evidence.

The Tribunal heard evidence from the owner, an employee and the investigating officers. The judge considered various precedents on the concept of "best judgement assessments" and its application, including the *Zhu Ghang* and *Khimji* decisions described above.

The judge noted that HMRC's calculations contained some basic flaws (in relation to the hours that the filling station was open) and some questionable extrapolation (the invigilations were not sufficiently varied – none at a weekend, three out of five on a Thursday, four in the morning). The assessment of £686,054.00 implied sales of diesel totalling £4,116,324.00 over the assessed quarters 08/15 to 10/17 – a period of 29 months or 792 days. This would require the company to receive an average of £5,197.38 every day in cash in addition to the declared takings. There was no evidence of another bank account, and no evidence of the pumps being tampered with.

The judge (Alastair Rankin) came to the following conclusion:

We note Mr Justice Carnwath in Rahman states that it is necessary for this Tribunal to find that HMRC's assessment is a "spurious estimate or guess in which all elements of judgment are missing; or is wholly unreasonable." As HMRC had no evidence for the volume of diesel sales during the evenings and at weekends we find that an important element of Mr Bingham's calculations was missing. This is not to criticise Mr Bingham – he could only work on the figures that he was given.

We follow Judge Cannan's example in his Golden Cube decision that "the principal issue on the appeal therefore is whether the Assessment is

excessive." In the absence of any evidence that the Company's receipts averaged an additional amount of almost £5,200.00 per day we have come to the conclusion that the assessment is excessive.

As Ms Brown did not ask us to consider a lower assessment and in the absence of any means of calculating a "best judgment" assessment for the reasons outlined above we allow the appeal.

First-Tier Tribunal (TC07636): *FW Services Ltd*

6.8 Penalties and appeals

6.8.1 Default surcharge

A landscape gardening company appealed against surcharges for 10/17, 04/18, 10/18 and 01/19. It had been in the surcharge regime from 10/17. The first three late payments did not lead a demand for a surcharge because the amounts at 2% and 5% were below £400. The 01/19 surcharge, calculated at 10%, was £572.

The appellant's grounds of appeal were that his part-time accounts manager had broken her arm in September 2017, and it was extremely difficult in Ynys Mon to find someone else who could operate Sage accounting. The accounts function was "paralysed". The company did not initially contact the Jobcentre because it believed that the manager would return; it was not until April 2018, when she decided she would not return, that a permanent replacement was sought.

The judge decided that this constituted a reasonable excuse for 10/17 which stopped in 04/18; removing the first default reduced the rate of penalty for subsequent defaults, so the 01/19 surcharge would be less than £400 and should be cancelled.

First-Tier Tribunal (TC07506): *Eglas Ltd*

A taxpayer appealed against a 10% surcharge of £493 for its return period 01/19. The return was filed electronically comfortably earlier (28 February), but the liability was settled by bank giro credit on Wednesday 6 March and was not credited to HMRC's account until 8 March, 1 day late.

The trader appealed against the penalty, claiming that the payment had been made in good time and on the same date as in all previous quarters. Unfortunately, it appeared that this was true, but the earlier payments had been treated as being in default. They had not incurred a financial penalty because the liabilities were at 2% or 5% and below £400. The liability notices had given adequate warning of the need to pay in good time. There was no reasonable excuse, and the appeal was dismissed.

First-Tier Tribunal (TC07530): *Hong Jiang*

A company appealed against 14 surcharges totalling £10,052 and extending from 01/15 to 05/19. The trader had failed to respond to directions and had asked for a postponement at the last minute after failing to give days to avoid. He agreed to give evidence by telephone, and in the course of oral evidence he appeared to the judge to be an unreliable witness, contradicting statements he had made in correspondence and even in the course of the hearing.

The judge dismissed in turn either the evidence or the possible legal effect of reliance on a factoring company that did not pay on time, reliance on the company's accountant, the death of the director's father, his personal cash flow difficulties, and the alleged disproportionality of the surcharges. The appeal was dismissed.

First-Tier Tribunal (TC07574): *Logan Technical Resourcing Ltd*

A company within the payments on account regime appealed against a 10% surcharge of £269,239 for its 10/17 period. The circumstances were

unusual: the surcharge liability period had begun as a result of an error in 10/15 relating to an input tax credit of £399.92, and had been extended by alleged defaults in 04/16 and 10/16, which were disputed by the company.

The original error arose because the head of finance had noticed the omission of £399 of input tax credit when reviewing the spreadsheets supporting the return. The payment amount was amended, but the finance manager failed to adjust the return. HMRC therefore recorded a default: even though the correct amount had been paid, it was less than the amount shown as the liability on the return. HMRC sent out a SLN, which the judge noted could not be appealed at the time.

In the quarter 04/16, the error of £399 arose again. HMRC were still expecting the extra payment from 10/15, and the company intended to make a correction on the current return; an extra £399 was shown on HMRC's ledger as due with the first instalment, and was then deducted from the balancing payment after submission of the return, but the return was not corrected. What was rather clearer was that the first payment on account instalment was paid 22 days late; that was definitely a default.

HMRC imposed a 2% penalty of £4,230 and extended the SLN. The head of finance decided not to appeal because the amount was modest compared to the size of the business, and she wished to draw a line under the matter. The company paid the penalty and the £399. Unfortunately, that amount was then shown as a credit on the company's VAT account, and deducted from the balancing payment for the 10/16 quarter. That resulted in a further default; the head of finance rang HMRC to explain on 16 January 2017, and no surcharge was issued, but a SLNE was raised covering the period to 10/17.

The balancing payment for 10/17 was £2,692,392 and was paid one day late. The head of finance accepted that there was no reasonable excuse for paying the first instalment late in 04/16 or the balance late in 10/17. However, she claimed that the appellant had taken reasonable care in the preparation of the returns for both 10/15 and 04/16.

HMRC argued that the penalty was imposed in accordance with the legislation, and even if there were genuine mistakes made in good faith, "the legislation does not pardon such errors". Only a reasonable excuse could remove the penalty, and there was none. The lateness of a payment was a question of fact, and the length of the delay was immaterial.

The appellant put forward a number of propositions:

- there was no default for 10/15, or else there was a reasonable excuse for it, in which case the 10/17 surcharge should be reduced to 5%;
- there was a reasonable excuse for any default in 10/16, which would lead to the expiry of the SLN and remove the 10/17 surcharge altogether;
- the surcharge was disproportionate and should be discharged.

In support of the first proposition, the taxpayer argued that its failure to claim a relief in 10/15 was not the kind of default at which the legislation was aimed. It should therefore not be counted. That would make 04/16 (on HMRC's reckoning) the first period of default, and the 10/17 period would be subject to a 5% surcharge. The company would also have paid a surcharge that, on this later argument, it should not have paid.

As an alternative, the non-payment of the £399 was subject to a reasonable excuse, because it was not VAT due, even though it was shown on the return.

In support of the first proposition, the company argued that everything else followed on from the first error. If the first period had been corrected at the time, there would have been no late payment in 04/16 and therefore no penalty, so there would have been no payment to misallocate as a credit in 10/16 and the correct VAT would have been paid at the correct time. Alternatively, the taxpayer honestly and genuinely believed that the correct VAT had been paid, and this was capable of amounting to a reasonable excuse.

The disproportionality argument was not based on the fact that the balancing payment was only 12 hours late, but on the fact that a surcharge of £269,000 arose from an underpayment of £399 that was not in fact due. This was an exceptional circumstance and not within the normal principles of *Trinity Mirror*.

The judge analysed the wording of s.59 VATA 1994 and concluded that Parliament could not have intended that HMRC should be entitled to surcharge errors in returns that were in favour of HMRC – that is, the return was incorrect in stating too high a liability, and the trader paid the correct liability. There was therefore no default in 10/15; alternatively, there was a reasonable excuse for non-payment because of the trader's honest and reasonable belief that the £399 was not due.

Following on from that, the late payment in 04/16 should have been regarded as the first default, leading to a SLN but not a 2% penalty. Even though the company had not appealed, the judge regarded the correctness of that penalty as appealable in connection with its effect on the later surcharge. If the amounts paid should not have been paid, they were validly credited against the balancing payment for 10/16; there was therefore no default in that period, and the SLN for 04/16 had expired before 10/17.

The judge noted that it was therefore unnecessary to consider the defence of disproportionality; however, he rejected HMRC's view that the FTT had no jurisdiction to consider it. The Upper Tribunal in Trinity Mirror had concluded that it could not identify a circumstance in which a surcharge might be disproportionate, but acknowledged it was possible in exceptional circumstances. The judge considered that the combination of factors in the present case might have cleared that hurdle.

The appeal was allowed and the surcharge for 10/17 was reduced to zero. It is not clear whether that effectively also cancelled the 04/16 surcharge, or whether that will still have been payable as assessed and not appealed at the time.

First-Tier Tribunal (TC07578): *Medivet Group Ltd*

A company appealed against a 5% surcharge of £1,368 for its 01/19 period. It had defaulted in 10/17 and again in 04/18, when a 2% penalty of £949 was imposed and paid. The returns had all been filed on time, and the VAT was paid one day late. The company had asked for an independent review, but the decision was confirmed.

The judge noted that there was considerable confusion in the history of the case, as reflected in amendments made by HMRC to previous defaults and surcharges. For example, a 5% penalty relating to the 07/18 quarter had been removed by HMRC by a letter dated 3 July 2019. On the same day, HMRC had removed a 10% penalty for the 10/18 quarter. The judge commented that the company had had to deal with very difficult cash flow problems for 8 months while believing that HMRC would impose £8,000 in penalties which eventually were cancelled. As a result of the cancellation of those penalties, the one under appealed was reduced from 15% to 5%, but was nevertheless upheld by HMRC.

The judge reviewed the history of the company's problems: the owner of a restaurant had retired and entrusted its management to a senior employee. After a period of about a year, he engaged accountants to investigate why the company was suffering cash flow problems when it ought to have plenty of money in the bank. They discovered a substantial fraud being carried out by the manager, possibly with the assistance of some of the staff. The owner dismissed the employees and tried to negotiate time to pay with HMRC, maintaining constant contact for some 14 months (while, in his words, having "no meaningful conversation with anyone at HMRC").

The judge considered the precedents of *ETB (2014) Ltd* (Upper Tribunal 2016) and *Perrin* (UT 2018) in considering what could be a reasonable excuse. In his view, the owner had acted in an objectively reasonable and responsible way; the effects of the fraud upon the appellant were still in January 2019 directly responsible for the company's inability to pay its VAT on time. Although the trader's belief that a TTP arrangement covered 01/19 was mistaken, nevertheless there was a reasonable excuse for late payment in that period, and the appeal was allowed.

First-Tier Tribunal (TC07581): *Mirencliff Ltd*

A company appealed against surcharges of £14,337 for 11/17 and £10,950 for 02/18. It had been in the surcharge regime since 02/14. The decision records a history of defaults and surcharges paid at 15%; also of Time To Pay arrangements and HMRC agreeing to cancel surcharges, while warning that TTP has to be agreed before the due date.

In respect of the two periods under appeal, there was no dispute that no TTP had been agreed, or that the payments were made late. The trader's appeal was based on long-running cash flow problems arising from a difficult customer. The judge reviewed the precedents on "insufficiency of funds", and concluded that the present case did not amount to a reasonable excuse. In spite of the warning letters explaining the availability of TTP, the trader had not negotiated with HMRC at the right time. The appeal was dismissed.

First-Tier Tribunal (TC07592): *Miles Water Engineering Ltd*

6.8.2 Penalties

A trader appealed against a "failure to notify" penalty of £20,405. The hearing proceeded in the absence of the appellant after consideration of whether it was in accordance with the interests of justice to do so. The trader operated a takeaway business; HMRC investigated it in 2017 and noted that the bank statements only reflected net payments received for

"Just Eat" sales rather than gross turnover. HMRC made a best judgement assessment based on cash sales amounting to 16% of turnover, and information obtained directly from Just Eat (as the trader could not access his Just Eat account). This showed that VAT registration was due from July 2015 onwards; VAT arrears were calculated using the Flat Rate Scheme.

The appellant's representatives responded that there had been two separate businesses, one of which was operated in partnership. HMRC asked for more details, but in the absence of a reply, confirmed their decision and assessed £33,315 in VAT; later they added the penalty, based on prompted disclosure, deliberate conduct and minimal cooperation (no reduction for telling, 15% for helping and 10% for giving access – penalty percentage of 61.25%).

The trader later accepted the VAT liability but appealed against the penalty, claiming that it was disproportionate and breached his human rights. The key question for the Tribunal was whether the behaviour which led to the failure was deliberate. The appellant argued that no liability to register arose because there were two businesses, both trading under the VAT threshold, and that he was only responsible for one business. However, the appellant consistently failed to provide any evidence that there was a separate business owned by his wife. In correspondence with HMRC, the contention that his wife had any involvement was not raised until HMRC had issued their best judgement decision; after that, his account was inconsistent. The wife had never declared any self-employed income.

Judge Anne Fairpo agreed with HMRC's assessment of the behaviour and the appropriate level of mitigation, and dismissed an appeal based on proportionality and breach of human rights. The penalty was upheld.

First-Tier Tribunal (TC07534): *Saghir Ahmed*

A scrap metal dealer has been to the FTT for the fourth time in a case concerning £160,281 assessed as output tax on despatches to a Belgian customer without sufficient evidence and the denial of £2.6m input tax on *Kittel* grounds. TC04584 and TC05036 were case management hearings in 2015 and 2016; in TC06208 (late 2017), the judge had concluded that its transactions were contrived, and on the basis of a combination of factors, concluded that its directors knew, or at the very least had the means of knowing, that their dealings were connected with fraud.

The latest appeal concerns "deliberate conduct" penalties totalling £1,444,813 relating to the errors. HMRC applied in November 2018 to have part of the appellant's case struck out as having no reasonable prospect of success. The company's appeal against the zero-rating penalty accepted that it had been careless; in relation to the input tax claim the company argued that it had taken reasonable care, or had at the most been careless. Having lost the earlier appeals, it had to accept that the returns were inaccurate.

HMRC claimed that the appeals were an abuse of process, as the FTT had found that the directors knew that their returns were inaccurate. The conduct therefore had to be "deliberate". The judge considered a number of arguments, and concluded as follows:

"I disagree with the Appellant that an allegation of deliberate conduct is tantamount to an allegation of fraud and/or must inevitably involves some element of dishonesty. I disagree with the thrust of the Appellant's submissions that deliberate conduct in Schedule 24 has a higher threshold than actual knowledge of connection to fraud in a *Kittel*-type appeal. I simply do not see (whether as a matter of law or language) why that should be the case."

Rather, he agreed with the Tribunal's decision in *Auxilium Project Management Ltd* that "a deliberate inaccuracy occurs when a taxpayer knowingly provides HMRC with a document that contains an error with the intention that HMRC should rely upon it as an accurate document". On the basis that the earlier decision effectively proved that this threshold had been met, the judge agreed with HMRC that most of the grounds of appeal were both an abuse of process and should be struck out as having no prospect of success.

The company was allowed to continue an appeal on significantly narrowed grounds, mainly concerning the level of mitigation. HMRC had delayed issuing a Statement of Case until the outcome of the present appeal, and were given 28 days to do so.

First-Tier Tribunal (TC07541): *C F Booth Ltd*

A company appealed against a "careless inaccuracy" penalty of £3,846 in relation to an understatement of output tax of £24,933 for the periods from 03/14 to 06/17. The company had failed to notice, for an extended period, that it had deducted an exempt commission retained on holiday lettings from the amount declared as turnover for VAT. When this was discovered, the output tax was promptly corrected without argument.

The judge examined the circumstances of the company, which placed greater than usual reliance on its accountants because of the terminal illness of the owner. He referred to precedent and concluded that "in determining whether a taxpayer has taken reasonable care, one tests this by considering the behaviour of a reasonable taxpayer (an objective test) in the position of the particular taxpayer bringing the appeal. We need to consider all the circumstances in which a taxpayer finds itself. Furthermore, a taxpayer will still have taken reasonable care if an accuracy in a return is a result of a failure by an agent if the taxpayer has taken reasonable care to avoid that inaccuracy. Again, what is reasonable care depends on all the circumstances."

In the circumstances of the case, it had been reasonable for the taxpayer to rely more heavily on the accountants than might in other circumstances be acceptable. The judge was highly critical of the accountants for failing to reconcile the annual accounts to the VAT returns and to notice the discrepancy. The judge considered that the taxpayer had taken reasonable care and allowed the appeal.

The judge also considered the alternative defence of "special circumstances". The judge could only impugn any decision by HMRC in relation to special circumstances, and substitute his own decision for that of HMRC, if he concluded that HMRC's decision in respect of special circumstances was flawed. In his view, HMRC had come to flawed decisions in not considering the illness of the owner on three separate

occasions when dismissing the possibility of allowing a special reduction in the penalty. He would also have allowed the appeal on that basis.

First-Tier Tribunal (TC07548): *Udlaw Ltd*

An individual appealed against penalties levied on him under VATA 1994 s.61 in relation to VAT evasion by a company he owned. The £284,718 penalties were charged at 90% of the VAT evaded; he claimed that he had not been dishonest, and that the 10% reduction for cooperation was insufficient.

The representatives did not agree on the test to be applied:

"Mr Jones, on behalf of HMRC, submits that the objective part of this test requires the Tribunal to consider what a reasonable and prudent taxpayer would have been expected to have known or to have done in the circumstances. Mr Brown disagrees with this and says that, once it is established what Mr Jarvis knew, the only question is whether the actions which he took (or failed to take) in the light of that knowledge were, objectively, dishonest – i.e. it is irrelevant what a reasonable tax payer would have been expected to know or would have done."

The judge preferred the taxpayer's representative's interpretation: HMRC's version "to some extent confused [the test for dishonesty] with the question as to whether or not a taxpayer might be said to have a reasonable excuse for their failure".

The judge went on to examine the history of a business which had accepted centrally issued assessments for an extended period, eventually going into liquidation owing HMRC over £300,000 in VAT, surcharges, penalties and interest. The appellant claimed that he had submitted paper VAT returns with cheques for the VAT due, but the Tribunal did not believe this. Looked at objectively, his conduct was dishonest.

Various arguments that the VAT assessment was excessive were dismissed because no evidence had been produced to support them. The level of cooperation warranted no more than a 10% reduction in the penalty. The appeal was dismissed.

First-Tier Tribunal (TC07550): *Geoffrey Charles Jarvis*

The proprietor of an Indian takeaway appealed against VAT assessments of £36,585 and "deliberate conduct, concealed" penalties of £27,440 for periods from 06/11 to 06/16. The trader asserted that he had declared all of his takings; he claimed that HMRC's views on the likely split between cash and card takings did not apply to his restaurant, because of special circumstances.

The judge concluded that the assessments were raised to best judgement and in time (which it was for HMRC to prove). It was then up to the trader to displace them, and he had produced no evidence at all to support his claims to support the accuracy of his original returns. It was more likely than not that HMRC's assessments were valid. The appeal against the VAT was dismissed.

On the other hand, it was for HMRC to prove deliberate conduct to justify the penalty. It was entirely possible that employees had removed the cash and defrauded the trader. Although that would not be a defence against the assessment on the VAT, it would be a defence against a deliberate

conduct penalty. The judge did not consider that HMRC had disproved this possible alternative explanation; rather, they had claimed that, as a sole proprietor, he was simply responsible for what happened in his restaurant. That was not enough to justify such a harsh penalty.

HMRC had not initially suggested "careless behaviour" as an alternative to "deliberate"; the judge asked for submissions from the parties as to whether this should be considered in the alternative. HMRC said that they would pursue such a penalty if deliberate conduct was not found, and the judge agreed that it was appropriate. Even if he had been defrauded by the staff, the proprietor had failed to put in place systems and reviews that would have helped to make sure that his VAT returns were accurate (and his turnover was not going missing).

The penalty was reduced accordingly.

First-Tier Tribunal (TC07566): *Ansar Ali*

HMRC have updated their factsheet *VAT dishonest conduct penalties* with information for taxpayers who need extra support. This appears to refer to the sentence at the outset: "If you have any health or personal circumstances that may make it difficult for you to deal with this matter, please tell the officer that's contacted you. We'll help you in whatever way we can."

CC/FS20

HMRC have also updated their *VAT Civil Penalties* Manual to confirm that policy advice and guidance on VAT civil penalties and default interest is now given by the Specialist Technical Team and not, as was previously, Tax Administration, Litigation and Advice (TALA).

VCP10140, VCP10386

One of the CIOT's main Budget representations to the Treasury was a request for a legislative definition of "deliberate" behaviour for tax penalties and extended time limit assessments. This definition should put beyond doubt that 'deliberate' behaviour requires a person to have known they were providing an inaccurate return or document to HMRC leading to an inaccurate self-assessment, or to have deliberately chosen not to provide a return or document at all. Such a definition would provide a starting point for discussions about behaviour between taxpayers, agents and HMRC.

The CIOT refers to HMRC's example of deliberate behaviour given in factsheet CC/FS7a *Penalties for inaccuracies in returns and documents*, and in Code of Practice 9, where the words 'fraud' and 'deliberate' are used interchangeably. The representation also stresses the CIOT's view that when making penalty determinations, HMRC should take account of any information taxpayers have included in the 'additional information' boxes on tax returns, despite the potential for 'confusion and unfairness' introduced by recent tax cases such as *Tooth* and *David Cliff*. The disclosure of additional information is mainly relevant to direct taxes.

6.8.3 Article

In an article in *Taxation*, Rachel Clark examines the FTT decision in *Cliff* (TC07358). This is a direct tax case, but it concerns the distinction between a "deliberate" and a "careless" error; the taxpayer had taken a

"considered and conscious choice" to describe his activity as a trade in thoroughbred horses when he was only an investor. The article considers that the FTT's decision – that it was not necessary for HMRC to show that the trader intended to avoid tax – is questionable and could have wide-ranging consequences.

Taxation, 27 February 2020

6.8.4 Late appeals

On 22 December 2017, HMRC assessed a company to £3,368 in respect of its 10/14 period. This was confirmed on review on 5 February 2018, following which the company appealed to the Tribunal on 24 October 2018. HMRC opposed an application to admit the appeal out of time.

The VAT in dispute was charged in relation to zero-rating a vehicle that the taxpayer had supplied for use by a wheelchair user. HMRC had decided that fitting a hard cover canopy to a pick-up truck did not meet the criteria for relief.

The appellant claimed that he had genuinely believed that an e-mail to the reviewing officer in January had made it clear that he wanted to appeal to the Tribunal if the review went against him. However, he had done nothing to follow this up until Debt Management tried to collect the debt. In the circumstances, the judge could see no reason to depart from the "robust approach to rule compliance" that the courts adopt after the "*Jackson* reforms" to procedure. The refusal was on the basis of the need for legal certainty alone; although HMRC also argued that the prospect of success was low, this could not be judged without a more in-depth hearing, which the judge did not consider appropriate or necessary to reach the decision on strike-out.

First-Tier Tribunal (TC07497): *Donald Mackenzie Ltd*

An individual appealed against a decision in 2014 that he should have been registered from 1 January 2012, and an associated assessed liability and penalty. There was a long history of confusion about what the basis of the appeal was, given that the trader had not submitted a tax return and therefore could not appeal against the assessment. The judge in the present hearing concluded that his grounds of appeal could be interpreted as including a competent appeal against the registration decision; however, applying the usual *Martland* criteria, there was insufficient excuse for a delay in appealing of three and a half years. The appellant had given details of mental health issues arising from the tax problems that led to the breakdown of his marriage; the judge said he had taken these into consideration, but there was no independent evidence of their severity and the language used to describe the problems did not appear to amount to a reasonable excuse. The application to appeal was refused.

First-Tier Tribunal (TC07500): *Amer Nawaz*

6.8.5 Procedure

HMRC applied to have a company's appeal struck out on the basis that it had no reasonable prospect of success. The dispute related to refusal of input tax in relation to supplies where the company had insufficient evidence to support zero-rating of scrap metal sold to a customer in

Belgium. The withheld input tax was said to represent the output tax that should have been accounted for.

HMRC argued that the company's appeal could not possibly succeed. It had admitted that it had not complied with Notice 725 in that it had not obtained adequate evidence of despatch until two years after the supply.

The judge considered the procedural history of the dispute and the confusion about what decisions had been taken, what could or had been reviewed, when rights of appeal arose and what appeals had been made. She concluded that the appeal did have a reasonable prospect of success, and deserved a full hearing.

The company's representative claimed that HMRC's failure to carry out a statutory review had hindered the company's ability to make its appeal, and applied for costs on an indemnity basis. The judge did not agree that costs were justified; it was apparent that there had been issues in the progress of the appeal from both parties. Both parties would have been better served by seeking a case management hearing rather than relying on a strike-out application to sort these issues out. Nevertheless, HMRC's actions had not been sufficiently unreasonable to justify a costs order against them.

First-Tier Tribunal (TC07558): *H Ripley & Co Ltd*

A company appealed against a notice of requirement to deposit security on 8 February 2019. The appeal was listed for hearing on 22 October 2019; on 21 October the company notified the Tribunal that it wished to withdraw its appeal. On 5 November the company applied to reinstate the appeal, without giving any reasons for withdrawal or the request to reinstate.

Judge Anne Fairpo considered that there is a public interest in the finality of litigation. The merits of the case were not relevant; there would be prejudice to either party in allowing or not allowing reinstatement. On balance, the lack of any reason for the appellant's actions counted against them. An applicant cannot expect relief from the consequences of their actions without providing a good reason. The application to reinstate was refused.

First-Tier Tribunal (TC07602): *De Build Ltd*

An individual appealed against a personal liability notice issued in respect of penalties assessed on two companies of which he was a shareholder and director. The amount charged on him was approximately £6 million; a similar amount was charged against another individual who had been similarly involved with the companies. Each blamed the other for any irregularities that might have occurred, so their appeals would be heard separately.

Judge Barbara Mosedale heard a dispute about the admissibility of various documents, and also whether those documents should be disclosed to the other party. She divided the documents into various categories and ruled most of them to be relevant and admissible, giving indications of how they should be redacted before being shared with the other party. Some documents were only relevant and admissible to the extent that they referred to companies mentioned in HMRC's statement of case.

First-Tier Tribunal (TC07598): *Mark Mitchell*

An appellant applied for an order barring HMRC from taking any further part in the proceedings. This was the second such application; the first, in July 2018, had resulted in directions for HMRC to issue a corrected statement of case and for both parties to serve lists of document and evidence. Failure to comply by 17 August would lead to striking out or barring.

HMRC supplied the statement of case on 31 July and a list of documents on 8 August. The appellant wrote to HMRC on 17 August asking for further documents to be disclosed; HMRC responded that some of these were already on the list, and others were privileged. HMRC subsequently withdrew their objections to disclosing these documents, stating that the officer who believed them to be privileged had made a mistake.

The appellant argued that such a mistake constituted a breach of the unless order, and the result should be barring. The judge examined the arguments in detail and refused the application. He expressed the view that the appeal should now proceed to a full hearing as quickly as possible.

The dispute is about input tax of some £8,000 that HMRC did not consider related to the registered business. The appellant has taken that as an allegation of sham or fraud, and some of the claims that HMRC have no prospect of success relate to the fact that their pleadings are not appropriate to such an allegation. However, no such allegation has been made or is necessary.

First-Tier Tribunal (TC07544): *Daniel Bussau*

A company made a hardship application in relation to a VAT assessment of £6,189 for its periods 12/15 and 03/16. The appellant asserted that a VAT refund of £13,000 and a CIS repayment of £34,958 were due to the company and that it was unable to pay the VAT claimed of £6,189 until HMRC have issued the refund and repayment. HMRC refused the hardship application and the company appealed to the Tribunal.

The Tribunal noted the officer’s response to the application. She had asked for specific information to explain the view that hardship would follow, including a range of accounting information. That information had not been provided; it appeared that a different firm of accountants prepared the management accounts, and HMRC had no authority to deal with them. The accountant who attended the hearing said he no longer acted for the company, but he could not understand why HMRC had not dealt with the matters he had raised when he did.

The judge ruled that there was no reason for HMRC to grant a hardship application when they had received no response to a request for information reasonably required. They could not approach a third party without authority. The application for hardship was refused.

First-Tier Tribunal (TC07638): *ROK Construction and Hire Ltd*

Two companies appealed against a decision by HMRC to refuse to allow VAT group registration. There were two issues in the substantive dispute: whether one of the companies was established in the UK and therefore eligible to be included in a group; and if so, whether it was appropriate for the protection of the revenue to exclude it. There then followed a dispute about disclosure of documents.

HMRC had discussed a disclosure schedule with the taxpayers and it had been presented for approval by the Tribunal; however, the schedule had not been signed, and the judge directed that a short hearing should follow to finalise the agreement. A dispute then followed about what had been agreed, and the parties returned to the Tribunal for directions.

The judge reviewed the state of the argument and the competing contentions of each side, before agreeing that the draft order from the earlier hearing should stand. HMRC had agreed to it at the time, and might have changed their mind subsequently, but they had no good reason for that reversal.

Disclosure was to be made within 5 weeks of the issue of the new decision.

First-Tier Tribunal (TC07642): *Barclays Services Corporation and others*

6.9 Other administration issues

6.9.1 Coronavirus Checklist

As well as the guidance on deferring payment of VAT set out at 6.3.1 above, the government has announced the availability of grants to help businesses with cash flow. These include the Small Business Grants Fund and the Retail, Hospitality and Leisure Grant Fund, and the Self-employment Income Support Scheme. The first two are related to business rates, and will presumably be treated as subject to direct tax as reducing costs; the details of the self-employed grant are so far not complete, but HMRC will contact eligible businesses (those with income of up to £50,000 in the last year or on average over the last three years) in June with details of how to apply. The grant will be taxable as trading income, but cannot be subject to VAT as it will not be consideration for any supply.

www.gov.uk/government/publications/coronavirus-covid-19-business-support-grant-funding-guidance-for-businesses; www.gov.uk/guidance/claim-a-grant-through-the-coronavirus-covid-19-self-employment-income-support-scheme

6.9.2 Promoters of tax avoidance schemes

HMRC have published their tax avoidance strategy to tackle those who promote mass-marketed tax avoidance schemes. The strategy focuses on strengthening HMRC’s powers, disrupting supply chains and deterring taxpayers from taking up schemes. For example, HMRC will put out the following messages to people they believe might enter into avoidance schemes:

- most schemes do not work
- it could cost you more than you bargained for
- you may have to pay significant legal fees
- you could face a criminal conviction

- you could face publicity as a tax avoider
- your scheme is never approved by HMRC
- you could be marked out as a high-risk taxpayer
- HMRC is likely to beat your scheme in court
- the risk is normally all your own
- you'll have to pay the tax upfront anyway

www.gov.uk/government/publications/tackling-promoters-of-mass-marketed-tax-avoidance-schemes/tackling-promoters-of-mass-marketed-tax-avoidance-schemes

6.9.3 Spring Budget

The Budget was delivered on March 11, before all the calculations were thrown out by Covid-19. The VAT measures have been covered elsewhere, but in summary are:

- zero-rating of electronic publications from 1 December 2020;
- zero-rating of women's sanitary protection from 1 January 2021;
- changes to zero-rating of prescription drugs from 1 April 2020 and 1 January 2021;
- implementation of the call-off stock quick fix from 1 January 2020;
- changes to the Agricultural Flat Rate Scheme to operate from 1 January 2021, with new entry (turnover £150,000) and exit (turnover £230,000) rules;
- confirmation that "postponed accounting" will apply to VAT on imports from 1 January 2021.

The Budget measures were reviewed in an article in *Taxation*.

Taxation, 19 March 2020

6.9.4 Finance Bill published

The government has published Finance Bill 2020, containing 105 clauses and 14 schedules, running to 176 pages. The Bill includes a number of measures for which legislation was published in draft on 11 July 2019 and also at the Budget on 11 March 2020. The date for second reading has not yet been announced.

www.gov.uk/government/collections/finance-bill-2020

6.9.5 Liability for VAT fraud

A Scottish-incorporated company provided payroll processing services on behalf of recruitment agencies. In December 2016, HMRC discovered the existence of an alleged VAT fraud: one of the controlling individuals admitted in an interview that he had not accounted for VAT charged and retained. The company had traded for only a year, but it had charged its clients £7.7m in VAT and retained it all. The company and its liquidators took action against six defendants for the return of monies wrongly paid out to them. One of them accepted that it had no entitlement to £322,000

and returned it; two more escaped summary judgment in respect of claims for £1.786 million and £450,000 in an action in the High Court in November 2018, but admitted liability in a further hearing in February 2020. An interim payment was agreed.

The fourth defendant did not appear in the High Court, and in his absence the judge agreed that he had dishonestly assisted with a breach of trust and found him liable for the sums claimed of £1.8 million.

High Court: *Payroller Ltd and another v Little Panda Consultants Ltd and another*

A number of companies entered into transactions connected with fraudulent trading in emissions trading allowances. After HMRC had refused credit for input tax and the companies entered insolvent liquidation, their liquidators sued a subsidiary of RBS (SEEL), arguing that breaches of fiduciary duty by the directors had been dishonestly assisted by traders employed by the bank. The claimants alleged dishonest assistance and knowing participation in fraudulent trading. Two traders employed by RBS SEEL, who caused RBS to buy very large quantities of EUAs from an intermediary called CarbonDesk Ltd. It was alleged that, against a background of rumours of VAT fraud in the emissions trading market, the two traders had clear suspicions from 17 June 2009 about the legitimacy of the very significantly increased volume and nature of the very profitable trading which they were doing with CarbonDesk; but that instead of raising their suspicions with the compliance department at RBS SEEL or with CarbonDesk directly (as the traders later contended that they did), in fact the two traders dishonestly turned a blind eye and carried on trading regardless.

The court decided for the claimants. On the evidence, by 24 June 2009, any reasonably attentive trader would have had the most acute suspicions about CarbonDesk's business, and how it was obtaining a seemingly unending source of large volumes of EUAs to sell to RBS. The traders had not asked questions of CarbonDesk because they had had a clear suspicion that the EUAs which they were being sold were connected with fraud, but they had decided together that it would be best not to ask and thereby risk learning the truth. By continuing to trade with CarbonDesk thereafter, they had acted dishonestly. The bank and its subsidiary were liable for dishonest assistance and knowingly being party to fraudulent trading from 26 June 2009 to 6 July 2009.

High Court: *Bilta (UK) Ltd (in liquidation) and others v NatWest Markets plc and another company*

6.9.6 Fulfilment House Due Diligence Scheme

HMRC have updated their guide *Fulfilment House Due Diligence Scheme – checks and record keeping* with a new e-mail address registered traders must use to inform HMRC of customers not meeting their obligations under the scheme.

www.gov.uk/guidance/carry-out-checks-and-keep-records-if-youre-approved-for-fhdds

HMRC have issued a factsheet *Fulfilment house due diligence scheme: Penalties for offences and contraventions* to set out the new criminal sanction and civil penalties that HMRC may apply from 1 April 2019

where businesses fail to comply with their obligations under the fulfilment house due diligence scheme.

www.gov.uk/government/publications/penalties-for-offences-and-contraventions-against-the-fulfilment-house-due-diligence-scheme

6.9.7 Value Added Tax Bill

Sir Christopher Chope MP is making another attempt to have a Value Added Tax private member's bill passed by the Commons. Its stated aims are to enable the maximum turnover threshold for exemption from the requirement to register for VAT to be raised; to make provision for the exemption of certain goods and services from liability to VAT; and for connected purposes. It was given a first reading on 10 February 2020 and is scheduled for a second reading on 11 September.

https://services.parliament.uk/bills/2019-21/valueaddedtax.html

6.9.8 Updated factsheets

HMRC have updated their factsheet *Unannounced visits for inspections approved by the tribunal*. It explains the background to such visits, and is intended to be given to the subject at the start of the inspection. It contains some important points:

You have the right to seek advice about the inspection, but we will not delay carrying out our inspection while you do this.

If you choose not to allow us to carry out the inspection, we'll charge you a £300 penalty. You might also have to pay further penalties of up to £60 a day until you allow us to carry out the inspection.

It also sets out considerations about people who work from home, and whether the inspectors will need to speak to employees.

CC/FS5

6.9.9 Alcohol Wholesaler Registration Scheme (AWRS)

The AWRS was introduced on 1 April 2016, with the effect that the selling of alcohol wholesale is a controlled activity; persons are prohibited from carrying out that controlled activity unless they are approved by HMRC and registered under the AWRS. Two companies appealed against refusal of registration. The arguments are similar to those that arise in cases about notices requiring deposit of security: HMRC had refused registration on the basis of connections to previous supplies to illicit supply chains, defaulting traders and fraudulent evasion of VAT, as well as bankruptcy owing HMRC unpaid debts.

The Tribunal's jurisdiction was supervisory, so the appellant had the burden of proof to show that the decision had been reached unreasonably. Judge Anne Fairpo went through the various objections raised by the appellants and, with very minor exceptions, found all of them to be short of the required level of proof. The appeals were dismissed.

First-Tier Tribunal (TC07644): *Morgan James Ltd and Exeter Drinks Ltd*

6.9.10 Prosecutions

Five directors of a printing and mailing business who attempted to conceal sales of more than £3 million in a bid to avoid paying tax have been jailed for a total of 11 years. Their printing business generated a great deal of waste paper and scrap aluminium, which they sold to a recycling business and pocketed the proceeds. The fraud was perpetrated between 2004 and 2012.

www.cps.gov.uk/cps/news/five-directors-jailed-hiding-payments-avoid-paying-ps26-million-tax

HMRC have published a review of their prosecution activities in 2019. HMRC's fraud investigations have led to more than 600 individuals being convicted for their part in tax crimes and commenced new criminal investigations into more than 610 individuals. The Fraud Investigation Service continues to bring in around £5 billion a year through civil and criminal investigations.

www.gov.uk/government/news/busted-hmrc-reveals-biggest-criminal-cases-of-year-2019