VAT UPDATE
JULY 2022

Covering material from April – June 2022

Notes prepared by Mike Thexton MA FCA CTA (Fellow)

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

VAT Update July 2022

Contents

1. INTRODUCTION....1
  1.1 Appeals pending....1
2. OUTPUTS....3
  2.1 Scope of VAT: linking supplies to consideration....3
  2.2 Disbursements....11
  2.3 Exemptions....11
  2.4 Zero-rating....24
  2.5 Lower rate....26
  2.6 Computational matters....26
  2.7 Discounts, rebates and gifts....26
  2.8 Compound and multiple....27
  2.9 Agency....29
  2.10 Second hand goods....29
  2.11 Charities and clubs....29
  2.12 Other supply problems....29
3. LAND AND PROPERTY....32
  3.1 Exemption....32
  3.2 Option to tax....32
  3.3 Developers and builders....35
  3.4 Input tax claims on land....35
4. INTERNATIONAL SUPPLIES....37
  4.1 E-commerce....37
  4.2 Where is a supply of services?....37
  4.3 International supplies of goods....44
  4.4 European rules....50
  4.5 Foreign refund reclaims....57
5. INPUTS....59
  5.1 Economic activity....59
  5.2 Who receives the supply?....59
  5.3 Partial exemption....59
  5.4 Cars....66
  5.5 Business entertainment....67
  5.6 Non-business use of supplies....67
  5.7 Bad debt relief....67
  5.8 Other input tax problems....67
6. ADMINISTRATION AND PENALTIES....68
  6.1 Group registration....68
  6.2 Other registration rules....68
  6.3 Payments and returns....70
  6.4 Repayment claims....72
  6.5 Timing issues....76
  6.6 Records....76
  6.7 Assessments....79
  6.8 Penalties and appeals....80
  6.9 Other administration issues....87

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 latest update to the HMRC website appeared on 25 May 2022.

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

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

- *Beigebell Ltd*: HMRC succeeded in appeal (covered in July 2020 update) against the FTT decision that a company's directors did not have the means of knowledge of the connection of their company's transactions to a missing trader fraud: case remitted to a differently constituted FTT.
- *DCM (Optical Holdings) Ltd*: the taxpayer has been granted leave to appeal against the Court of Session's decisions in favour of HMRC (hearing 8 February 2022, decision awaited).
- *Gray & Farrar International Ltd*: HMRC have been granted leave to appeal against the UT decision in the company's favour on place of supply (the UT refused leave, but a direct application for leave to the CA succeeded).
- *Hippodrome Casino Ltd*: HMRC are seeking permission to appeal the FTT decision in the company's favour.
- *Hotel La Tour Ltd*: HMRC have been granted permission to appeal the FTT decision in the company's favour on the deductibility of the incidental costs of selling a subsidiary.
- *Mid-Ulster District Council*: HMRC have been granted leave to appeal on particular points against the FTT's decision on local

authority sports provision (on the distortion of competition issue). UT hearing May 2022.

- *Netbusters (UK) Ltd*: HMRC have been granted leave to appeal to the UT against the FTT decision that the company's provision of sporting facilities was exempt (hearing May 2022).
- *News Corp UK & Ireland Ltd*: the company has been granted leave to appeal to the Supreme Court against the CA's decision that its digital newspapers did not qualify for zero-rating before the law was changed on 1 May 2020 (listed for hearing November 2022).
- *NHS Lothian Health Board v HMRC*: Court of Session allowed taxpayer's appeal on grounds that "no repayment" had to be the wrong answer; remitted to FTT for reconsideration of the amount; HMRC have been granted leave to appeal to the Supreme Court (hearing June 2022).
- *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).
- *Revive Corporation Ltd*: MTIC case remitted by the UT to the FTT for rehearing.
- *The Prudential Assurance Company Ltd*: FTT decision in company's favour in the July 2021 update. HMRC granted permission to appeal to the UT (hearing listed for November 2022).
- *Thorsteinn Gardarsson t/a Action Day A Islandi*: HMRC succeeded in their appeal against the FTT decision that a trader's products qualified as "books" rather than "stationery", and some issues have been remitted to a differently constituted FTT for further consideration (no longer on HMRC's list).

1.1.1 Decisions in this update

Although there are many decisions in this update, none of them have previously been listed on HMRC's website as outstanding.

- *Chelmsford City Council*: HMRC's appeal against the FTT's decisions on local authority sports provision dismissed by the UT; cross-appeal would also have been dismissed if relevant.

2. OUTPUTS

2.1 Scope of VAT: linking supplies to consideration

2.1.1 Change of policy on business tests

HMRC have issued a Brief to explain a change of policy in relation to the criteria for deciding whether an entity is carrying on a business activity. They will no longer use the long-standing "Lord Fisher tests" that led to the decisions on charitable nurseries and creches in *Yarburgh Children's Trust* and *St Paul's Community Project*; instead, they will use the tests considered appropriate by the Court of Appeal in *Wakefield College*.

The Brief is important, so the full text is reproduced below.

Purpose of this Brief

This brief explains how HMRC now approaches determining whether or not an activity is a business activity for VAT purposes.

HMRC previously accepted that where a charity supplies nursery and crèche facilities for a consideration that is fixed at a level designed to only cover its costs, this is not a business activity for business purposes. This was based on the courts' decisions in Yarburgh Children's Trust [2002] STC 207 and St Paul's Community Project [2005] STC 95. Details on this are set out in Business Brief 02/05: VAT — Supplies of nursery and crèche facilities by a charity.

Recent court cases have provided further clarification on how to determine whether or not an activity is a business activity. In determining this, there should be no reliance on an organisation's overall objective or profit motive.

Who needs to read this

You should read this brief if you are:

- *a charity organisation*
- *a non-profit making organisation*
- *business providing nursery and crèche facilities*
- *a business that receives grants or subsidies*
- *an organisation or a business carrying out non-business activities*

Background

Historical cases

The principles laid down in the cases of Lord Fisher [1981] STC 238 and Morrison's Academy Boarding Houses Association [1978] ('Morrison's Academy') have historically been used to decide whether an activity is business or economic activity for VAT purposes. The 6 criteria that emerged from both cases, known as the 'business test', include:

- *is the activity a serious undertaking earnestly pursued*
- *is the activity an occupation or function that is actively pursued with reasonable or recognisable continuity*

- *does the activity have a certain measure of substance in terms of the quarterly or annual value of taxable supplies made*
- *is the activity conducted in a regular manner and on sound and recognised business principles*
- *is the activity predominately concerned with the making of taxable supplies for a consideration*
- *are the taxable supplies that are being made of a kind which, subject to differences of detail, are commonly made by those who seek to profit from them*

In Yarburgh Children's Trust [2002] STC 207 and St Paul's Community Project [2005] STC 95, the courts held that the activities of both charities did not constitute a business. This was due to them not being predominantly concerned with the making of taxable supplies for a consideration when they provided nursery and crèche facilities at a fee that only covers the cost of providing the services.

More recent judgments have helped to clarify that these criteria are only indicators and they cannot replace the principles set out by the courts in determining what constitutes a business.

Decisions in recent cases

The Court of Appeal in Longridge on the Thames [2016] BVC33 emphasised that the correct test for determining whether an activity is a business activity is whether there is a direct link between the services or goods supplied and the payment received by the supplier. The 'predominant concern' is irrelevant. This means focusing on whether there is a direct link between the services the recipient receives and the payment made rather than on the wider context of the organisation's charitable objectives or motive.

The court established that where an organisation is involved in a range of activities, it is appropriate to look at each activity separately and then identify which of them amount to business activity and those that do not. It would not be appropriate to settle for just an aspect of the activities by reference to their predominant concern or predominant activity. It is the nature of the activity that is to be considered and not whether the activity is predominant or not.

In Wakefield College [2018] BVC 22, the Court of Appeal considered whether the activities were business activities for VAT purposes based on a 2-stage test.

The 2-stage tests are:

Stage 1: The activity results in a supply of goods or services for consideration

This requires the existence of a legal relationship between the supplier and the recipient. The first step is to consider whether the supply is made for a consideration. An activity that does not involve the making of supplies for consideration cannot be business activity for VAT purposes.

The Court of Appeal in Wakefield emphasised that a 'supply for consideration' is a necessary condition but not a sufficient condition for an 'economic activity'.

Stage 2: The supply is made for the purpose of obtaining income therefrom (remuneration)

Where there is a direct or sufficient 'link' between the supplies made and the payments given, the activity is regarded as economic. The Court in Wakefield College [2018] made a distinction between consideration and remuneration. Simply because a payment is received for a service provided does not itself mean that the activity is economic. For an activity to be regarded as economic it must be carried out for the purpose of obtaining income (remuneration) even if the charge is below cost.

Changes to HMRC's Policy

HMRC's long-standing policy has been that a business activity is possible even in the absence of a profit motive.

In light of the recent cases, as set out in this brief, HMRC will no longer apply the business test based on the 6 indicators from Lord Fisher and Morrison's Academy in determining whether an activity is business.

The 2-stage test given in this brief, is the approach that should be taken in determining whether an activity constitutes a business activity.

Businesses can no longer rely on the old 'business test' to decide whether an activity is business or not, but it can be used as a set of tools designed to help identify those factors which should be considered.

The Brief does not give a time-frame for the operation of the new policy, or comment on whether it affects past rulings.

Revenue & Customs Brief 10/2022

The *VAT Business/Non-business Manual* has been extensively updated to reflect the new policy. New pages have been added to explain that the definition given in VATA 1994 s.94 is not exhaustive, and the concept of "business" for VAT may differ from its meaning in other tax contexts. For example, rental income is not generally considered "business" for income tax or inheritance tax, but it is for VAT.

VBNB15000, VBNB20100

The guidance has also been expanded to cover the new emphasis on whether activities are for the purpose of generating income, the situation in which a taxpayer has more than one activity (each must be tested separately), and the way in which VAT on costs should be apportioned between business and non-business use.

VBNB30200, VBNB30400, VBNB30500

2.1.2 Local authority sports facilities

In TC07909: *Chelmsford City Council*, TC07910: *Midlothian Council*, and (TC07911): *Mid Ulster District Council (formerly Agherafelt District Council)* the FTT had to consider the VAT liability of charges paid by members of the public for access to sports and leisure facilities provided by local authorities. Lead cases were designated for each part of the UK, and a panel of three judges (Peter Kempster, Anne Scott and Alastair Rankin) heard the appeals. The first of these cases has now proceeded to the Upper Tribunal.

First-Tier Tribunal

Chelmsford City Council's claim for a repayment of £0.9m was made in December 2010 and rejected by HMRC. The Council contended that the charges in dispute did not attract VAT on three alternative grounds:

(1) Its supplies of sporting and leisure activities to members of the public are not "economic activities", and are therefore outside the scope of VAT;

(2) Its supplies of sporting and leisure activities to members of the public are provided by the Council in its role as a public authority acting under a special legal regime, and therefore it is not a taxable person in respect of those supplies; or

(3) Its supplies of sporting and leisure activities to members of the public are provided by the Council in its role as a public authority, and therefore it is not a taxable person in respect of those supplies, by virtue of Note 3 Group 10 Sch.9 VATA 1994.

In HMRC's view, the supplies were properly chargeable to output tax; the claim to recover output tax accounted for, while retaining the VAT on costs previously claimed because s.33 VATA would apply, was not justified.

The precedent case law cited to the Tribunal was very extensive, and evidence was taken on the wide range of facilities provided by the council to the public. One of the key precedents was *London Borough of Ealing v HMRC* (Case C-633/15), in which the CJEU had held that council sports facilities were within the scope of the exemption at art.132(1)(m) PVD. The appellants argued that the question of whether they were within the scope of VAT at all was a prior question, and relied on arguments based on art.9 and 13 rather than the *Ealing* decision. The application of *Ealing* might result in a repayment of output tax, but might also have negative consequences for some councils which had been able to disregard their exempt activities as insignificant in making s.33 claims. However, Chelmsford City Council reserved the right to rely on art 132(1)(m) if it lost the current appeal.

The Council accepted that it was making supplies for a consideration within art.2 PVD, but not that it was a "taxable person acting as such". The argument was based on the CJEU decision in *Gemeente Borsele* (Case C-520/14) and the Court of Appeal's judgment in *Wakefield College*. The Council argued that its provision of facilities did not constitute "participation in the market" for a number of different reasons, including the level of net expenditure, the provision of free services, and HMRC's acceptance that provision by outsourcing to a third party (as in *Edinburgh Leisure*) was non-economic, allowing a s.33 claim in respect of the third party's charges.

HMRC responded with detailed arguments on the principles to be derived from *Borsele* and other cases, and also on the application of the rules on whether the Council was acting "under a special legal regime".

The judges considered the precedents in detail, and made the following decision on the "article 2 argument":

113. We consider that the relevant factors in the current appeal for the purposes of arts 2 and 9 are as follows, and we give our findings on each:

(1) The supply to local residents of facilities for leisure, sporting and physical recreation is a core activity of the Council. See the evidence of

Mr Lyons ([21(20b)] above) and Mr Reeves ([22(5)] above). That is in contrast to the provision of school transport by the municipality in Geemente Borsele, and the provision of legal aid by the public office in Finland, which in each case was very much ancillary to the respective body's principal activities.

(2) The number of customers and the total revenue raised by the Council for the supply of facilities for leisure, sporting and physical recreation are both significant. See the evidence of Mr Lyons ([21(20a & 20c)]) above) and Mr Reeves ([22(5) & (6)] above). The CJEU in Geemente Borsele said (at [31]) it was relevant to look at "the number of customers and the amount of earnings."

(3) Although concessionary fees are available to qualifying users, (almost) all users pay something for use of the facilities. In contrast, in Geemente Borsele (at [33]) only one-third of transport users paid contributions, and in Finland (AG Opinion para [50]) only 34% of users paid any contributions.

(4) Although the cost of providing the facilities exceeds the fees received from users, the fees do make a significant contribution to the costs of provision. Fees collected accounted for around one third of costs - see the evidence of Mr Lyons ([21(20a)] above) and Mr Reeves ([22(18b)] above). That is in contrast to the position in Geemente Borsele (at [33]) where the charges covered only 3% of costs, and in Finland (at [50]) where the charges covered only around 8% of costs. It is more in line with the situation in Wakefield College where, after noting (at [75]) that in both Geemente Borsele and Finland "the total amount raised by charges was insubstantial, both in absolute terms and relative to the cost of the service", the Court of Appeal (at [82]) stated: "the subsidised fees made a significant contribution to the cost of providing courses to the students paying those fees, to the extent of some 25–30%."

(5) The fact that the Council does not aim (and has never aimed) to break even (let alone make a profit) on the provision of the facilities does not matter. That is a subjective factor only and must be ignored - see, for example, Wakefield College at [55], Longridge at [84], and Lajvér at [35].

(6) The fact that many users pay concessionary rates does not matter. Per Arden LJ in Longridge (at [93]): "The concessionary charges were also not an indicator against the existence of an economic activity because the economic activity springs from the receipt of income, not profit."

(7) The fact that the costs of providing the facilities for leisure, sporting and physical recreation are subsidised in large measure by grants from UK central government (see the evidence of Mr Lyons ([21(13)] above) and Mr Reeves ([22(11)] above)) does not matter. Per the CJEU in Lajvér (at [38]):

"… the fact that the investments were largely financed by aids granted by the Member State and the European Union cannot have a bearing on whether or not the activity pursued or planned by the applicants in the main proceedings is to be regarded as an economic activity, since the concept of "economic activity" is objective in nature and applies not only without regard to the purpose or results of the transactions concerned but

also without regard to the method of financing chosen by the operator concerned, which also holds true in relation to public subsidies."

(8) The fact that the leisure, sporting and physical recreation facilities are provided in fulfilment of statutory duties does not matter. Per the CJEU in Finland (at [40]):

"It must first of all be stated that, in view of the objective character of the term 'economic activities', the fact that the activity of the public offices consists in the performance of duties which are conferred and regulated by law, in the public interest and without any business or commercial objective, is in that regard irrelevant."

114. Taking together all those factors and our findings, we conclude that the provision of the leisure, sporting and physical recreation facilities by the Council constitutes the supply of services for remuneration, and thus that supply constitutes economic activity within art 9 PVD.

The judges therefore agreed with HMRC in respect of the first issue. Turning to the question of whether the Council was acting under a special legal regime, the main precedents were *Fazenda Publica v Camara Municipal do Porto* (Case C-446/98) and *Saudacor* (Case C-174/14). It was clear from those cases, and the other authorities cited to the judges, that the decision whether art 13 applies in particular circumstances is highly fact-specific. The judges derived the following principles from the precedents:

128. In determining whether an activity is being engaged in under a special legal regime, the following factors are irrelevant:

(1) the subject matter of the activity (Fazenda Pública at [19]);

(2) the purpose of the activity (ibid); and

(3) the fact that private providers carry out similar activities (Isle of Wight at [33]).

The judges considered that the situation of the sporting facilities was similar to that of the waste management services that were held to be outside the scope of VAT in *The Durham Company*; even though the relevant provision gave councils a power to provide sporting facilities rather than a duty, nevertheless that was enough to constitute a special legal regime.

Nevertheless, it was then necessary to analyse all the conditions laid down by national law for the Council's provision of sports and leisure facilities, to determine whether that activity was being engaged in under a special legal regime applicable to bodies governed by public law or under the same legal conditions as those that apply to private economic operators. Based on the witness evidence about the Council's corporate plans and policies, the judges were satisfied that the conditions applicable to the different providers were significantly different. The first paragraph of art.13 was therefore engaged.

It was then necessary to consider whether this would lead to significant distortions of competition, which would require the supplies to be brought back within the scope of VAT. Both parties accepted that this would require further evidence, and the judges granted leave to apply for a continuation hearing.

As the Tribunal had heard full argument on the "Note 3 issue", the decision included consideration of the question, even though it was only relevant to the outcome if the Council was not operating under a special legal regime. VATA 1994 Sch.9 Group 10 Note 3 states that a local authority is not to be treated as an eligible body for the purposes of the exemption. Before the *Ealing* case, this was believed to require local authorities to charge output tax on sporting supplies if they were supplied for consideration; the exclusion from exemption meant that they were entitled to a s.33 claim if there was no consideration. The judges commented that the reference to the CJEU in *Ealing* was based on a mistaken premise, that Note 3 related to the art.133 conditions on distortion of competition. In the Council's view, the effect of Note 3 was to exercise a derogation allowed by art.13(2), confirming that the otherwise exempt activities were to be regarded as being engaged in by the Council as a public authority; and the result was that the Council had no economic activity.

The judges considered the *Ealing* decision in some detail, and rejected the Council's representation of it. The decision had concluded that Note 3 was ineffective, with the result that local authorities were eligible bodies and their supplies (if within the scope of VAT) were exempt. It was not correct to reinterpret Note 3 in a different way to implement a derogation under art.13(2).

Summing up on *Chelmsford*, Judge Kempster concluded that:

- the Council's argument based on art.2 was rejected;
- the Council's argument based on art.13(1) was accepted, subject to further consideration of whether this would lead to a significant distortion of competition.

The decision on Midlothian Council followed the same structure, with different evidence but the same consideration of precedent and principle. The same conclusions were reached.

The decision in relation to Mid Ulster District Council was different. After coming to the same conclusions on art.2 and the first part of art.13, the judges relied on evidence about the special rules requiring fairness between the two communities in Northern Ireland, the promotion of integration and countering all forms of social deprivation. Only local authorities were in a position to meet these obligations; the Tribunal was satisfied that there was no non-negligible alternative provision in Northern Ireland, and therefore no real or potential risk of distortion of competition. The Council's appeal was allowed.

Upper Tribunal

HMRC appealed on the "special legal regime" issue; Chelmsford City Council (CCC) cross-appealed on the "Note 3" issue. It withdrew a separate appeal on the "article 2" issue shortly before the UT hearing. The case came before Mrs Justice Joanna Smith and Judge Swami Raghavan.

On the first issue, HMRC argued that the FTT had erred in law in applying the test laid down in case law for identifying a special legal regime. They argued that the "generic conditions" under which CCC operated were not sufficient to put it in a different position to the Irish

local authorities considered by the CJEU in *Commission v Ireland* (Case C-554/07) and that if any of those conditions was enough to transform the power in s.19 LGMPA into a special legal regime, then the same would equally be true of all local authority powers, an outcome which would be directly contrary to the decision in the *Ireland* case.

HMRC also sought to advance an additional argument, that the CJEU has drawn a distinction between a public body being authorised to carry on an activity (so it falls within its remit) and the use of powers specifically to exercise that activity, such as rule-making or penalty imposition. HMRC argued that this distinction was consistent with the requirement to interpret derogations (such as art.13(2)) strictly.

The UT went through a number of CJEU precedents in some detail, before summarising the propositions that were agreed to be established by these cases:

(1) Art.13(1) PVD derogates from the general rule in providing for circumstances in which local government authorities will not be regarded as taxable persons. Given that it is a derogation, it must be interpreted strictly (*Isle of Wight* at [60]);

(2) The task of the national court is to "analyse all the conditions laid down by national law for the pursuit of the activity in issue…to determine whether that activity is being engaged in under a special legal regime applicable to bodies governed by public law or under the same conditions as those that apply to private economic operators" (*Fazenda* at [21]);

(3) The subject matter and purpose of the activity are not relevant (*Fazenda* at [19]).

(4) Authorisation by statute alone is not enough. Something more is required (*Commission v Ireland* at [49]).

The UT examined and rejected six arguments put forward by HMRC's counsel in support of the contention to that a special legal regime only applied where the council used "sovereign powers" such as making rules or levying penalties. The judges stated that "if the Court was seeking to lay down a hard-edged test, along the lines for which Mr Hill contends, it is to be expected that it would do so explicitly." The fact that counsel had to rely on interpretation and parts of A-G's opinions that were not adopted by the full court suggested that this was not the court's intention.

The UT went on to consider the way the FTT reached its decision on this issue. It approved the FTT's approach, which was to identify the legal regime that applied (s.19 LGMPA) and then to consider whether that met the conditions to be regarded as "special" for this purpose. The reasoning, and HMRC's criticism of it, was examined at length, and the UT concluded that there was no error of law. Even if they were wrong in that conclusion, the judges considered that they would have come to the same decision if they had to set aside the decision below and remake it: there were sufficient elements deriving from national law reflected in the council's policies on sports provision to justify the conclusion that a special regime applied. No private operator would be subject to the same conditions.

As HMRC had failed to overturn the decision below, strictly it was not necessary for the UT to decide on the cross-appeal. However, as the

judges had heard argument, they dealt with it briefly. They described the legal background as "complex", and set out an explanation of the *Ealing* decision and its consequences.

The central issue was whether Note 3 implemented art.13(2), as CCC contended, or was a failed implementation of art.133(d), as HMRC contended. In either case there would be no output tax, but it would make a difference to the council's entitlement to claim VAT refunds. The UT agreed with HMRC that CCC's arguments on this issue were not well founded. The council could not rely on the principle of conforming interpretation because art.13(2) gives Member States an option, not an obligation. The plain intention of Parliament in enacting Note 3 was to make these supplies exempt, and the CJEU had held it to be ineffective as an incorrect implementation of art.133(d). There was no authority to suggest that a national court should or could then try to find another basis in the Directive for giving it effect. If it had mattered, the UT would have dismissed CCC's cross-appeal.

The overall conclusion was that HMRC's appeal was dismissed.

Upper Tribunal: *HMRC v Chelmsford City Council*

2.2 Disbursements

Nothing to report.

2.3 Exemptions

2.3.1 Financial exemption

Advocate-General Medina has given an opinion in a case referred by the Polish court in relation to a sub-participation agreement which is described as follows:

Investment fund A pays bank B an upfront amount upon conclusion of that agreement. In return for that payment, bank B ('the originator'), which has lent money to C ('the principal debtor'), agrees to pay investment fund A ('the sub-participant') the proceeds obtained by the originator under the original loan agreement with the principal debtor. While the cash flow and the risk are removed from the originator's balance sheet and transferred to the investment fund concerned in the present case, the originator maintains legal ownership of the assets.

The question is whether the services provided by the investment fund constituted "the granting of credit" within PVD art.135(1)(b). The A-G considered that the question raised important issues for financial transactions in general, and the case was therefore "of a sensitive nature".

The applicant in the case asked for a tax ruling that its transactions were exempt. In 2015 the Polish Minister for Finance ruled that they did not fall within any of the available exemptions and were therefore subject to the standard rate of 23%. The company's appeal against the ruling was allowed by the court of first instance in Poland, but on a further appeal by the tax authority, questions were referred to the CJEU.

The issues, according to the referring court, were the balance between features of the arrangement that resembled a straightforward loan, and features that did not: on the one hand, it was clear that the economic purpose and effect of the arrangement was to provide liquidity to the originator by the advance of funds that would be paid back later; on the other hand, the source of the repayment was specifically defined, and if the original debtor did not pay, the sub-participant had no recourse against the general assets of the originator.

The A-G noted that, because the ruling related to future rather than past transactions, the descriptions in the order for reference were in more general terms than might otherwise be expected, and he considered that some information was missing. It would be necessary for the referring court to determine the exact nature of the transaction at issue.

The A-G started by discussing whether there was a supply for consideration within art.2 PVD. There was a legal relationship between the sub-participant and the originator; the reciprocal consideration was the upfront payment by the sub-participator and the promise of future repayments by the originator. The sub-participant's remuneration for the transaction is the difference between the upfront amount it has paid and the amount of the proceeds of the receivables that the originator transfers to the sub-participant.

The A-G noted two precedent cases on acquisition of debts: *MKG-Kraftfahrzeuge-Factoring GmbH* (Case C-305/01), in which the acquisition of debts without recourse to the original creditor was held to be a business activity and taxable as debt collection; and *GFKL Financial Services AG* (Case C-93/10), in which the purchase of defaulted debts at a price below their face value (in the hope of recovering more than was paid) was held not to constitute a supply of services and therefore not an economic activity for VAT purposes.

The *GFKL* case was not a comparable situation, because the debts were neither acquired nor defaulted. The originator remained the principal debtor's creditor, and the sub-participant acquired the right to future cash flows, not the debt itself. The A-G considered that the sub-participant's assumption of risk, as well as the provision of liquidity, in the context of a continuing relationship between the parties, confirmed that this was a supply for consideration and within the scope of VAT.

The A-G went on to analyse the exemption for the granting of credit in detail. According to precedent, there must be two cumulative elements satisfied: capital and remuneration for making that capital available, without which the exemption does not apply. Although the "remuneration" in this case was the difference between the amount advanced and the amount recovered, rather than interest, the A-G considered that the economic objective of the transaction involved the advancing of credit.

However, the transfer of risk was an additional element that had to be regarded as part of a single complex transaction. Neither the advancing of credit nor the transfer of risk could be regarded as ancillary or principal elements of the supply. As the transfer of risk was not mentioned in art.135(1)(b), it was necessary to consider the scheme of the exemption to decide whether such a transaction fell within its scope.

The A-G compared the various different transactions described in art.135(1)(b) to (f), and concluded that the transfer of risk was part of the later transactions (involving securities and investments) but not part of the "more traditional" credit operation described in art.135(1)(b). After further referring to EU law on securitisation and the underlying purpose of the financial exemptions in the PVD, the A-G gave an opinion that the transactions in this case should not be regarded as falling within the exemption: the transfer of risk was an essential element of the supply, and it was not covered by art.135(1)(b).

CJEU (A-G) (Case C-250/21): *SzefKrajowej Administracji Skarbowej v O. Fundusz lnwestycyjny Zamknięty reprezentowany przez O S.A*

2.3.2 Insurance supplies

A UK-based insurance intermediary specialised in providing travel insurance for people over the age of 50. It received certain insurance-related supplies of services from a connected Gibraltar-based company. In 2016 HMRC decided that these supplies should be subject to a reverse charge, and on 26 January 2017 an assessment was raised for £7.9 million covering a single period from 1 April 2009 to 31 March 2015. At the same time, HMRC registered the company with effect from 1 April 2009, and charged a belated notification penalty of £1.2 million (15%). Later HMRC decided to reduce the penalty, and asked the Tribunal to mitigate it to £216,000 (about 2.75%).

The company appealed against the assessment and the penalty, and the case came before Judge Anne Redston. She summarised the issues as follows:

(1) whether the Tribunal had the jurisdiction to hear the appeal against the Assessment, as Staysure made a VAT return after it had filed its Notice of Appeal;

(2) whether Intervest's supplies to Staysure were exempt or standard rated;

(3) whether the Assessment was out of time; and

(4) whether to uphold, cancel or mitigate the Penalty.

Summary

The first issue was relatively straightforward. The company had not filed a VAT return at the time it lodged its appeal against the assessment, which invalidated that Notice of Appeal in accordance with VATA 1994 s.83(1)(p)(i). The later filing of a VAT return could not validate the Notice. However, the company applied for leave to appeal out of time, and HMRC did not object.

The second issue involved determining the nature of, and therefore the liability of, the supplies. The Gibraltar company (I) was contractually obliged to provide insurance leads to Staysure and was paid only when a lead resulted in a concluded sale. The judge concluded that I's services were within the insurance exemption, essentially because they were linked to essential aspects of the work carried out by Staysure, namely the finding of prospective clients and their introduction to the insurer with a view to the conclusion of insurance contracts. That was enough to decide the matter in favour of the taxpayer. The decision goes on to set out the

detailed reasoning on this and the other issues, as requested by both counsel in case HMRC appeal.

On the time limit issue, the decision is novel, important and striking. HMRC have always believed that their power to nominate a long return period under SI 1995/2518 reg.25(1)(c) effectively allows them to assess an unregistered taxpayer without time limit – the registration is backdated to the date HMRC can show liability first arose, the registration period runs up to the decision to register, and the time limit to assess that period runs from the end of that period, not the beginning or any particular date within it. The company argued that this could not be right: "prescribed accounting period" in s.73(6) refers to a three-month period. The long return period should be divided into three-month periods, and the time limit should be applied to each of them. The judge reviewed the case law, none of which was binding. On her own consideration of the interpretation of the statutes, she preferred the taxpayer's argument, and would have allowed the appeal on that basis as well.

If the judge was correct on liability, the penalty would fall away. However, if she was wrong on liability, the penalty would still be valid, even if the assessment was not. She therefore considered whether the company had a reasonable excuse, and concluded that it did not: although it was argued that the owner had taken professional advice and had genuinely believed that the supplies were exempt, there was no evidence as to when the advice had been taken, from whom, on the basis of what information or whether it was in any way caveated. There was therefore insufficient evidence to conclude that the company had a reasonable excuse. The judge considered that the penalty, if it was due, should be mitigated further to £159,171 (2%) to reflect the company's cooperation during a long enquiry.

Details

The judge set out the history of the company and the dispute. I had started to make supplies to S on 1 January 2009. The services were regarded as exempt, and S was not registered for VAT. On 1 April 2015 the businesses reorganised, and the services were then treated as standard rated; S registered with effect from that date.

HMRC started enquiring into the services in December 2013. The company continued to correspond with HMRC after the decision in October 2016 and the assessment in January 2017; after HMRC refused to carry out a statutory review of the assessment because no return had been filed for the period, the company at last filed a return for the period showing VAT payable as NIL and total inputs of £40 million. Case management hearings followed, and HMRC did not object to the appeal on the grounds that the return had not been filed until after the appeal notice; in their skeleton argument for the substantive hearing, they explicitly stated that they had no objection, on the grounds that a return had now been filed. The judge considered the principles of allowing late appeals from *Martland*; the length of the delay (over four years) was clearly serious and significant, but the reasons included both HMRC and the Tribunal proceeding with case management without flagging the issue. The judge considered that the required balancing exercise favoured granting permission to make the late appeal.

The judge next described the nature of the business, including the role of I in generating business for S, and how it was remunerated. She reviewed the relevant case law on what constitutes a single service, and what constitutes an insurance-related service, and summarised the principles she derived from the cases as follows:

(1) Whether or not a person is an insurance broker or an insurance agent depends on what they do. How they choose to describe themselves or their activities is not determinative (Insurancewide.com at [85(3)]).

(2) It is not necessary for a person to be carrying out all the functions of an insurance agent or broker for the exemption to be satisfied (Insurancewide.com at [85(8)]).

(3) However, it is essential that the person has a relationship with both the insurer and the insured party (Taksatorringen) but this does not need to be a contractual relationship (Beheer, confirmed in Insurancewide.com at [80]).

(4) The requirement that the person has a relationship with the insurer is satisfied where the person is the subcontractor of a broker, which in turn has a relationship with the insurer (Aspiro at [37]).

(5) Where the person is a subcontractor of a broker, the exemption is satisfied:

(a) where the relationship with the customer is indirect (Aspiro at [37]; Q-GmbH at [37]), or where the subcontractor is one of a chain of persons bringing together an insurance company and a potential insured (Insurancewide.com at [85]); but

(b) the subcontractor's services must be linked to the essential aspects of the work of an insurance broker or agent, namely the finding of prospective clients and their introduction to the insurer with a view to the conclusion of insurance contracts (Andersen at [36]; Insurancewide.com at [85(7) and Aspiro at [39]).

The judge's conclusion that I's services were those of an insurance broker or agent are important, as this is a borderline that has been argued many times. She agreed with the taxpayer's representative for the following reasons:

(1) The provision of leads is Intervest's primary obligation under the Contract. Its other obligations were integral parts of that same obligation: the quote service filtered the leads; the process of generating the leads had to be managed so as to fit with Staysure's available resources, and it also provided opportunities for further product development.

(2) Almost all the sales made by Staysure were directly or indirectly the result of the Website, which was owned and operated by Intervest.

(3) The nature of the supply can also be seen from the way Intervest is remunerated: it is paid only when a lead generates an insurance contract. Intervest did not charge Staysure the costs it incurred for advertising, marketing, webhosting, or the development and operation of the quote engine.

Counsel for HMRC argued that I provided marketing, advertising and the operation of the website, and these were the predominant nature of its

supplies. The judge rejected this, holding that the "view of the typical consumer" would be that the company supplied "qualified leads" rather than advertising. It used advertising to generate those leads, but that was not what it supplied to S. The judge also rejected HMRC arguments based on the fact that I only sold S's products rather than giving advice (as Insurancewide did) and was acting as an undisclosed agent effectively invisible to the customer.

In conclusion, she decided that the services constituted a single supply which was within the exemption, and that determined the appeal in favour of the taxpayer.

In case she was wrong on that, she went on to consider the issue of the time limit, which has much wider possible implications. It was common ground between the parties that there was no binding authority directly on the question. The time limit comes from VATA 1994 s.73(6), which refers to "the end of the prescribed accounting period". HMRC explicitly disclaimed reliance on the one year limit from "knowledge of the facts" in s.73(6)(b), presumably because they accepted that they had known all the facts for more than a year before the issue of the assessment in January 2017.

SI 1995/2518 reg.25 defines return periods as 3 months long by default, but allows for the first return to begin on the effective date of registration, and allows the Commissioners to vary the length of periods and their start and end dates where they consider it necessary in a particular case. The assessing officer confirmed that it was HMRC's normal practice to issue assessments based on a single long return period where a trader was registered retrospectively. She said she had previously worked in the Registration section and had never seen a case where HMRC had acted differently.

The judge reviewed domestic case law on time limits and return periods in chronological order, followed by the single EU authority (*Test Claimants in the Franked Investment Income Group Litigation v HMRC* (Case C-362/12)), discussing her view of the significance of each one. The CJEU ruled: "*according to settled case-law, the principle of legal certainty, the corollary of which is the principle of the protection of legitimate expectations, requires that rules involving negative consequences for individuals should be clear and precise and that their application should be predictable for those subject to them (see, inter alia, Case C-17/03 VEMW and Others [2005] ECR I-4983, paragraph 80). As has been observed in paragraph 33 of this judgment, limitation periods must be fixed in advance if they are to serve their purpose of ensuring legal certainty.*" Counsel for the company argued that HMRC's use of long accounting periods undermined the legal certainty that Parliament had intended by introducing time limits in the legislation.

The judge said she found this a difficult question: "*On the one hand, it is clear from the CJEU's judgment at [44] that that rules involving negative consequences for individuals should be clear and precise and their application should be predictable for those subject to them, and it is also clear that this applies to limitation periods. On the other hand, I agree with Mr Mantle that a person who has failed to register is not in the same position as the appellants in FII Test Claimants, who had not breached*

any legal requirement and plainly had a right to rely on the principles of EU law."

The judge reasoned that Parliament could not have intended for there to be effectively no time limit where a trader had not registered: if that was the intention, the 20-year time limit in s.77 would be meaningless. She concluded that the statutory references to "prescribed accounting period" must mean periods of three months, and a long accounting period designated under reg.25 consisted of a succession of such three-month periods. The time limits in s.73 were directly linked to those in s.77. Although HMRC had discretion to vary the length of return periods in reg.25, Parliament could not have intended to give them discretion to negate the effect of the time limits set out in primary legislation.

The judge also cited HMRC's internal guidance from the VAT Assessments and Error Correction Manual (VAEC1160) as indicating that HMRC themselves accepted that the one-year time limit (knowledge of the facts) applied to registration periods, which suggested that the effective negation of time limits implied by the officer's view was not HMRC policy.

The judge followed through with the logic to hold that the single assessment did not fail completely because part of the period was out of time: it was comprised of a number of prescribed accounting periods, and the last of these (1 January 2015 to 31 March 2015) would be in time, if she was wrong on the liability issue.

The penalty was issued under VATA 1994 s.67 and mitigated under s.70, because it related to a period before the rules changed on 1 April 2010. The principles of "telling, helping and giving access" therefore did not apply. S.70 allowed the Tribunal to "reduce the penalty to such amount (including nil) as they think proper", and having considered all the circumstances, the judge concluded that a reduction to 2% would be appropriate. She confirmed that a penalty does not depend on the validity (or even the issue) of an assessment, and it would therefore still stand even if she was wrong on the liability but right on the time limit.

The overall conclusion was to allow the appeal, but the judge set out the appeal rights of the parties, probably in expectation that HMRC will not agree with her decision.

First-Tier Tribunal (TC08465): *Staysure.co.uk Ltd*

2.3.3 Not insurance

The operator of Self Invested Pension Schemes (SIPP) charged investors fees for its services. Although pensions business is treated as insurance for financial regulatory purposes, it treated its fees as taxable up to 2014. It then reviewed its VAT position and made a claim in March 2016 to recover overpaid VAT, arguing that its fees should have been treated as exempt. The claim was rejected in October 2019, and after the decision was upheld on review in February 2020, the company appealed. The FTT considered the matter in principle without regard to the amounts involved, which could be agreed between the parties if the appellant was successful.

The FTT reviewed the application form, fees schedule, terms and conditions and key features document. The SIPP was a registered pension scheme under income tax rules, so members received tax relief on

contributions and were restricted in the ways in which they could access their money. They (or their financial advisers) were responsible for taking decisions about investments.

The Tribunal discussed a range of precedents about insurance transactions in general UK law, as well as VAT cases leading up to the CJEU decision in *United Biscuits (Pensions Trustees) Ltd* (Case C-235/19). That case showed that the definition of insurance for VAT is narrower than for other regulatory purposes, and pensions business is not necessarily covered by the VAT exemption. It also highlighted the fact that the UK had incorrectly treated investment management of pension schemes by insurance companies as within the exemption up to 31 March 2019, leading to a fiscal distortion between insurance-based pension schemes and those not benefiting from the exemption.

Judge Amanda Brown noted that the case involved three days of detailed argument by counsel. The appellant's case was essentially predicated on a submission that the provision of a pension is an activity constituting the provision of long-term insurance when viewed through the lens of the EU insurance directives, the Financial Services and Markets Act and historic domestic case law on what constitutes insurance.

The appellant argued that the VAT case law had mainly concerned "indemnity insurance", where the insurer agrees to indemnify the insured against loss. By contrast under a life insurance contract the insurer agrees to make payment of a sum by reference only to the uncertainty as to timing or order of events, each sum being determined at the time of payment and potentially subject to fluctuation. The SIPP contract ensured that, in return for the payment of the fees, the payments would be made in accordance with the tax rules in FA 2004.

HMRC responded by arguing that *United Biscuits* defined the essential features of "insurance transactions", and they were not present in the SIPP. In particular, the appellant bore no risk: it was a defined contribution scheme, so the pot of money built up by the policyholders would be used to pay out all and any benefits. They bore all the risk.

The Tribunal noted that its task was to determine the VAT liability, and was therefore cautious in expressing a view on whether the SIPP was "insurance" under general UK law. It decided that, on balance, the contract did meet the tests set down in a 1904 case involving Prudential.

The Tribunal also noted that HMRC guidance suggested that meeting these tests would make the contracts eligible for VAT exemption. However, "HMRC guidance is not the law and enforcing its application is not within the jurisdiction of this Tribunal (that is a matter for a judicial review challenge in the Administrative Court)." The Tribunal had to apply the VAT law, and in the developing precedents the assumption of risk by the insurer appeared to be significant. "In order for a supply to be exempt as an insurance transaction, the insured must pay the insurer to assume a financial risk. Such a conclusion includes within the scope of the exemption both indemnity and contingency insurance as, under a conventional (non-investment) life assurance policy the insured pays a fixed, up-front, annual or monthly premium over the term of the policy and the insurer bears the risk on a fixed sum payment on the happening of the insured event (death/critical illness etc). However, excluded from

exemption is any policy/scheme which meets the Prudential life/death uncertainty without the assumption of financial risk."

The Tribunal had not been presented with any evidence about SIPPs provided by insurance companies, so it was not possible to consider an argument based on fiscal neutrality. However, even if it could be shown that other taxpayers had benefited from the exemption, in accordance with the *Rank Group* decision (Case C-259/10) a taxpayer could not use fiscal neutrality to benefit from a legal error by the authorities.

The FTT concluded that the SIPPs were not insurance transactions for VAT purposes, so the fees charged by the company were not exempt. The appeal was dismissed. The Tribunal noted "by way of postscript" that "by reference to HMRC's guidance in this area the appellant's case had clear merit. By reference to the case prosecuted by HMRC their guidance is outdated and misleading and should be amended without delay."

First-Tier Tribunal (TC08479): *Intelligent Money Ltd*

2.3.4 Education

A Romanian commercial company provided educational services consisting of the organisation of activities supplementing the school curriculum, such as homework support classes, educational programmes, foreign language classes, art classes, sporting activities, picking children up from school and the provision of after-school meals. The tax authorities ruled that it should have registered for VAT; it argued that it should be exempt because it was providing services closely related to school education.

The referring court noted that it was not included within a national programme for providing "school after school", which was a condition for exemption under Romanian law. However, it considered that the company might be able to rely on the direct effect of art.132(1)(j) PVD. That would in turn depend on whether it could be included or excluded by the expression "an organisation recognised as having similar objects", given that it appeared not to be so recognised by the Romanian authorities.

It was for the national courts to consider whether the conditions exceeded the limits of the state's discretion in applying the principles of EU law, in particular the principles of equal treatment and fiscal neutrality. Subject to that consideration, the appellant clearly did not satisfy the requirement to be recognised by the state as having similar objects, and was therefore excluded from exemption.

This meant that it was not necessary to answer a separate question about whether the company's activities fell within "services closely related to school education", given that it did not provide the education itself.

CJEU (Case C-612/20): *Happy Education SRL v Direcţia Generală Regională a Finanţelor Publice Cluj-Napoca, Administrația Județeană a Finanțelor Publice Cluj*

2.3.5 Hospital care

Art.132(1)(b) PVD exempts medical care (and closely related goods) supplied "by bodies governed by public law or, under social conditions

comparable with those applicable to bodies governed by public law, by hospitals, centres for medical treatment or diagnosis and other duly recognised establishments of a similar nature." Art.133 permits Member States to restrict the exemption in art.132(1)(b) by imposing one or more conditions: it can be restricted to non-profit making bodies, bodies managed on an essentially voluntary basis, bodies subject to price regulation, and situations in which distortion of competition would not arise.

The German law restricted the exemption to certain categories of "approved" hospital. A private limited company that was not on the approved list appealed against a ruling that the majority of its supplies were taxable. The German court was concerned that the domestic law might impose conditions that were not compatible with the PVD, in particular in the light of the principle of fiscal neutrality.

Advocate-General

Advocate-General Hogan commented that the CJEU uses the expression "fiscal neutrality" in three different ways:

- the idea that the tax should be "neutral" from the point of view of a taxable person, in that input tax is recoverable so that the total tax collected is the VAT fraction of the amount paid by the final consumer;
- the principle of equal treatment of similar transactions;
- the principle of distortion of competition.

The A-G drew a distinction between the second and third of these senses. Prevention of distortion of competition is a principle of interpretation where other methods of interpretation do not lead to a conclusive result; but equal treatment is an overarching principle of law. He considered that both of these concepts were relevant to the dispute.

The A-G went on to examine the scope of the exemption in art.132(1)(b), in order to consider whether it precluded the way in which the equivalent provision was written into German law. It imposed conditions on three aspects of the supply:

- the nature of the service provided,
- the form of the establishment providing the service, and
- the manner in which the service is provided.

The first condition was not controversial in the present case. The "form of the establishment" has to be "hospitals, centres for medical treatment or diagnosis and other duly recognised establishments of a similar nature." After detailed consideration of the principles underlying the rule, the A-G concluded: "*It follows that, in my view, both the wording, the context and the objectives pursued by Article 132(1)(b) of the VAT Directive, and the need to interpret any provision in a manner which does not call into question its validity, demonstrate that the discretion available to the Member States to define the conditions under which an establishment governed by private law is to be regarded as 'duly recognised' extends solely to the conditions which must be satisfied in order for an establishment to be duly authorised to carry out, within a structure in*

which resources are pooled, the health and medical services covered by that exemption. In essence, therefore, the 'duly recognised' requirement relates to professional standards only."

Unusually, the A-G noted that precedent decisions appear to be inconsistent: *Lup* (Case C-106/05) claimed to rely on *Dornier* (Case C-45/01), but in fact applied a different analysis to the relevance of the extent to which the care in an institution was paid for by public health insurance. However, he was confident that the overall conclusion remained that a distinction between two institutions could not be based solely on the extent to which the care was funded by health insurance: the key question was whether the services were equivalent from a qualitative point of view in the light of the professional qualifications of the service providers in question. If an institution was largely funded by public health insurance, that was an indication that it was "duly authorised" by the State; but the converse did not follow – if an institution's patients were mostly private, it would still be duly authorised if it was able to show that it met the appropriate legal medical standards to allow it to operate.

The A-G went on to consider the expression "under comparable social conditions". He considered that the required comparison involved consideration of the requirements imposed on the institution with respect to its patients, rather than its whole operation. "Comparable" meant "similar but not necessarily identical".

The judgment in *Idealmed III* (Case C-211/18) appeared to apply the "comparable social conditions" to the services provided and not to the provider. However, the A-G considered that it was based on a different situation and should not be more widely applied.

The conclusion on whether the German law was compatible with the PVD drew a distinction between:

- on the one hand, several of the German conditions for exemption, which the A-G opined were neither "social conditions" nor within art.133, and therefore not legitimate; and
- on the other hand, the requirement that, in order to be exempt, a private hospital must have carried out, during the previous financial year, at least 40% of hospital services invoiced for an amount lower than the amount reimbursable by the social security bodies. This was capable of constituting a "social condition" for the purposes of art.132(1)(b), if a comparable requirement was imposed on bodies governed by public law.

The A-G's opinion is a very detailed examination of the EU rules on exemption; even though it may not be particularly relevant to the medical care exemption in the UK, it provides a model of legal analysis that could be helpful in other contexts.

Full court

The full court considered that the issue was the requirement for suppliers to be "duly recognised" within art.132(1)(b). It noted that some language versions of the Directive placed the expression "duly recognised" at the end of the article, implying that it applied to all the bodies listed there (including hospitals and centres for medical treatment); others, including

the English and German versions, placed the expression between "other" and "establishments of a similar nature", suggesting that only those entities had to be "duly recognised". Consistently with the context and purpose of the provision, the condition should be understood as applying to all the establishments mentioned.

The court then considered at length whether the German law's conditions for recognition were compatible with EU legal principles, and concluded that they were not. The principles of equal treatment and fiscal neutrality would be breached if a private hospital had to charge VAT on services that were objectively identical to those supplied by recognised hospitals; the need for inclusion or exclusion from a regional plan or the conclusion of contracts with the general health insurance scheme could not override this.

The second question asked what factors should be taken into account in deciding whether a private hospital was providing medical care "under social conditions comparable with those applicable to bodies governed by public law". The answer given was:

"*The competent authorities of a Member State may take into consideration – where they are intended to attain the objective of reducing medical costs and making high-quality care more accessible to individuals – the regulatory conditions applicable to the services supplied by hospitals governed by public law and indicators of that private hospital's performance in terms of staff, premises and equipment and the cost-efficiency of its management, in so far as those indicators are also applicable to establishments governed by public law. Account may also be taken of the method of calculating fixed-rate daily fees and the fact that the services supplied by that private hospital are borne by the social security regime or under contracts concluded with public authorities, so that the cost borne by patients is similar to that borne by patients for similar services supplied by hospitals governed by public law.*"

CJEU (Case C-228/20): *I GmbH v Finanzamt H*

2.3.6 Burial services

A company installed prefabricated burial vaults in a graveyard to deal with problems of unstable soil structure. It considered that the supplies were "in connection with the disposal of the remains of the dead" and were therefore exempt. HMRC ruled that they were taxable, and the company appealed.

Judge Heather Gething reviewed the case law relied on by HMRC, which comprised *Network Insurance Brokers Ltd v HMRC* (High Court 1998) and *CJ Williams Funeral Service of Telford* (VAT Tribunal 1999). *Network* was about an insurance broker that sold funeral plans. The company argued that it did more than provide a financial product – it made arrangements for the funeral. The High Court judge explained that its services were too far removed from "the disposal of the remains of the dead" in VATA 1994 Sch.9 Group 8: item 2 exempted "The making of arrangements for or in connection with the disposal of the remains of the dead", and the insurance broker was effectively "making arrangements for the making of arrangements". *Williams*, by contrast, offered cold storage facilities to other undertakers who did not have their own, and wanted the supply to be taxable in order to be able to recover input tax; the Tribunal

held that the supply was directly related to disposal of bodies, and was exempt.

The company relied on Notice 701/32 which refers to lining of a grave to deal with unstable soil. It argued that preparing graves in advance should be no different to preparing graves immediately before burial, and it should make no difference whether the work was done by an undertaker or another supplier. The only purpose of constructing the graves was to dispose of the remains of the dead.

HMRC argued that the exemption would only apply where the supply was in connection with the disposal of the remains of a particular dead person, and had to be made by the undertaker, not a sub-contractor. The undertaker had responsibility for the dead body and was therefore directly concerned with the disposal, whereas a sub-contractor was not.

The judge noted that Moses J had said in *Network* that it did not matter that services were provided in advance, nor that they were in connection with a particular funeral. The key question was to identify the result of the service: did it directly lead to the disposal of the remains of the dead? The decision in *Williams* showed that the service did not have to be supplied by the undertaker personally, but could be subcontracted.

The Notice did not have the force of law, nor was it a guide to statutory interpretation. However, the judge pointed out that HMRC accepted that digging graves was an exempt service when carried out by an undertaker, and it was hard to accept that it would be different if it was carried out by someone else. The *Network* case suggested that exemption covered "the type of supplies normally carried out by undertakers", which would include the preparation of graves.

The judge went on to apply the "always speaking" rule of statutory interpretation that was used, and then rejected, in the *News Corp* case. The prefabricated structures were a modern solution to the problem of unstable soil structures; if the methods specifically mentioned in the Notice were exempt, then so was a different way of achieving the same objective. Applying the exemption fulfilled the purpose of the statutory provision.

The supplies were "in connection with the disposal of the remains of the dead" within item 2 of Group 8, and the appeal was allowed.

First-Tier Tribunal (TC08484): *Hodge and Deery Ltd*

2.3.7 Manual update

The *VAT Health Manual* has been updated to explain the nursing agency concession and how it may be incorrectly applied by businesses to supplies of staff that should be standard rated.

VATHLT2360

2.4 Zero-rating

2.4.1 Flapjacks were not cakes

The definition of "cakes", and the application of that definition, has been considered again by the FTT, this time in connection with 36 varieties of food products described as "flapjacks". Excepted item 2 in VATA 1994 Sch.8 Group 1 provides that "confectionery, not including cakes" should be standard rated. Confectionery is defined as "sweetened prepared food which is normally eaten with the fingers". It was common ground that the flapjacks fell within the definition, but if they were also cakes, they would be zero-rated.

Following a visit to the company in 2016, HMRC became aware that it had applied the zero rate to a range of products. After further enquiries and consideration of samples by a specialist HMRC team, assessments were raised covering the period from 12/13 to 07/18 (assessments for two periods were later withdrawn).

Judge Christopher Staker noted that he and his side member had volunteered to taste samples of all 36 products, but the taxpayer's counsel agreed that a sample of four would be sufficient to be representative. There were also about 2,000 pages of documents and authorities to digest. The company had also applied to adduce additional evidence concerning similar products that had been sold zero-rated by competitors; the Tribunal questioned whether this was relevant to a decision of whether this company's products were correctly zero-rated under the law, and the company withdrew the application.

The judge commented after tasting two of the products that they did not seem "sweet" to him, and raised the question of whether they were truly "confectionery" within the statutory definition. The company's counsel made an oral application to introduce a new ground of appeal to this effect, but the judge rejected it, presumably because it would have been a fundamental change to the initial grounds of appeal in which the company had accepted that the products were confectionery.

The decision describes the curious supply chain:

Step 1: GNUK manufactured the products, then sold them to Glanbia Nutritionals (Ireland) Limited ("GNIL"), a member of the same corporate group that was outside the Appellant's VAT group.

Step 2: GNIL sold some of the products itself to third party customers, and supplied some of the products back to GNUK.

Step 3: GNUK sold to third party customers the products that it had acquired back from GNIL at step 2.

(2) The price at which GNUK sold the products at step 3 was higher than the price at which GNIL sold the products to GNUK at step 2.

(3) The HMRC decision under appeal finds that the Appellant should be assessed to output tax at the standard rate on GNUK's sales both at step 1 and step 3.

(4) The sales by GNIL to GNUK at step 2, and the sales by GNUK at step 3, both involve the very same goods and these sales at both steps should be subject to the same rate of VAT.

(5) GNIL's invoices to GNUK for the sales at step 2 indicated that the sales were zero rated. No amounts in addition to the purchase price stated in the invoices was ever paid by GNUK to GNIL in respect of VAT on those sales, and no amounts of VAT in respect of those sales have been paid by GNIL to HMRC.

(6) HMRC never issued a VAT assessment to GNIL in respect of its sales to GNUK at step 2, and HMRC are now out of time to issue any such assessment.

(7) At the time that HMRC formed the view that GNUK should be assessed to VAT in respect of its sales at step 3, HMRC were aware that GNUK had acquired the goods from GNIL, and at that time HMRC would have still been within time to issue a VAT assessment to GNIL in respect of its sales to GNUK at step 2.

(8) The quantum of the assessment to VAT issued by HMRC to GNUK on its sales at step 3 has been calculated on the basis that the price at which it sold the goods to its third party customers was a VAT-inclusive price; that is to say, one sixth of the price actually paid to GNUK by its third party customers has been treated as the VAT element of the payment.

The judge referred to the HMRC Manual *VAT Food*, which at VFOOD6200 states "It is our policy that there is a difference between flapjacks and cereal bars. This policy development arose because, at the inception of VAT, flapjacks were widely accepted as cakes, and cereal bars were not widely available, if at all. Flapjacks were accepted as being a cake of common perception and widespread home-baking, not because of any specific reasoning behind such factors as their recipe, ingredients or the manufacturing process… The problem that has arisen is that a flapjack is, historically, accepted as a cake, but should probably now be categorized as a cereal bar, and therefore standard-rated, within the legislation." The manual goes on to explain that HMRC regard many modern products that are sold with the description "flapjacks" as in fact "cereal bars"; only products that contain nothing but oats are traditional flapjacks.

The judge noted that the origin of the distinction between zero rated food and standard rated exceptions appears anomalous today, but had its origins in the distinction between "essentials" and "luxuries" that was drawn on the introduction of VAT in 1972 and effectively frozen in 1979. The words in Excepted Item 2 must be given the ordinary meaning that would be attached to them by "the ordinary person"; the correct classification of a product is a "short practical question calling for a short practical answer". It was not an exercise that could be based on authority and precedent, and it was not necessary for a Tribunal to identify each and every aspect of similarity and dissimilarity between the product in issue in the case, and the products that were in issue in previous cases. In any particular case a Tribunal may choose to focus upon and mention particular aspects of the product. The healthiness or otherwise of a product generally has no bearing on its VAT classification.

Crucially, the sole question was whether the product was a "cake" for the purposes of Excepted Item 2. It made no difference that it was called, or sold as, a "flapjack". The Tribunal had a full appellate jurisdiction on the question, and was not considering the reasonableness or otherwise of HMRC's decision. Nevertheless, the Tribunal took note of HMRC's

policy on flapjacks and, in the interests of consistency, "will not discard it lightly".

The factors to be taken into account included ingredients, taste, texture, appearance and presentation, size, packaging, marketing, manufacturing technique, shelf life, consistency when stale, circumstances of consumption, and name. None of these factors was determinative on its own. The judge went through the different factors in detail, and concluded that none of the products had sufficient characteristics of a "cake" to fall within the definition for the purposes of the provision. They were all standard rated, and the appeal was dismissed.

The decision is notable for introducing the concept of a "platonic" or "archetypal" cake, which "the ordinary person would consider… to be something that is baked, which is made from a thin batter containing flour and eggs, and which is aerated in the process of baking." Each of the products contained significant amounts of protein, which was not traditionally associated with cakes, and they were not baked but combined with syrup at 85 degrees Celsius. That was quite different from the traditional preparation of a cake.

There was a secondary issue: the company that was the subject of the assessment to output tax had received a supply of the flapjacks from another member of the corporate group that was not in the same VAT group. It claimed that, if it was liable for output tax, it should have a corresponding credit for the input tax that would have been due on the purchase. The judge rejected that argument in line with the Court of Appeal's decision in *Zipvit*. The judge considered himself bound by the CA decision on the question of whether a VAT invoice was a prerequisite for a deduction (it was), when that issue had not been considered by the CJEU (which decided that VAT was not "due or paid").

First-Tier Tribunal (TC08439): *Glanbia Milk Ltd*

2.5 Lower rate

2.5.1 Hot food and catering

The *VAT Retail Scheme Manual* has been updated to give further guidance on the application of the temporary 5% VAT rate for catering that expired on 31 March 2022.

VRS13020

2.6 Computational matters

Nothing to report.

2.7 Discounts, rebates and gifts

Nothing to report.

2.8 Compound and multiple

2.8.1 No separate supply

An insurance broker developed, marketed and sold "telematics" car insurance, in which a device was fitted to the cars driven by drivers (mainly aged 17 to 25) to measure their driving performance. The data gathered by the devices was monitored to provide feedback to the drivers and the insurers, who would reduce or increase the premiums according to the perceived level of risk. The company was only a broker and did not underwrite any of the risk.

In 2018 it submitted an error correction notice to reclaim just over £2 million in input tax incurred on the purchase and fitting of the devices. It argued that it was making a taxable supply of the devices to the policyholder and was therefore entitled to claim input tax. That supply was alternatively argued to be for non-monetary consideration (in agreeing to enter into the policy) or no consideration (in which case a taxable supply could still arise under VATA 1994 Sch.4 para.5).

HMRC rejected the claim, holding that there was no supply of the goods to the policyholder. The only supply made by the company was of insurance intermediary services made to the insurers; the costs incurred in fitting the device were cost components of that exempt supply. The company appealed to the FTT, where it came before Judge Greg Sinfield.

The judge set out the issues for determination as follows:

(1) Did ISL make supplies of the Device and related services to the policyholders for consideration?

(2) If ISL did not make supplies to the policyholders for consideration, did ISL make a deemed supply of the Device?

(3) If ISL made a taxable supply to the policyholder for consideration, how should the VAT chargeable on the supply be calculated?

(4) If ISL made a deemed taxable supply of goods, how should the VAT chargeable on the deemed supply be calculated?

Because the PVD applied throughout the period, and UK legislation had to be construed as conforming to the PVD, the judge cited only the articles of the PVD that were relevant. These included articles 2(1), 14(1), 16, 24(1), 73, 74, 168 and 135(1)(a).

The evidence included a detailed consideration of the contracts between the company and the insurers, and the company and the insured. The starting point for determining whether there was a supply for consideration was to consider the contracts; in this case, there was no suggestion that the contracts were in any way artificial, and counsel for the taxpayer did not suggest that the commercial and economic reality was in any way different.

The analysis is very detailed, but the conclusion was clear: under the contracts, the company did not make a supply of goods for consideration either to the policyholder or to the insurer. The policyholder was required to have a working device fitted to their car as a condition of having the insurance, and the company undertook to incur the costs of fitting it as part of its obligations to the insurer. The contracts explicitly stated that

the device did not become the policyholder's property as a result. Payments for having new devices fitted were collected by the insurer in the same way as premiums, and the judge held that they were extra consideration for the insurance cover.

HMRC argued that the deemed supply rules could not be used to create a right to deduct input tax where none existed. The goods were cost components of a purely exempt supply, and that could not be recharacterised as a partly exempt supply with a deemed taxable element. Counsel for the taxpayer responded that a deemed supply had been used to generate a right of repayment in *Church of England Children's Society*, a 2005 High Court decision which was binding on the Tribunal. The judge agreed with HMRC that the reasoning in that case had been superseded by the CJEU decisions in *Mateusiak* (Case C-229/15) and *Mitteldeutsche Hartstein-Industrie* (Case C-528/19).

Mateusiak dealt with a deemed supply on deregistration, but the principle was the same: there could be no deemed supply without a prior right to deduct input tax. The right to deduct input tax could not be generated purely by the deemed supply. In *Mitteldeutsche Hartstein-Industrie*, the taxpayer had incurred costs on improving a public authority's roads, and the CJEU held that it had not made a deemed supply to the authority because the costs were incurred for its own purposes. The judge considered that *Church of England Children's Society* had been decided "per incuriam" (incorrectly) and he did not have to follow it.

Because he had decided that no supply or deemed supply was made by the company, it was not necessary to consider what the output tax on such supplies would have been. The appeal was dismissed.

First-Tier Tribunal (TC08462): *WTGIL Ltd*

2.9 Agency

Nothing to report.

2.10 Second hand goods

Nothing to report.

2.11 Charities and clubs

Nothing to report.

2.12 Other supply problems

2.12.1 City cards

The full court has now ruled on the case, referred from Sweden, in which A-G Capeta's opinion was covered in the last update. It concerned a type of voucher: a "city card" sold to visitors to Stockholm (for about €65), entitling them to admission to about 60 attractions for a limited time (in the example, 24 hours from first use) and up to a set value (about €176). The card also gave unlimited rights to certain transport services and sightseeing tours. The services included in the card are either subject to tax, at various rates, or are tax exempt. The card is presented to be read by a special card-reading machine; once the value limit has been reached, the card is no longer valid, apart from the unlimited right to use transport services.

The parties to the dispute disagreed on the classification of the card. The tax authority considered that the high value and short duration suggested that it was expected that customers would not reach the value limit, and this meant that it was not a voucher at all. The company considered that it should be a voucher because suppliers were obliged to accept it as consideration. The referring court noted that city cards had been discussed by the VAT Committee when the present rules on vouchers were being developed, but that no consensus had been reached. The question referred was whether they were vouchers, and if so, whether they were multi-purpose vouchers.

Advocate-General

The A-G began by considering the history of the treatment of city cards by different member states. Some regarded them as a credit transaction, exempt from VAT. Some regarded them as fully taxable on the face value; others regarded them as taxable on the face value after deduction of the amounts paid for actual provision of the services. Of these three, only the third "profit margin" option would be applicable if the cards were to be treated as multi-purpose vouchers. The other two would be contrary to the 2016 vouchers directive: that sought to distinguish vouchers from credit transactions, ruling out exemption, and also did not approve taxation of supplies that ought to be exempt, which would apply to some of the underlying services covered by the card (such as admission to museums).

The A-G went on to consider the 2016 directive. In her view, this did not seek to change the treatment of vouchers but rather to rationalise it; it did not create an exception to the normal rules of VAT that would require narrow interpretation, contrary to the submissions of the Italian government and the Swedish tax authority.

The directive introduced the definition of a voucher that is now found in art.30a(1) PVD: an instrument that entails an obligation to accept it as consideration or part consideration for a supply of goods or services and which contains information about the goods or services for which the voucher can be used as consideration, or, alternatively information about the potential suppliers. This definition does not include all instruments that are commonly referred to as vouchers: for example, 'discount vouchers' are excluded from the VAT Directive's definition, even if they were included in the original proposal for the 2016 Directive. They do not meet the definition because they cannot be used as consideration on their own. The A-G commented that a city card cannot be treated as a voucher simply because it is called one; it has to meet the conditions of the PVD definition.

The definition requires that the instrument must encompass an obligation for the suppliers of goods or services to accept it as consideration or part consideration for a supply of goods or services they provide, and the goods or services to be supplied or the identities of their potential suppliers are either indicated on the instrument itself or in related documentation. The A-G commented that something had to satisfy both these conditions to be regarded as a voucher; however, it was not necessarily the case that every instrument that satisfied the conditions was a voucher.

There is a wide variety of city cards available under different schemes. The A-G noted that not all would satisfy the conditions, and their classification as vouchers had to be considered on a case-by-case basis. She went on to examine whether there were good reasons for excluding even those that met the definition from being treated as vouchers. She examined the arguments put forward by the tax authority – mainly that the city cards did not enable customers to see how the value reduced as they were used, and that part of the value represented an effective "subscription" for unlimited transport services – and did not consider them good enough reasons to exclude the city cards from being regarded as vouchers.

What was much more important was the correct application of special treatments to the underlying supplies – the use of the voucher to purchase exempt services. As the use of the voucher for different purposes was not known at the time the voucher was purchased, it had to be a multi-purpose voucher. The A-G then very quickly came to the conclusion that the "profit margin basis of taxation" should be adopted, which would give rise to a comprehensive, uniform, transparent and neutral tax scheme for such vouchers, even though it is perhaps not explicitly recognised by the PVD.

The A-G recommended that the court should confirm that the card was a MPV. As that was the only question referred, consideration of the "profit margin basis" was no more than part of the A-G's background discussion of the issues.

Full court

The full court agreed with the A-G and the taxpayer that the basic conditions for the card to be treated as a voucher were met – it could be presented as consideration for the supply of services, and the suppliers and the nature of the services it could be used to obtain were identified in related documentation. The fact that a consumer could not take advantage of the full range of services covered, and the short duration of the validity period, were not relevant considerations.

The court rejected a submission by the Italian government that the card constituted a single supply of services. The diversity of the services covered by the card, and the different VAT treatments of those services, contradicted this contention.

It was then a short step to conclude that the card was a multi-purpose voucher, because it was clear that it could be used for supplies that had different VAT liabilities.

The full court did not even mention the way in which the cards should be taxed. The main issue, not covered by the questions referred, is the treatment of unused credit on the card at the expiry of the validity period. Because it is treated as a MPV, that profit to the card issuer is not apparently subject to VAT at all.

CJEU (Case C-637/20): *Skatteverket v DSAB Destination Stockholm AB*

2.12.2 Termination of leases

HMRC have updated the Notice *Motoring expenses* to reflect the change of policy on early termination charges as it applies to car leases. The notice now says:

Where a business terminates its lease early, the leasing company will treat the termination payment and any associated rebate of rental as taxable. It will normally offset the termination payment against the rebate and issue the business with a VAT invoice for the difference. From 1 April 2022, if a business terminates a contract early, the fees charged are regarded as further consideration for the contracted supply.

The 50% block (which prevents recovery of 50% of the VAT charged, to cover private use of the car) will apply because the termination charge is additional charge for the rental of the car.

If the rebate exceeds the termination payment, the leasing company will issue the business with a VAT credit note for the balance. If VAT on the rentals was 50% restricted, the business will need to adjust only 50% of the VAT credit in the VAT account.

VAT Notice 700/64

2.12.3 Fuel scale rates

HMRC have updated the table of deemed outputs for private use of road fuel in a car where the business claims back input tax on all road fuel purchased. The new table applies to whole prescribed accounting periods starting on or after 1 May 2022.

www.gov.uk/guidance/vat-road-fuel-scale-charges-from-1-may-2022-to-30-april-2023

3. LAND AND PROPERTY

3.1 Exemption

Nothing to report.

3.2 Option to tax

3.2.1 TOGC?

A company appealed against an assessment for £17 million for its 01/16 period. The appeal had originally been brought by the vendor of a property, but during the proceedings it was realised that the representative member of its VAT group should be the appellant, and the Tribunal issued directions to substitute that company.

The company had treated the sale of some land and property as part of a VAT-free transfer of a going concern. Curiously, Judge Heid Poon starts by noting that the HMRC decision was not listed in s.83(1) VATA 1994, which would suggest that the Tribunal did not have jurisdiction to consider it. However, the assessment is surely covered by the general jurisdiction to consider "the VAT chargeable on any supply of goods or services" in s.83(1)(b).

The group property company (HGPL) acquired the site in January 2004, having opted to tax it the day before the purchase. The VAT group occupied part of the site as business premises, but some parts of the site were leased to other businesses, in particular Teddington Studios. On 22 September 2011, Teddington Studios exercised a break right to surrender its 1999 lease, with the exit date being 24 December 2014.

In 2013, the company decided to apply for planning permission to develop the site, with a view to selling it with the benefit of planning consent. A planning application for residential development was submitted in March 2014 and granted in October 2014, subject to the signing of a s.106 agreement to undertakings required by the Council. Formal consent for the construction of 213 flats and 6 houses was granted on 19 December 2014.

The property had been marketed informally during 2014, and formally placed on the market with a marketing brochure on 7 November. An offer of £85 million was received from a developer on 5 December, and Heads of Terms were sent by the sales agent to P on 19 December. The marketing brochure stated that the property was opted to tax and the Heads of Terms stated that VAT would be payable on the purchase price.

P opened negotiations with the express intention of achieving a TOGC sale that would help with cash flow and save SDLT. A new lease was granted to a company that advised P, at a rent of £22,000 a year excluding VAT, with an unspecified duration. Commercial reasons were given for the adviser needing to have premises on the site. The negotiations, which were carried on intensely over a short period, discussed the risk that HMRC might not accept the TOGC structure and how the parties could be protected if that turned out to be the case.

The sale contract was signed on 24 December 2014. The terms relating to VAT were as follows:

5.1 Subject to the following sub-clauses of this clause 5, all sums payable under this contract by the Buyer are expressed exclusive of any VAT.

5.2 (Save as provided in clause 5.8.1) the parties intend that the sale of the Property pursuant to this Contract shall be treated as a transfer of business as a going concern ("TOGC") within Article 5 of the Value Added Tax (Special Provisions) Order 1995 ("The Special Provisions Order").

5.3 The Seller warrants that it is registered for VAT and has exercised its option to tax pursuant to Part 1 Schedule 10 of the Value Added Tax Act 1994 ("VATA") or is bound by such an option.

(2) Under sub-clause 5.4, the Buyer warrants the following, and to keep the Seller indemnified against breach of any of the warranties (clause 5.5), whereby:

5.4.1 That, ... it shall apply to register for VAT, exercise its option to tax pursuant to Part 1 Schedule 10 VATA, give appropriate notification of such option to HM Revenue & Customs and supply copies of such application and notification to the Seller.

5.4.2 That is [sic] shall not revoke the said option to tax within one year following the date on which completion takes place.

5.4.3 That Article 5(2B) of the Special Provisions Order does not apply to the Buyer.

5.4.4 That it shall continue to carry on a rental business in respect of the Property for at least 6 months after completion takes place.

The contract also provided for the buyer to indemnify the seller against VAT, interest and penalties in the event of HMRC not accepting the TOGC treatment.

The decision sets out a series of events throughout 2015, leading up to completion. Another lease was granted to the demolition contractor 3 days before completion.

The company's appeal was based on the argument that it had carried on two activities, both of which were transferred to P: property development and property leasing. The leasing business had involved leasing to the group's own operations for many years, including at the date of exchange of contracts; the leasing to P's agent and the demolition company was a continuation of that activity. The company also argued that the work it had done to obtain planning permission constituted a property development business that was transferred to P, which intended to carry it on.

HMRC responded that the seller did not carry on a property development business before the sale, and that the leases in existence at completion were to the buyer's tenants, not the seller's. The intention was for P to have vacant possession at completion. HMRC did not argue that the arrangements were abusive in the specific VAT sense, but contended that the clear intention to affect the VAT treatment was relevant in interpreting the facts. The contracts were drafted in order to give the impression of

the transfer of a business, without actually delivering that outcome in fact. The sale contract was for a property, not a business.

The judge pointed out that there was no question that the VAT payable, if any, would be fully deductible by P. The tax at stake was therefore in reality the SDLT of £680,000 that would be payable in addition if the transaction was subject to VAT.

She went on to describe the TOGC rules in art.19 PVD and art.5 SI 1995/1268, and commented on the difference between them: the UK rule requires the transferee to carry on "the same kind of business", whereas the EU rule has no such requirement. The A-G in *Zita Modes* (Case C-497/01) explicitly stated that "it is not necessary for the transferee's business to be the same as that of the transferor". However, she said "Neither party takes issue with this divergence in the TOGC provisions, since the express requirement of continuance with the same kind of business by the transferee is within the margin of discretion of a member state when exercising the option to implement the no-supply rule. This is as provided by the second sentence of Article 5(8), a member state 'may take the necessary measures' to prevent any distortion of competition".

This meant that it was important to pay attention to the UK court decisions, because they were considering a UK rule that differed in an acceptable way from what the CJEU would take into account. The UT decision in *Royal College of Paediatrics* emphasised the need to consider all the circumstances of the case, including the intentions of the parties, in deciding whether the same kind of business would be carried on.

For reasons set out in some detail, the judge concluded that the transferor did not carry on, and had never intended to carry on, a business of property development. Its activities in relation to the site were at all times aimed at selling the site with the benefit of planning consent. The s.106 agreement was entered into with the intention that the developer would fulfil its conditions, not the seller. In addition, the marketing documentation showed that it was the intention to sell a freehold asset, not a property development business. Even when the parties were engaged in the discussion of structuring the transfer as a TOGC, those discussions never touched on the possible construction of a transfer of a property development business. The contracts exchanged in December 2014 referred only to freehold premises.

The fact that the contract was stated to be a TOGC was not conclusive, if the commercial and economic reality was different. In accordance with a number of precedents, the label adopted by the parties was not conclusive for the purpose of characterising the transaction. That was not to say that the contract was artificial or abusive, but it was still necessary to consider the nature of the transactions as they were, not as they were described. Those facts were considered in the context of all the surrounding circumstances, and the conclusion was the same.

The judge noted the VAT grouping aspect: although the appellant was the representative member, whose business was mainly in publishing, the *Intelligent Managed Services* decision required her to consider the business of individual group members. She therefore stated that she had concluded that the property company within the group was not carrying on a property development business.

The taxpayer's counsel acknowledged that the case for a TOGC of a property lettings business was weaker. The Teddington Studios lease had ended on the date of exchange of contracts. Completion was delayed to allow the group itself to relocate. At all times it was clear that the intention was for P to have vacant possession. The tenants who remained were "friendly" to the buyer – the buyer's agent and the demolition company. That was similar to the situation in the *Royal College of Paediatrics* case; the "critical feature of the special relationship between the putative tenants and the purchaser is fatal to the argument that there could have been a TOGC as a property lettings business."

The appeal was accordingly dismissed.

First-Tier Tribunal (TC08495): *Haymarket Media Group Ltd*

3.3 Developers and builders

3.3.1 Supplies by utility companies to developers

HMRC have updated the *VAT Fuel and Power* manual to give guidance on supplies of electricity to property developers while a site is being developed into housing. Some companies have applied the reduced rate to supplies that relate to individual houses once electricity and gas meters have been installed in them. HMRC do not accept that this is correct: in their view, domestic use can only start when the house has been transferred to a third party and is occupied as a dwelling. The guidance also includes comments on Climate Change Levy.

MP3150

3.3.2 Meaning of "building"

HMRC have updated the *VAT Construction* manual to give more detail on the definition of the term "building" for VAT purposes in light of the decisions in *Catchpole* (TC01995) and *Fox* (TC01957), specifically that the term 'building' can refer to more than one building.

VCONST14010

3.4 Input tax claims on land

3.4.1 Supplementary DIY claims

HMRC have issued a Brief to explain their policy following the FTT decision in *Andrew Ellis and Jane Bromley*. The Brief says:

In the case, two DIY housebuilders claims were submitted to HMRC. HMRC repaid the first claim having accepted valuation for council tax purposes as evidence of completion. HMRC received a further claim following the grant of planning permission by the Local Planning Authority for further required works. The second claim was rejected as it was out of time and as a valid claim had already been made and paid.

The court found that the first claim was paid in error as the evidence of completion given by the Valuation Office was invalid and should not have been accepted. As the first claim was paid in error the second claim should have been allowed and was not outside the 3 month time limit.

HMRC policy in relation to the decision

HMRC policy is that only a single claim is allowed under the DIY Scheme and this has not changed. However, where it is agreed that a claim has been repaid in error, HMRC will accept a subsequent claim with evidence that the claim has been made within 3 months of completion.

HMRC already allow (on a case by case basis) acceptance of supplementary claims. This is for invoices and works carried out before the claim was submitted, which may have been left out in error or invoices issued late by the contractor.

The FTT decided that there was nothing in VATA 1994 s.35 that restricted DIY claimants to a single claim, and the judge considered that such a limitation in the VAT Regulations would be ultra vires. That part of the decision has not apparently been accepted by HMRC.

Revenue & Customs Brief 8/2022

3.4.2 Snagging as part of construction

HMRC have added further guidance to the *VAT Construction Manual* to clarify when "snagging" can be treated as part of a construction project and therefore eligible for zero-rating. Normally these works are carried out by the original contractor under the terms of the original contract and so are not seen as a separate supply of construction services. However, circumstances may arise where the original contractor is not able to carry out the remedial works and another is contracted to carry out the works. This is seen as a separate supply of construction services:

- if this is made before completion of the building, it is a supply 'in the course of construction' and is eligible for the zero rate
- if this is made after completion, it is not a supply 'in the course of construction' and is ineligible for the zero rate.

The additional guidance describes a 2007 Tribunal case: *Following the Tribunal decision in Mr and Mrs James (VTD 20426), a case related to the DIY Housebuilders's Scheme, there may be circumstances where the defect is so bad that even though the building may now be occupied and a Certificate of Completion issued, the building cannot be said to be complete or fit for purpose. The court ruled that as a matter of fact and degree the construction was not completed at the time of the remedial works. In particular, the plasterer had provided visibly poor workmanship, and legal proceedings had commenced before the completion certificate was issued. In such circumstances, we accept that the supply of remedial works is a supply 'in the course of construction' and eligible for the zero rate so long as it is made at the earliest practicable opportunity.*

VCONST02600

4. INTERNATIONAL SUPPLIES

4.1 E-commerce

Nothing to report.

4.2 Where is a supply of services?

4.2.1 Fixed establishment

BC, a German company, had its registered office in Germany. It has marketed pharmaceutical products in Romania continually since 1996 for the purposes of the regular supply of wholesale distributors of medicinal products there, and for that purpose concluded a storage contract with a company established in Romania. It also has a tax representative in Romania and is registered for VAT there.

A Romanian company was incorporated in 2011 to supply management consultancy in the field of public relations and communication; it may also engage in secondary activities consisting in the wholesale supply of pharmaceutical products, management consultancy, advertising agency activities, market research and carrying out opinion polls. It was a wholly-owned member of the same group as BC, and BC was its only customer.

The contract between the Romanian company and BC included a variety of administrative and regulatory compliance work, as well as marketing and handling of orders and invoicing. BC undertook to pay a monthly fee for the services provided by the Romanian company, calculated on the basis of the total expenses actually incurred by that company, plus 7.5% per calendar year. These charges were invoiced without VAT, because the Romanian company considered that the place of supply was Germany.

Following a tax inspection, the Romanian authorities raised an assessment on the basis that the human and technical resources of the Romanian company were continually available to BC and therefore constituted a fixed establishment in Romania. The assessment was for nearly €9 million, plus interest and a late payment penalty.

The company appealed, and questions were referred to the CJEU. The wording of the national provisions on fixed establishments differed from art.11(1) of the Implementing Regulation. The national court considered that precedents in this area dealt with different situations; in this case, it might be relevant that the subsidiary was established specifically to make supplies exclusively to the German company that were related to its continuing business activities in Romania. The referring court was also not clear about the relationship between the fixed establishment rules and the supply of goods: was it necessary for the local operation to be directly involved in the supply of goods, or was it sufficient that that company has, in that Member State, technical and human resources that are made available to it through contracts for marketing, regulatory, advertising and representation activities that are capable of having a direct impact on the performance of that company's economic activity?

The court started by referring back to *Dong Yang Electronics* (Case C-547/18) as a reminder that the starting point for the place of supply rules was the main establishment; the fixed establishment rule was an exception that was to be used only when certain conditions were satisfied. The court also noted that the rule for fixed establishments in relation to B2B services (PVD art.44) depended on the FE having human and technical resources capable of receiving supplies for its own needs, not making supplies. This was considered in *Welmory* (Case C-605/12).

The court considered the question of whether it was necessary for the foreign established company to own human and technical resources in the country, or whether it was enough for it to have immediate and permanent access to such resources through a related company which it controls. It was necessary to consider the economic and commercial reality rather than merely the legal status of the entity concerned. *Dong Yang* was authority for the principle that the existence of a FE could not be deduced merely from the existence of a subsidiary in the country. However, it would be too restrictive to require direct ownership of the human and technical resources. It would be necessary for the referring court to consider whether BC had “a structure” in Romania, in terms of human and technical resources, which was sufficiently permanent. The court would provide the elements of interpretation of EU law to enable it to make that decision.

It was clear that BC had uninterrupted access to the subsidiary’s human and technical resources both through shareholding control and a service contract that could not be terminated at short notice. Those resources were substantial, including 200 employees, of whom 150 were sales representatives. However, as the subsidiary was a legal person, it should be assumed that it used its resources for its own needs, unless the German company could treat them as its own.

The court went on to consider the relevance of the interaction between the supplies of goods by BC and the supplies of services by the subsidiary. It noted that these were distinct and separate and subject to different schemes of VAT. Crucially, the resources on which the Romanian authorities based their argument were used to supply the services to BC; they could not both supply and receive the same services. Those services were received by BC in Germany, and BC did not have a structure in Romania that was capable of receiving the services that the Romanian subsidiary supplied.

It would be for the referring court to confirm a number of underlying facts, but the overall conclusion was that the subsidiary did not constitute a fixed establishment, which would nullify the assessment.

CJEU (Case C-333/20): *Berlin Chemie A. Menarini SRL v Administraţia Fiscală pentru Contribuabili Mijlocii Bucureşti – Direcţia Generală Regională a Fi-nanţelor Publice Bucureşti*

4.2.2 Passenger transport

A-G Szpunar starts his opinion in a case referred from Luxembourg by noting that the issue arose from the Congress of Vienna in 1815. This established that the rivers Moselle, Sure and Our, where they formed the border between two countries, would belong to both countries. This

provision still exists in a treaty between Luxembourg and Germany dating from 1984.

A Luxembourg company operated passenger boat tours on the Moselle. Initially, the Luxembourg authorities did not require VAT on the tickets, on the grounds that the services were supplied outside the territory. When the company bought a boat from a Netherlands supplier (in 2004), it was subject to acquisition tax, but the tax authority did not allow deduction on the grounds that it was not used for a taxable activity. This ruling was rejected by the Luxembourg Court of Appeal (in 2014), on the basis that the activity was taxable either in Germany or in Luxembourg, and the company therefore had a right of deduction. The tax authority then sought output tax on tickets for 2004 and 2005. That was rejected by the Luxembourg court (in 2019) on the grounds that Luxembourg would require a specific arrangement with Germany on the application of VAT on the "condominium" (as the commonly-owned river was described).

Finally, questions were referred to the CJEU to determine where these transactions should be taxed, and the A-G has given an opinion. This raised the preliminary question of whether tourist trips were "passenger transport" and therefore subject to the place of supply rules as such. There was a difference between "services in field of transport" which were subject to regulation under a different EU Directive, and "transport services" under the VAT Directives. The context and wording of the place of supply rules implied that the purpose of "transport services" had to be to move people or goods over significant differences, so that it was relevant to consider where the means of transport was situated during the supply "according to the distances travelled" in order to determine where the service was consumed. Nevertheless, at the end of this discussion of different meanings, the A-G concluded that services consisting in the organisation of cruises by river boat constitute transport services within the meaning of Article 9(2)(b) 6th Directive (now articles 48 and 49 PVD).

The A-G went on to disagree with the initial treatment of the supplies by Luxembourg as outside the scope. It appeared that both Luxembourg and Germany had regarded the Moselle as "not in the interior of the country"; that would mean that EU Directives did not apply there, which was an absurd result. Its specific status had not been foreseen or catered for by those drafting the 6th Directive, but the principles of VAT should be applied to it. The special status of the river made it possible for the neighbouring states to agree between them how transactions relating to it should be taxed, but it was a breach of treaty obligations for neither of them to collect tax.

The Commission proposed that, in the absence of an agreement between the countries, and in the very unusual circumstances, the place of supply should be determined by the starting point of the transport (Luxembourg). The A-G considered that this had no basis in the Directive. The transport service took place entirely on the water, which was entirely in the condominium. The Commission's proposal would also deprive Germany of the right to tax the transactions.

The A-G proposed that one or other of the countries should treat the transactions as taxable, until a formal agreement was entered into between them. If one country levied tax, any further charge levied by the other

country would contravene the basic principle that a double charge to tax would be wrong.

CJEU (A-G) (Case C-294/21): *État du Grand-Duché de Luxembourg v Navitours SARL*

4.2.3 Inadmissible question

The CJEU has refused to answer the questions referred by the Hungarian court in a case concerning a Hungarian business that was alleged to be avoiding tax by relocating its operations to Madeira. Although "no answer" is not very informative, there are a number of features of the case that are worth noting.

Advocate-General

Advocate-General Kokott considered that the court could give an answer in which both the Portuguese and Hungarian authorities claimed that they had the right to tax a transaction on the basis of a place of supply in their territory. The A-G noted that the Directive had been correctly transposed into domestic law in both countries, and the situation would give rise to genuine double taxation of one and the same transaction despite full harmonisation of the law. That contravened a number of underlying principles of VAT, in particular the neutrality of the tax.

The dispute concerned decisions of the Portuguese and Hungarian tax authorities on the place of supply of IT support services provided by a Hungarian undertaking (D) to a Portuguese undertaking (L). The case was related to an earlier dispute involving another Hungarian undertaking, WebMindLicences (WML), which was the subject of a reference to the CJEU some years ago (Case C-419/14). In that case, the question was whether it was an abuse of rights for a business established in a member state with a high rate of tax to use a fixed establishment in another member state to make supplies to consumers there at a lower rate. The answer was that the referring court had to analyse all the circumstances to decide whether the arrangement was wholly artificial, or whether the fixed establishment genuinely had the appropriate structure in terms of premises and human and technical resources to make supplies and engage in economic activity in its own name and on its own behalf, under its own responsibility and at its own risk.

The appellant in the present case considered that the required analysis had been carried out and the answer was that there was a genuine fixed establishment making supplies in Portugal. However, the Hungarian tax authorities maintained that the operation was solely operated by WML in Hungary, and the logical consequence was that the IT support services supplied by the Hungarian business to L must in reality be supplied to the main establishment in Hungary.

The connection between D, L and WML was not spelled out in the order for reference, but one of the questions suggested that the owner of WML is also the manager and/or owner of D. D supplied services to L comprising support, maintenance and construction of websites amounting to some €8 million between December 2009 and the end of 2011. L was incorporated in Portugal in 1998 and its principal activity in the relevant period was the provision of electronic entertainment services.

D was subject to a tax inspection by the Hungarian authorities, who decided that its supplies were in reality made to WML rather than to L; as a result, the place of supply was Hungary and Hungarian output tax was due. Assessments were issued in February 2020 for VAT of approximately €1.25 million, together with a penalty of €1 million and default interest of €350,000 on the basis of a finding that the services provided by the website were supplied by WML rather than by L, and the licence agreement between L and WML was fictitious.

The company appealed, and the tax authority asked the Portuguese authorities to clarify the facts. In the company's submission to the CJ, it claimed that the answer clearly showed that L was established in Portugal and carried on an independent economic activity there, and was therefore capable of receiving supplies from D. The Hungarian court decided to refer questions to the CJ because of the possible disagreement between the two tax authorities, leading to a potential double charge to VAT.

The questions referred set out the circumstances of the case in unusual detail, given that the procedure normally deals with questions of principle. The facts about L are all given as part of the question:

"…the acquirer of the licence:

(a) had rented offices in the first Member State, IT and other office infrastructure, its own staff and extensive experience in the field of e-commerce, as well as an owner with extensive international connections and a qualified e-commerce manager;

(b) had obtained know-how reflecting the processes for operating the websites and making updates to them, and issued opinions on, suggested modifications to, and approved those processes;

(c) was the recipient of the service that the taxable person provided on the basis of that know-how;

(d) regularly received reports on the services provided by the subcontractors (in particular, on website traffic and payments made from the bank account);

(e) registered in its own name the internet domains allowing access to the websites via the internet;

(f) was listed on the websites as a service provider;

(g) took steps itself to preserve the popularity of the websites;

(h) itself concluded, in its own name, the contracts with partners and subcontractors that were necessary in order to provide the service (in particular, with banks offering payment by bank card on the websites, with creators providing content accessible on the websites and with webmasters promoting that content);

(i) had a complete system for receiving revenue from providing the service in question to end users, such as bank accounts, full and exclusive powers of disposal over those accounts, an end user database enabling end users to be invoiced for that service and its own invoicing software;

(j) indicated on the websites its own headquarters in the first Member State as the physical customer service centre; and

(k) is a company independent of both the grantor of the licence and the Hungarian subcontractors responsible for carrying out certain technical processes described in the know-how…

The questions appear to proceed on the assumption that WML does provide the services through the website to the consumers in Portugal. The question therefore asks whether the granting of a licence from WML to L, in the circumstances in which WML supplies the services but L has all the trappings of economic activity, produce the answer that L can be treated as the recipient of the cross-border support services.

The A-G starts by noting that the place of supply appears to be irrelevant, if both potential recipients (L and WML) are entities with a right of deduction. However, the appellant in the case (D) is required to account for output tax if the supply is situated in Hungary, and is not required to do so if the supply is situated in Portugal.

It was clear that L was a business established in Portugal (specifically Madeira, which may mean that a special low rate applied to its outputs), and WML was a business established in Hungary; the place of supply rules for these services, both before and after the rules changed on 1 January 2010, was the place of establishment of the recipient of the service. The question was therefore to determine the "true recipient" – L or WML. The referring court also asked a subsidiary question about the possible impact of a finding of abuse of rights in the granting of the licence.

The A-G recommended that the questions should be substantially shortened and rephrased: in effect, the referring court was asking whether the various provisions of the PVD must be interpreted as meaning that, in the circumstances of the present case, the contracting party governed by civil law that paid the consideration (L) is the recipient of the supply, on the basis of which the place of supply is determined; or whether the possible existence of an abusive practice between the contracting party and a third party (WML) mean that that third party is to be regarded as the recipient of the supply, and the place of supply is determined on that basis.

The A-G divided her opinion into three sections:

- determination of the recipient of the supply
- possible impact of abuse of rights
- problem of conflicting determinations by different tax authorities

The determination of the "correct" recipient is determined by general principles under the PVD, whereas a finding of abuse depended on an assessment of the facts. Such a finding would require a recharacterisation of the transactions so as to re-establish the situation that would have prevailed in the absence of those transactions. The fact that the two businesses concerned could deduct input tax counted against a finding of abuse, because it was not obvious what tax advantage they could obtain, even with a lower tax rate in Portugal than in Hungary.

According to general principles, a taxable supply of services exists where there is a legal relationship between a provider of the service and a recipient pursuant to which there is reciprocal performance. In that relationship, the remuneration received by the provider of the service

constitutes the value actually given in return for the identifiable service supplied to the recipient. This is the case if there is a direct link between the service supplied and the consideration received. In the present case, there was a contract between L and D, and L paid for the service. There was no contract between WML and D, and WML made no payment. According to general principles, therefore, L had to be regarded as the recipient of the service, and L's place of establishment would determine the place of supply.

The A-G disagreed with the Hungarian authorities that the place of supply could be shifted by an abusive practice for several reasons:

- fiscal neutrality – VAT was charged on transactions regardless of any problem with the legal basis of those transactions or the parties to them;
- the supplier had to be able to determine the liability of the supply from information available to it, which would not normally include abuse by the recipient;
- people acting in their own name on behalf of someone else were normally treated as receiving supplies for VAT purposes.

This outcome might be different if the court concluded that the entire legal structure between all three parties (D, L and WML) was a single "significantly abusive" arrangement. That did not appear to be contemplated by the reference for a preliminary ruling.

The A-G then considered what would happen if the two tax authorities maintained their contrary positions. A double charge to VAT was contrary to the principles of VAT. It could arise from a divergent interpretation of the rules, or a divergent assessment of the underlying facts. The authorities in the two countries had the obligation to exchange information in accordance with Directive 904/2010 and to reach agreement by way of the VAT Committee (PVD art.398). If those possibilities were exhausted, then reference should be made to the CJEU.

Full court

The full court referred back to the *WebMindLicences* decision, in which it had ruled that it was for the referring national court to establish the facts and to decide whether there was an abusive practice in the form of a wholly artificial arrangement that did not reflect economic reality and was set up with the sole aim of obtaining a tax advantage. The court had pointed out that the fact that the manager and sole shareholder of WML was the creator of WML's know-how, that it exercised influence or control over the development and exploitation of that know-how and over the supply of the services which were based on it and that management of the financial transactions, staff and technical instruments necessary for the supply of those services was carried out by subcontractors, and the reasons which may have led WML to make the know-how concerned available to L instead of exploiting it itself, did not appear decisive in themselves.

The court had also ruled that the tax authority in Hungary was obliged to send a request for information to the Portuguese tax authorities in order to help assess whether there was an abusive arrangement. However, it was apparent from the order for reference that the two tax authorities had

continued to treat the transaction differently, and this led the Hungarian court to make a further reference.

The problem was that the questions referred did not make it clear why the answers given in *WML* were inadequate to determine the issue; rather, they represented an attempt to make the CJEU decide the issue itself rather than explaining a point of the principle of EU law. The CJEU therefore had no jurisdiction to answer the questions referred.

If the national courts of two member states support their respective tax authorities in applying the law to the facts – Hungary maintains that the arrangement is abusive and Portugal maintains that it is not – it is hard to see how the issue can be resolved.

CJEU (Case C-596/20): *DuoDecadKft v Nemzeti Adó- és Vámhivatal Fellebbviteli Igazgatósága*

4.3 International supplies of goods

4.3.1 Crossing the Irish Sea

HMRC have updated a variety of guidance to try to clarify the treatment of movements across the Irish Sea. These consequences are set out below:

- Goods sold on passenger ferries
- Moving goods – general
- Moving goods – partial exemption
- Moving goods – VAT groups

4.3.1.1 Goods sold on ferries

HMRC have updated their Notice *The VAT treatment of passenger transport* with information on accounting for VAT on goods sold on board ferries between Great Britain and Northern Ireland. These will continue to be treated as UK domestic supplies with UK VAT due and accounted for through the seller's UK VAT return.

A passenger who takes goods bought on board off the ship is not required to make any declaration in either Great Britain or Northern Ireland.

On board supplies will be treated as taking place outside the UK, and outside the scope of UK VAT if goods are sold on journeys that visit the UK as part of a voyage to or from third countries.

If a passenger lands they will have to declare any goods bought on board to customs under the normal passenger rules.

Where goods are sold on journeys between Northern Ireland and an EU member state, these will be taxed in the place of departure.

Notice 744A

4.3.1.2 Moving own goods across the Irish Sea

HMRC have updated their online guidance to explain the consequences of a trader moving goods they own or control between Great Britain and Northern Ireland:

This refers to goods that are business assets, which are moved from Great Britain to Northern Ireland. They can be either goods:

- *owned by a taxable person*
- *under a taxable person's control, for example, leased machinery, goods on sale or return or approval*

The owner of the goods, or person having control of the leased goods is the person liable for VAT on the removal into Northern Ireland, and should follow the normal accounting rules.

Additional rules apply to partly exempt businesses.

When a VAT-registered business moves goods from Great Britain into Northern Ireland, VAT will be due. The business will need to account for VAT on the movement. This should be included as output VAT on the VAT Return.

Where the goods are being used for taxable sales, the VAT may also be reclaimed as input VAT on its UK VAT Return, subject to the normal rules.

Where a business uses the goods for exempt activities, or where the goods are put to a taxable use and also exempt use, it may be required to make an adjustment to its partial exemption calculations.

Where a business has control of another party's goods, and moves them from Great Britain to Northern Ireland, they will be required to account for the VAT on the movement. They should issue an import document to the owner, if it is the owner that has the right to recover any input tax.

Input tax recovery of the VAT on own or third-party movements follow the normal VAT rules.

www.gov.uk/government/publications/accounting-for-vat-on-goods-moving-between-great-britain-and-northern-ireland-from-1-january-2021/accounting-for-vat-on-goods-moving-between-great-britain-and-northern-ireland-from-1-january-2021

4.3.1.3 Exemption and partial exemption

HMRC have updated their online guidance on exemption and partial exemption to cover the situation when an exempt or partially exempt business buys goods and then moves those goods to Northern Ireland. The guidance now says:

If you move your own goods from Great Britain (England, Scotland and Wales) to Northern Ireland, you will usually be able to recover the full amount of VAT as if it had been a taxable supply.

However, if you make supplies that are exempt from VAT you may not be able to recover some or all of the VAT on goods when they are first purchased. If you then move the goods from Great Britain to Northern Ireland you will incur a VAT charge.

You may also be further restricted in what input tax you can recover. For example, if you are making exempt supplies. This will mean that you have incurred an input tax restriction twice on the same goods.

To prevent this, you should reattribute the previously unrecovered input VAT on the original purchase in Great Britain as if the goods had been used for a taxable purchase. You can do this when making your annual adjustment.

Example

For example, if you purchase goods that are valued at £10,000 plus VAT of £2,000. Because you are making exempt supplies, only £1,000 of the VAT is recoverable.

If you then move the goods to Northern Ireland you will be charged VAT of £2,000. The partial exemption calculation at that time only permits £900 to be recovered.

This would mean you have paid £4,000 VAT and only claimed £1,900 as input tax.

To remedy this, you should treat the movement as if it were a fully taxable supply. This will allow you to recover the originally restricted input tax as being fully attributable to that taxable supply.

You can do this as part of your annual adjustment. The VAT may be reclaimed subject to the normal rules.

The instruction to make the adjustment as part of the annual adjustment does not appear to be based on the regulations – a "payback" adjustment under reg.109 would properly fall in the period in which the change of intended use happens.

www.gov.uk/guidance/vat-exemption-and-partial-exemption#if-you-move-your-own-goods-from-great-britain-to-northern-ireland

4.3.1.4 VAT groups

HMRC have updated the Notice *Group and divisional registration* to explain the consequences of a group having members established in Northern Ireland and Great Britain. In effect, the group is still treated as a single entity, but a single entity now has to account for VAT when goods are moved across the Irish Sea. The same applies to groups, as the Notice explains:

UK VAT groups can continue to include members that are established in Northern Ireland as well as members that are established in Great Britain. However, there are a small number of changes to the way in which a VAT group will operate when they move goods from Great Britain to Northern Ireland, or where goods in Northern Ireland are sold between members.

Usually, supplies of goods between members of a VAT group are disregarded for VAT. This means that the group does not have to account for VAT on the supply. However, where goods are supplied between members of a VAT group, and those goods move from Great Britain to Northern Ireland, VAT will now be due in the same way as when a business moves its own goods.

Where supplies of goods are made between members of a VAT group, and those goods are located in Northern Ireland at the time that they are supplied, these will only be disregarded if both members are established, or have a fixed establishment, in Northern Ireland. Where one or both members only have establishments in Great Britain, the disregard will not apply and VAT must be accounted for by the representative member. This VAT may be reclaimed subject to the normal rules.

Notice 700/2

4.3.1.5 Valuing goods for import VAT

The online guidance on valuing goods for import VAT has also been updated to point out that "There are additional considerations for goods you move into Northern Ireland."

If you move goods into Northern Ireland that are 'at risk' of onward movement to the EU, you may have to pay the applicable customs duty.

The VAT due should be calculated on the customs value including any duties due.

You should continue to work out the customs value and add the VAT value of your goods to box 22 of your import declaration as normal.

The concept of "at risk of moving to the EU" is explained at www.gov.uk/guidance/check-if-you-can-declare-goods-you-bring-into-northern-ireland-not-at-risk-of-moving-to-the-eu; and the customs value is explained in Notice 252, both accessed through hyperlinks from the online guidance.

www.gov.uk/guidance/how-to-value-goods-for-import-vat

4.3.2 Northern Ireland Protocol

The Northern Ireland Protocol Bill, published on 13 June 2022, aims to amend the operation of the Northern Ireland Protocol in the domestic law of the UK. It will disapply elements of the Protocol, and provide delegated powers to government ministers to make new law in connection with the Protocol, including where provisions cease to have effect in the UK and to implement any agreement with the EU regarding the Protocol.

The aim of the legislation is to simplify the rules relating to goods crossing the Irish Sea, in particular where the goods will remain within the United Kingdom, and to allow Northern Ireland to benefit from the same tax and spending policies as the rest of the UK in relation to VAT, for example the VAT reductions on installation of energy-saving materials.

The passage of the Bill will be controversial because of its unilateral amendment of the Brexit agreements with the EU.

4.3.3 Problems with VAT returns for imports

HMRC have updated their online guidance to reflect problems that some importers had problems accessing March 2022 statements. They say that the issue has now been identified and resolved and March 2022 statements should be available to download. The guidance goes on:

"*If you are still experiencing problems with your statements, contact the imports and exports helpline.*

You can estimate your import VAT figures for the months you cannot access statements for.

Your estimate should be as accurate as possible, based on the amount you've paid for the goods and any other costs you agreed to cover. For example:

- *packaging*
- *transport*
- *insurance*

Your estimate can include any customs duties due on the goods, but it does not have to do so.

Once you can access the service and get your statement, you'll need to make an adjustment to reflect the difference from your estimate, and account for this on your next return."

The guidance goes on to refer to "technical difficulties" with April 2022 statements – statements downloaded before 16 May 2022 should not be used to prepare VAT returns, but a replacement statement should be downloaded after that date.

www.gov.uk/guidance/complete-your-vat-return-to-account-for-import-vat#access

4.3.4 Indirect exports

HMRC have updated their *VAT Exports Manual* to clarify the wording that describes "indirect exports". This now says:

An indirect export occurs when your overseas customer or their agent collects or arranges for the collection of the commercial goods from you the supplier within the UK and then takes them outside the of the UK. This includes goods collected ex-works.

Commercial goods means goods which are exported for a commercial purpose by a business customer and not goods intended for the personal use of the customer.

If your customer does not have a business establishment in the UK the supply is eligible for zero rating as an indirect export even if that customer is VAT registered in the UK.

The Manual goes on to cite the law that defines indirect exports (VATA 1994 s.30(8) and SI 1995/2518 reg.129).

VEXP20300

4.3.5 Simplified Import VAT Accounting (SIVA)

HMRC have updated their guidance on applying for SIVA to include details in relation to the Customs Handling of Import and Export Freight (CHIEF) system from 1 October 2022.

From 1 October 2022, businesses will no longer be able to make import declarations on the CHIEF system. Instead, they will need to use the Customs Declaration Service. If businesses already make import declarations using CHIEF, HMRC will transfer their existing customs authorisations to the Customs Declaration Service. Businesses do not

need to apply for a new authorisation to use the Customs Declaration Service if they already hold an active authorisation. This means that:

- to make declarations on Customs Declaration Service, businesses must use the reference number HMRC has already given to them;
- their existing authorisation letter remains valid.

www.gov.uk/guidance/vat-and-import-duty-reducing-financial-guarantees

4.4 European rules

4.4.1 Documentation

In the context of a sale and leaseback transaction in Slovenia, a dispute arose as to whether the documents created by the supplier constituted a "VAT invoice", giving rise to an obligation to pay output tax and an entitlement to deduct input tax. Questions were referred to the CJEU, where A-G Rantos has given an opinion.

Art.203 PVD states that "'VAT is payable by any person who mentions this tax on an invoice". Art.218 states that "For the purposes of this Directive, Member States shall accept as invoices all documents or messages on paper or in electronic format which fulfill the conditions determined by this Chapter." Art.219 adds "Any document or message which modifies the initial invoice and refers to it in a specific and unequivocal manner is assimilated to an invoice." The information required for inclusion on a VAT invoice is set out in art.226(7) and (9).

A company (RED) owned some land in Ljubljana. In order to finance some new construction, it entered into a sale and leaseback transaction with another company, R: in November 2007, R undertook to buy the property from RED, and RED undertook to pay monthly instalments totalling nearly €1.3 million. The contract indicated that VAT on the transaction would be €110,000, but R did not provide RED with a VAT invoice, and did not declare or pay the VAT. RED claimed a deduction on the basis that the contract itself constituted an invoice within PVD art.203.

By a second contract dated 3 days after the first, RED concluded a contract for sale of the property. RED issued a VAT invoice to R, and R deducted this as input tax. Two years later, the parties agreed to terminate the leasing agreement after RED had failed to meet its obligations. R subsequently sold the property to another buyer at a price including VAT.

Following an enquiry, the tax authorities raised an assessment on RED to deny the deduction it had claimed on the first contract. This would appear to negate the loss of tax revenue from R's failure to account for output tax. However, the tax authority also ordered R to pay interest on the tax debt, on the basis that it had been liable to account for output tax from the conclusion of the contract. R appealed, arguing that no invoice had been issued.

The A-G examined the various requirements of the PVD and their purposes, which were to protect tax revenue by ensuring that a person who charged VAT was liable to pay it to the authorities, and that the authorities could check that VAT deducted had been accounted for by the supplier. After detailed discussion, the A-G concluded that a written contract could be considered an invoice for the purpose of the PVD, even if it did not contain all the data listed in art.226, if sufficient elements were indicated in the document to allow the authorities to check the payment of the tax due and, where applicable, the right to deduct input tax.

CJEU (A-G) (Case C-235/21): *Raiffeisen Leasing v Republic of Slovenia*

4.4.2 Customs debt

A company acted as customs representative for two Italian importing companies. In 2017 and 2018 it was assessed for customs duties and import VAT due on importations by the companies (one of which was in insolvency proceedings), on the basis that it was jointly and severally liable for the levies. The assessments were based on corrections of import declarations that the Italian tax authorities considered were inaccurate.

The company appealed, arguing that joint and several liability of a representative does not apply to VAT, but only to customs duty. It is not mentioned in PVD art.201. The Italian court was not sure whether the national law would have to explicitly state that an import agent was jointly and severally liable in order for that liability to apply, so it referred questions to the CJEU.

After dismissing an objection from the Italian government on admissibility, the court considered first whether the Customs Code provisions applied directly to VAT. Examining the words of art.77(3) of the code and also the context and objectives of the regulations, the court concluded that the Code only applied to the customs debt itself, not to VAT. The PVD did not import the provisions of the Code in determining who was liable for import VAT.

The question then was whether the PVD itself allowed Italy to require the import agent to pay the VAT without an express provision for joint and several liability. The court held that it was permissible for a Member State to so designate an import agent, but the principle of legal certainty required that such a measure should be established, explicitly and unequivocally, in the national law. It was for the referring court to determine whether this was the case, but the implication of the judgment is that the Italian law did not satisfy this requirement.

CJEU (Case C-714/20): *U.I. Srl v Agenzia delle dogane e dei monopoli – Ufficio delle dogane di Venezia*

4.4.3 Limitations on Kittel

A-G Kokott has given an opinion in a case referred from Lithuania about the extent to which a purchaser of goods can be refused an input tax deduction because it “knew or ought to have known” that the output tax would not be paid. The A-G starts by stating that the well-known principle that is used to combat fraud appears to have been extended by Lithuania to cover purchases from businesses that are experiencing financial difficulties.

The present dispute arose in the context of a forced sale of real estate by an insolvent developer. A company had taken over the rights of a bank that originally made a loan to the developer, and when no one bid for the land in an auction, it was sold to the company at a valuation of €5.468 million. The seller drew up a VAT invoice showing this as a gross amount, and the buyer deducted it as input tax, but (as everyone must have expected) the output tax was not paid to the authorities by the seller, because it was insolvent.

The authorities regarded the claim for input tax as an abuse of rights and refused repayment, as well as charging interest for late payment and a

penalty. The company appealed, and in due course questions were referred to the CJEU.

The A-G set out her opinion in sections:

A – Introduction

B – Problems arising from insolvency of taxable persons

C – Whether the doctrine of fraud is relevant in this case

D – Whether the doctrine of abuse of rights is relevant

E – Whether deduction can be denied using art.273 PVD

F – Whether the basic conditions for deduction are met when the value of the supply is not paid for but is set against existing debts

Section B is brief: the case law of the court consistently affirms that the right of the recipient of a supply to deduct input tax continues to exist, in principle, even if the supplier does not use the amount received to pay his or her VAT liability and, due to a lack of assets, the tax authorities cannot successfully enforce that tax liability.

Section C is even briefer: the situation in the present case did not involve a fraud. The fact that a taxable person in financial difficulties sells goods in order to pay off his or her debts and declares the VAT incurred in that context, but subsequently fails to pay it or to pay it in full does not constitute fraud. It could not therefore be alleged against the claimant of input tax that it knew or should have known that it was involved in VAT fraud.

Section D starts with a reminder of the two requirements for a finding of abuse of rights: first, the transactions concerned must result in the accrual of a tax advantage the grant of which would be contrary to the purpose of the VAT Directive, and, second, it must also be apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain that tax advantage.

The A-G noted that the PVD allows Member States to introduce a reverse charge procedure for compulsory (i.e. insolvent) sales of real estate (art.199(1)(g)). She concluded from the existence of a specific provision to this effect that the legislature did not regard the situation as an abuse of rights; if it had, it would not have allowed Member States to deal with the risk to the revenue by specific legal provisions.

The A-G distinguished the present situation from that considered by the CJEU in *Alti OOD* (Case C-4/20). Although the court had made what the A-G described as “far-reaching statements” in that decision, it was in a different context – the allocation of liability under a joint and several liability provision, and the possibility of charging default interest on the amount transferred. If those statements were applied generally, it would render art.199(1)(g) absurd.

Further, the arrangements were not “wholly artificial” – they were the only way in which the company could acquire the assets. It could not pay the net price only, and then pay the VAT to the authorities in order to be able to deduct it, because there was no reverse charge provision in Lithuania.

Lastly, characterising this as an abuse of rights would be tantamount to prohibiting trading with businesses that were in financial difficulties. That could not be right.

In section E, the A-G very quickly dismissed the idea that art.273 could be relevant – that only applies to the prevention of evasion and to ensure the correct collection of VAT. Neither of those circumstances were present in this case.

After dismissing all of the Lithuanian authorities' reasons for disallowing the VAT, the A-G raises her own question of whether the basic conditions for a deduction are met in the first place, as the referring court had apparently assumed. In her view, the claimant of input tax would only be entitled to a deduction if it had borne the VAT, which would not be the case if it had never made the funds available to the tax debtor for the payment of the VAT debt. It would be for the referring court to determine if that was the case.

CJEU (A-G) (Case C-227/21): *'HA.EN.' UAB v Valstybinė mokesčių inspekcija*

4.4.4 Reduced rate

A temporary reduced rate was available for labour-intensive services under art.106 – 107 and Annex III PVD. The applicable rules have been examined in a case referred from Portugal, but as the provisions were repealed in 2009, the case is of historical interest only. The question was whether repairing and renovating lifts in residential apartments qualified, when the Annex referred to "repair and renovation of private dwellings". The court was satisfied that facilities shared by all the residents of an apartment block were part of the "private dwellings" and therefore qualified for the reduced rate. Routine maintenance would not qualify.

CJEU (Case C-218/21): *AutoridadeTributária e Aduaneira v DSR – Montagem e Manutenção de Ascensores e Escadas Rolantes SA*

4.4.5 Double jeopardy

A sole trader accountant was found guilty of tax and VAT evasion and sentenced to imprisonment. He appealed on the grounds that he had already been subject to a tax penalty which, for the purposes of human rights law, was a criminal penalty. He was therefore being punished twice for the same crime. Questions were referred to the CJEU on the proportionality of the penalty rules and their compliance with the Charter on Human Rights.

After detailed examination and discussion of the issues, the answer is vague: the fact that there might be custodial and financial penalties for the same offence was not contrary to the Charter, provided that the possibility of such a duplication was reasonably foreseeable at the time when the offence was committed; but national legislation must ensure that the combined punishments do not exceed the seriousness of the offence identified.

CJEU (Case C-570/20): *BV v Direction départementale des finances publiques de la Haute-Savoie*

4.4.6 Import VAT on confiscated goods

Under art.124(1)(e) of the Customs Code, a customs debt is extinguished where goods are a confiscated or seized and subsequently confiscated. A Lithuanian smuggler protested at being charged import VAT and excise duty on cigarettes that he had smuggled into the country from Belarus, only to have them confiscated and destroyed. The referring court was not sure whether art.124(1)(e) applied if the goods had passed the border (i.e. the debt was only extinguished if the goods were confiscated at the point of introduction), and also what the consequences were for VAT and excise duties.

The court considered the history of the provision and concluded that the time of seizure was not relevant – the customs debt was extinguished. However, fines and penalties for failure to comply with customs legislation could be imposed in addition.

By contrast, the excise duty and VAT laws did not provide for debts to be extinguished. They arose at the time of importation, because there was an assumption that the goods had been released to free circulation. In the absence of any provisions requiring the debts to be cancelled, they remained due.

CJEU (Case C-489/20): *UB v Kauno teritorinė muitinė*

4.4.7 Wrong chain

A Netherlands company, B, purchased goods from BOP, a Polish company, and resold them to its own customers located in other Member States. B treated the purchase from BOP as a domestic transaction and its own supply as an intra-community despatch; the Polish authorities considered that the supply by BOP was the despatch because the transport was made directly from BOP to the end customers. B had supplied a Polish VAT number in relation to its purchases; it could not provide the Polish authorities with evidence that it had accounted for acquisition tax in the destination countries (because it had not done so – its customers had); so the Polish authorities demanded "fallback acquisition tax" from B. The national court considered that this raised the possibility of double taxation, and referred questions to the CJEU. Advocate-General Emiliou has given an opinion.

The company argued in the national court that art.41 PVD, which imposes the fallback charge, only applies to cross-border transactions – that is, where the customer has secured a VAT-free supply by quoting a VAT number from a different country. It should not apply in the situation here, because B had quoted a Polish VAT number and had therefore received a domestic Polish supply. VAT had been paid at every stage, and there was no fraud.

The A-G noted that the company relied on art.36a PVD, which ascribes the transport in a chain such as this to the first supply (i.e. BOP to B), if and only if the intermediary has notified the first supplier of a VAT number issued by the country in which the transport starts – which it had done. However, art.36a was introduced by Directive 2018/1910 to take effect from 1 January 2020, after the transactions concerned in the case. It was clear from the workings leading up to that Directive that the existing case law did not determine the ascription of the transport to the supply

with clarity. The A-G considered that it would be for the referring court to consider that ascription in the light of pre-existing case law (e.g. *Euro Tyre Holding* (Case C-430/09)).

The A-G went on to comment on the application of art.41 if the court decided to ascribe the transport to BOP's supply to B (i.e. to treat that as an intra-community despatch). The rationale of art.41 was to transfer the taxation of the goods to the destination country, while avoiding double taxation through the operation of art.40.

The A-G next considered the question of whether, as B contended, art.41 had no application where the customer uses a VRN of the supplier's own country. In his view it did not. He noted that this was not a normal situation: it would be more usual for a Netherlands customer to use the Netherlands VAT number and apply the triangulation simplification. However, the use of a Polish VAT number did not rule out BOP's supply being a despatch for acquisition, because it involved intra-community transport. The use of a Polish VAT number before 1 January 2020 did not negate that.

The A-G also considered that the operation of art.41 could not be negated by the acquisition tax being accounted for by B's customers in the destination countries. The requirements of the law were for B to account for the acquisition tax; what its customers did was a separate mater.

The A-G agreed with the referring court and the Commission that this created a disproportionate tax burden for B. Because B had used a Polish VAT number, the tax authority ruled that BOP's intra-community supply was not exempt; it was therefore subject to 23% tax on the purchase (which BOP had already charged), as well as the fallback acquisition tax, and it was not permitted to deduct it. Art.41 was part of the broad system of the VAT Directive which ensured the collection of VAT in the place of consumption. The measures adopted by the Member States to ensure correct levying and collection of tax and prevention of fraud could not be used in such a way as to undermine the neutrality of the tax and impose unequal treatment on operators carrying out the same transactions. The principle of proportionality required that measures went no further than was necessary to achieve their purpose.

Art.41 applied to prevent evasion and fraud by ensuring that there was a tax charge somewhere following an exempt intra-community despatch. The A-G considered that it could not be used if the intra-community despatch was not exempt. That obviously created double taxation, which was against the principles of VAT, but it was rather a question of art.41 being used in a way that exceeded its purpose.

This could have been avoided by the use of triangulation, and should in future be avoided by the use of art.36a.

CJEU (A-G) (Case C-696/20): *B. v Dyrektor Izby Skarbowej w W.*

4.4.8 Liability of directors

A-G Kokott has given an opinion in a case referred from Bulgaria concerning a national law that transferred the liability of a taxable person to someone who caused that taxable person to be unable to meet its obligations - the directors of a company, for example. The question was whether this was a purely national, procedural regime for safeguarding tax

revenue, not affected by EU law, or was something that was governed by the Directive.

Art.205 PVD provides for Member States to make certain third parties jointly and severally liable for a taxable person's VAT in defined circumstances, but they do not refer to executive directors of companies or the case where an inappropriate salary is paid. Art.273 gives a more general discretion to introduce measures to ensure the correct collection of VAT and to prevent evasion, as long as they do not go further than is necessary to achieve the objective stated. After consideration of the logical basis of both provisions, the A-G concluded that neither of them allowed for a non-taxable person to be made liable for the VAT of a taxable person as the Bulgarian law provided.

This was in fact what the Bulgarian government contended: its national provision was not the implementation of VAT law, but rather a measure to punish a breach of fiduciary duties of directors towards their company. Such a breach has, at best, an indirect effect on the payment of VAT by a third party. That indirect connection to VAT was not enough to engage the CJEU's jurisdiction; the court could not answer the questions referred in the present case.

The A-G also considered the possibility that the court would consider that it did have jurisdiction, in which case her view was that the PVD neither required nor prohibited the transfer of liability to the directors. If a director caused an insufficiency of funds to pay VAT by awarding himself an unjustified salary, making him liable for the VAT appeared to be permitted by art.273 – it was a proportionate measure directed at achieving a legitimate objective.

CJEU (A-G) (Case C-1/21): *MC v Direktor na Direktsia 'Obzhalvane i danachno-osiguritelna praktika' Veliko Tarnovo pri Tsentralno upravlenie na Natsionalnata agentsia za prihodite*

4.4.9 Timber and reverse charges

Romania has implemented an optional reverse charge mechanism for sales of timber. The tax authority ruled that the owner of some forest land had exceeded the registration threshold in 2011 and raised an assessment for approximately €41,300 to cover underdeclared output tax for the years from 2011 to 2017. The company objected, arguing that the reverse charge mechanism meant that it should not be liable for the tax. This was initially rejected by the national court on the basis that the mechanism only applied to transactions between registered suppliers and purchasers, but questions were referred to the CJEU to clarify the law.

The referring court was concerned that registration should only be a formal requirement rather than a substantive requirement for exercising the right to a reverse charge mechanism; there was a further problem with fiscal neutrality, as the failure to raise proper invoices at the time would mean that the customer would not be able to deduct the VAT that was payable by this appellant.

The court ruled that the Romanian requirements were not contrary to the VAT Directive. The aim of the restriction was legal certainty and legal clarity, which were proportionate objectives in line with the aim of the provisions (to prevent fraud in the timber market in Romania). As an

exception to the general rules of VAT, the application of the reverse charge mechanism should be strictly applied, and the Romanian rules had that effect.

CJEU (Case C-146/21): *DirecţiaGenerală Regională a Finanţelor Publice Bucureşti – Administraţia Sector 1 a Finanţelor Publice v Direcţia Generalā Regionalā a Finanţelor Publice Bucureşti - Serviciul Soluţionare Contestaţii 1*

4.4.10 Conditions for option to tax

Lithuania has implemented an option to tax supplies of immovable property, but only where the recipient is registered for VAT. In 2020 the tax authority ruled that a taxpayer had incorrectly charged VAT on a 2015 supply because the recipient was not registered; an assessment to disallow input tax was raised, together with penalties and interest.

Questions were referred to the CJEU to clarify whether the Lithuanian restrictions were permitted by the PVD. The referring court had particular doubts because the recipient had applied for VAT registration and was registered one month after the transaction was completed, with no evidence of abuse.

The court noted that the PVD allows Member States to impose conditions on the exercise of the option to tax, and these conditions were within the permitted range. The court rejected arguments based on the distinction between "formal and substantive conditions for the right to deduct": these related to the status of the purchaser in this case, whereas the argument was about the liability of the supplier. The court regarded these as separate issues.

The court also rejected objections to the adjustment of the supplier's input tax as a result of having made an exempt supply. It did not appear excessively difficult or practically impossible to comply with the rules on the option to tax, so the principle of effectiveness was not engaged; there was no evidence that similar transactions in competition with each other had been treated differently, so the principle of fiscal neutrality was also inapplicable. The requirement for the recipient to be VAT-registered complied with the principle of legal certainty, because it was easy for a supplier to know whether the option would be effective or not. This could be contrasted with a rule that was based on the recipient's intended usage of the property, which would be much harder to satisfy: the authorities could not take into account that future use in determining whether an adjustment was required or not. The authorities should, however, consider whether there has been fraud or abuse by the taxable person who sought to exercise the option.

CJEU (Case C-56/21): *UAB 'ARVI' ir ko v Valstybinė mokesčių inspekcija prie Lietuvos Respublikos finansų ministerijos*

4.5 Foreign refund reclaims

4.5.1 Certificate of status

HMRC have changed the way in which they issue a certificate of status of taxable person (VAT66) to UK businesses. From 1 May 2022, they will issue certificates by e-mail, provided that the business has completed an

"informed consent form" and attached it to the request for a V66. The new certificate includes a direct link to the UK VAT registration checker. This allows the refunding tax authority to verify the information provided on the certificate.

The guidance sets out how taxable persons and agents should make the application for the certificate. Paper copies will now only be issued in exceptional circumstances.

www.gov.uk/guidance/get-confirmation-from-hmrc-that-you-are-trading-in-the-uk

5. INPUTS

5.1 Economic activity

Nothing to report.

5.2 Who receives the supply?

Nothing to report.

5.3 Partial exemption

5.3.1 Advertising costs

Two furniture manufacturers were partially exempt because they received insurance commission as well as the proceeds of selling sofas and other furniture. In 2009 one of the manufacturers, DFS, won an argument in the FTT that the costs of various forms of advertising were solely attributable to the taxable sales and none had to be apportioned to the exempt sales (TC00157). If sales of sofas increased, this inevitably led to greater sales of the insurance products, but the advertisements did not refer to insurance and there was therefore no direct and immediate link to the exempt income.

DFS and its competitor, Sofology, applied this decision to advertising costs that had extended since 2009 to include online advertising, specifically Google "search engine services" or "pay per click" advertising. HMRC considered that this was different from the television adverts, poster adverts, booklets and direct mailing literature that had been at issue before the FTT. They put forward alternative arguments about the cost of PPC advertising:

- It was directly and immediately linked both to the taxable supply of sofas and to the exempt supply of insurance intermediary services, in which case it fell to be apportioned according to the company's partial exemption method; or
- It was an overhead, not directly attributable to any particular output but to the business as a whole, in which case it fell to be apportioned as an overhead.

HMRC had raised assessments on Sofology for £35,500 (covering 1/4/2015 to 31/10/2016, raised on 6 June 2019) and on DFS for £371.800 (covering 1/2/2017 to 31/10/2019, issued on 12 February 2021). It was agreed that the FTT should consider the principles rather than the amounts, leaving the parties to agree the details if either of HMRC's arguments succeeded.

Tribunal Judge Tony Beare set out the law on input tax recovery from both the EU and IK legislation. He referred to the concept of a "cost component" as developed in the cases of *BLP Group plc* (Case C-4/94,

CJEU 1995) and *HMRC v Royal Opera House Covent Garden Foundation* (CA 2021). He said:

"*the Court of Appeal made it clear that the reference to "cost components" in Article 1(2) of the Directive does not mean that the cost of the transaction to which the input tax relates needs to be reflected in the prices charged by the taxable person for its taxable supplies (see ROH at paragraph [17]). It said that both "cost components" and objectively determined "purposes" were very general terms which were encapsulated in the "direct and immediate link" test (see ROH at paragraph [18]). Accordingly, although, for the sake of consistency, we will refer throughout this decision solely to the test's being one of a "direct and immediate link" between a cost and a supply, that phrase should be taken to be synonymous with the phrases "cost component" and "used for the purposes of*"."

It was for the national courts to determine whether there was a direct and immediate link, and if so with what outputs. There was:

- A right of deduction where there was a direct and immediate link only with taxable outputs;
- No right of deduction where there was a direct and immediate link only with exempt outputs;
- A requirement for apportionment where there was a direct and immediate link with both kinds of outputs.

On the other hand, there were other costs that did not have a direct and immediate link with outputs at all, including costs incurred in doing something that was deemed not to involve a supply (the TOGC in *Abbey National* case C-408/98) and other activities that did not involve making supplies (the share issue in *Kretztechnik* Case C-465/03 and the purchase of a subsidiary in *Cibo Participations* Case C-16/00). They also included costs that were too general in nature to be capable of being linked to any specific supply, such as the cost of audit and the cost of the office carpet (examples given in the 1999 HL judgment in *Redrow Group plc*). These costs were all categorised as "overheads", having a direct and immediate link with the business as a whole, and are "cost components of the undertaking's products".

The judge listed the following decisions on partial exemption and attribution as "seminal":

- *Southern Primary Housing* (CA 2003);
- *Dial-a-Phone* (CA 2004);
- *Mayflower Theatre Trust* (CA 2006);
- *Royal Opera House* (CA 2021).

He went on to explain the development of principles from those cases, in particular the rejection of a "but for" test as a basis of attribution. In *Southern*, a development company bought land and sold it (exempt) to a housing association, and then carried out development of housing (zero-rated) on the land. There was a link between the cost of purchasing the land and the supplies made under the development contract, but it was not direct and immediate. The direct and immediate link was only with the

land sale, and the input tax was not recoverable at all. The correct approach was to "look at transactions individually, component transaction by component transaction… Only if one transaction is merely ancillary to a main transaction can one disregard the distinct nature of each transaction."

Dial-a-Phone was about advertising costs which contributed to taxable sales of airtime contracts and exempt insurance intermediary supplies. Its adverts specifically referred to a free three-month insurance period, after which the company received a commission. Although there was no reference to paying for insurance after the free period, the adverts clearly attracted the customer to the insurance. The CA approved of the Tribunal's decision that the costs were directly used in both the taxable and the exempt supplies. It did not matter that the insurance supplies were "secondary" to the sales of airtime.

In *Mayflower*, the costs of a theatre production were held to be connected to the sale of tickets (exempt) and the sale of programmes (taxable), but not connected to the sale of sponsorship or refreshments. The link to the programmes was because the contract with the production company included the right to use images of the show in the programmes, and the cost was therefore as much part of the cost of the programmes as the ink and paper. The present judge said that *Mayflower* was authority for the proposition that costs should not lightly be allocated to overheads – they were not linked to the whole of the business, but to particular outputs.

Royal Opera House was significant not only because it was the most recent decision which reaffirmed the earlier principles, but also because the CA rejected the argument (accepted by the FTT) that a "close economic link" was sufficient to constitute a "direct and immediate link".

The judge also reviewed a number of first instance decisions about the link between advertising and particular outputs, including the first *DFS* case, and some others about the method of apportionment where costs were used for more than one output. The review is thorough and will be helpful to anyone researching this area.

After this consideration of the background, the judge turned to the evidence about the particular costs in the case. He explained that the appeal was concerned with two distinct types of pay-per-click advert:

(1) "shopping" adverts, in which the input of a search term by a user leads to photographs on the Google search page of specific products from the relevant retailer's website; and

(2) "search" adverts, in which the input of a search term by a user leads to text adverts in relation to the relevant retailer on the Google search page.

In both cases, by clicking on the relevant photograph or text advert, the user is taken to a page on the retailer's website which is called a "landing page". From the landing page, the user is then able to navigate to other pages on the retailer's website, as desired.

The evidence considered in detail the contractual arrangements with the insurer and the way in which a customer navigated through the websites. The training of staff in selling insurance and the way in which they went about it (for in-store and telephone sales) was also reviewed. The

marketing strategy of each company, including the objectives underlying the strategy, were gleaned from witness evidence.

On that basis, the judge concluded that the purpose of the PPC advertisements was to encourage prospective customers to enter its stores or to enter its website, as opposed to the website or store of a competitor. Neither appellant purchased PPC advertising with the purpose of encouraging prospective customers to purchase insurance.

The way in which insurance was sold suggested it was in every way secondary to the sale of sofas – unless the subject of insurance was raised by the prospective customer himself or herself at an earlier stage, insurance was not to be raised with the prospective customer until he or she had decided to purchase a sofa, for fear of losing the sofa sale. Nevertheless, the sale of insurance was very profitable, and both companies did what they could to increase the "attachment rate" – the percentage of sofa sales that were accompanied by a sale of insurance.

The arguments of the parties were then analysed in detail. The judge considered the relevance of the taxpayer's subjective intention, the relevance of the physical content of the advertisements, and the economic use of the costs in the light of all the facts about the business. The close links between the two products were set out by HMRC's counsel as follows:

…the two categories of supplies in this case were so closely intertwined that it made no sense to say that there was a direct and immediate link to one but not the other. For instance: (1) a customer buying a sofa was, subject to some minor exceptions, always offered insurance;

(2) in respect of Sofology, customers had to opt out of insurance, and not opt in, at the point when the sofa was sold;

(3) in respect of DFS, the staff were incentivised through commissions to offer insurance at the point when the sofa was sold;

(4) the majority of customers who bought a sofa also bought insurance and, as the attachment rates were fairly constant in each case, that meant that the Appellant could predict that outcome with a reasonable degree of certainty;

(5) the sale process was seamless – there was a single customer journey and information gleaned during the negotiations for the sofa was used by the sales staff in order to sell the insurance;

(6) a reduction in sales of insurance would reduce the marketing budget and hence, if all other market factors remained constant, lead to a reduction in sales of sofas; and

(7) in the case of Sofology, the same marketing strapline was used to sell both sofas and insurance.

The arguments were considered in great detail and the reasoning is so dense that it is hard to summarise. However, it seems that the *Royal Opera House* conclusion effectively won this case for the appellants: there was a close economic link between the sales of sofas and the sales of insurance, and there was therefore a close economic link between the advertisements and the sales of both – but the link to insurance sales was not direct and immediate. The advertisements did not mention insurance and did not direct customers towards insurance. This was significantly different from the situation in *Dial-a-Phone*. A number of factors suggested that sales of insurance were driven by what happened after the

customer responded to the advert, not the advert itself (the actions of sales staff).

The judge finished by explaining his rejection of each of HMRC's arguments one by one, and giving the following analogy:

To adopt the analogy of a road journey, if:

(a) a cost is incurred in order to reach destination A;

(b) nearly everyone reaching destination A is sought to be persuaded to continue their journey on to destination B; and

(c) the majority of travellers getting to destination A are in fact persuaded to continue their journey on to destination B,

then the link between the cost incurred in order to reach destination A and destination A is direct and immediate. Similarly, the link between the cost incurred at destination A in order to persuade the travellers to journey on to destination B and destination B is direct and immediate. However, the link between the cost incurred in order to reach destination A and destination B is only indirect. Travellers reaching destination B would not have done so but for incurring the cost of getting to destination A but that is not the relevant test for establishing whether a link is direct and immediate.

Both appeals were allowed.

First-Tier Tribunal (TC08480): *Sofology Ltd and another*

5.3.2 Special Method Override

HCL operated the Hippodrome Casino in central London. It considered that it was required to apply the Standard Method Override (SI 1995/2518 reg.107B) to adjust the recovery of its residual input tax, because the "use" of its residual inputs differed substantially from the apportionment that would be achieved by applying the turnover-based standard method. Over the six years under review, the difference between the standard method and the method suggested by the company was on average nearly £550,000 a year. HMRC rejected the company's method and contended that the standard method produced an acceptable result.

The company's method was based on floor areas used for various activities, adjusted for factors that were relevant to the business. The Hippodrome makes exempt supplies of gaming and taxable supplies of catering and entertainment; some of the catering and entertainment is intended to support the gaming activities. The Tribunal decision considers all of the activities of the casino in detail and sets out the various costs and the method, which will be useful to anyone wishing to consider a similar argument. For example, there is a comparison between the income generated by an electronic roulette table (approximately £400,000 a year) and a dining table in the steak house restaurant (approximately £50,000 a year). The two tables themselves occupied about the same space, but the dining table required considerably more surrounding space to support the activity. The argument, in essence, was that building costs were more appropriately apportioned based on the floor area used for taxable and exempt activities than the turnover generated by those activities, which would be skewed towards exemption because the income generated was higher.

HMRC's response was that the whole purpose of the company was to generate exempt income; its method gave approximately 50% recovery on building costs, when its own returns to the Gaming Commission suggested that 70% of visitors to the building were there for the purposes of gaming.

Judge John Brooks reviewed the operations, the arguments and the precedents. He disagreed with the company's counsel in the correct approach to the question: it was appropriate to start with the company's suggested method, rather than with the standard method, because the SMO should only be used if it gave a "more fair, reasonable and precise proxy of its economic use of its overhead expenditure" than the turnover based standard method. He then set out a number of factors which led him to the conclusion that the supplies of entertainment and hospitality from discrete and defined areas of the Hippodrome could not be regarded as merely an adjunct to, or an amenity for, gaming. Because the majority of the residual costs were property related, the floor area method was fairer than the standard method, and it was therefore to be preferred both for year-on-year recovery and for calculations under the Capital Goods Scheme.

The decision follows precedents, including *VWFS*, in holding that the Tribunal's task is simply to choose between the methods that have been put forward – the standard method for HMRC and the override method (equivalent to a special method) put forward by the company. The Tribunal should not attempt to devise a more precise method as its own alternative. On that basis, the appeal was allowed.

First-Tier Tribunal (TC08441): *Hippodrome Casino Ltd*

5.3.3 Updated Manual

HMRC have updated the *VAT Partial Exemption Manual* to reflect the impact of Brexit on the VAT system. The principles of fiscal neutrality and fair competition are now referred to only in the UK context:

Fiscal neutrality is a key feature of the VAT system. The VAT system must not distort competition between suppliers within the UK.

Fiscal Neutrality and Partial Exemption

For partial exemption (PE), fiscal neutrality means that a taxable person can deduct all the input tax incurred and used in making recoverable supplies and no more.

So when a taxable person who is partly exempt enters the chain of transactions, the tax burden consists of

- *any output tax charged on supplies*

plus

- *the irrecoverable input tax*

The VAT incurred on costs used in making exempt supplies cannot be deducted as input tax. So the taxable person who is partly exempt becomes a final consumer and is burdened with the non-recoverable input tax.

PE23500

5.3.4 Partial Exemption Toolkit

HMRC have updated the *Partial Exemption Toolkit* that is intended for agents to use when completing VAT returns for their clients (but is likely to be too detailed to be practical when completing routine tasks; it is a good document on which to base a thorough systems review).

www.gov.uk/government/publications/hmrc-vat-partial-exemption-toolkit--2

5.4 Cars

5.4.1 Not a qualifying vehicle

A partnership appealed against a decision to disallow input tax of £28,374. The expenditure disallowed included two vehicles, a personalised number plate and clothing. The appeal was made late but HMRC raised no objections and the Tribunal gave permission for it to proceed.

The partnership had been registered from 8 December 2017, with the declared activity being "subcontracting glam/camping, weddings and events". On 29 October 2020, the firm notified HMRC by e-mail that it would include input tax on the purchase of two cars in its October VAT return. It attached an e-mail from its accountants to the effect that input tax could be recovered on a car in exceptional circumstances if it was mainly used as a taxi, for driving instruction or for self-drive hire. The e-mail pointed out that the firm had obtained a Private Hire Operators Licence issued by Cotswold District Council.

The HMRC officer requested insurance documents for the vehicles and a list of invoices to be checked. These showed that the insurance was for "social, domestic and pleasure" use, not for business, and excluded the carriage of passengers for hire or reward. The officer notified the firm that the input tax on the cars was disallowed.

The partners gave evidence that they had other vehicles such as diggers that had similar insurance and only business use. It was not worth contacting the insurers to change the insurance because they would remain on the business premises due to lockdown restrictions. The insurance was later cancelled and replaced with "business only" use, but HMRC maintained their decision on the basis that there had been an intention to make the cars available for private use at the time of purchase.

The clothing was used by one of the partners for Pilates, in which she was training as a teacher. The personalised numberplate was fixed to a motorbike ridden by the other partner, and was claimed as a form of advertising. The officer proposed to allow 50% of the VAT on the clothing, but did not accept that the personalised numberplate was a valid expense of the partnership business, not least because it had the individual partner's name on it.

At the hearing, the partners stated that there was never an intention to use the cars for private hire. It appears that the licence had been obtained under the misapprehension that the possibility of this type of use would

give entitlement to input tax recovery. The fact that the cars were not used because of lockdown was not relevant, because actual use was not the test. Judge W Ruthven Gemmell was satisfied that the firm had not demonstrated that the cars were qualifying vehicles. He also agreed with HMRC that the difference between the name on the numberplate and the name of the VAT registered business meant that there was no demonstrable business purpose.

The judge's comments suggested that he considered the allowance of 50% of the input tax on the clothing to be generous. However, he did not interfere with that decision, as a Tribunal judge does not have the power to increase an assessment in such a circumstance. The appeals were dismissed.

First-Tier Tribunal (TC08496): *Firth and another (trading as Church Farm)*

5.5 Business entertainment

Nothing to report.

5.6 Non-business use of supplies

Nothing to report.

5.7 Bad debt relief

Nothing to report.

5.8 Other input tax problems

Nothing to report.

6. ADMINISTRATION AND PENALTIES

6.1 Group registration

Nothing to report.

6.2 Other registration rules

6.2.1 Updated Manual

HMRC have updated the *Place of Supply of Services Manual* to include further examples of the interaction between reverse charges and registration liability in the UK. The examples are useful reminders of the application of basic principles, including the necessity of non-established businesses claiming any UK VAT back directly from HMRC, and the fact that reverse charges must be accounted for by a registered customer even if the non-established supplier is registered for VAT in the UK for another reason. This is example 4:

A fully taxable UK business is not registered for VAT and to month ending 31 December 2021 has annual taxable turnover of £80,000. The registration threshold is £85,000. During January 2022 the business receives supplies of general rule services from a supplier based in Germany valued at £10,000. These services are taxed under the reverse charge mechanism so the UK business must include this value within its ongoing turnover calculation. This means that by 31 January 2022 the annual taxable turnover has risen to £90,000, resulting in a liability to be registered from VAT at that date. The business registers for VAT from 1 March 2022. The reverse charge is not actually charged on the supply of services from Germany, because the business was not VAT registered at the time they were received. However, any further supplies of general rule services received after 1 March 2022 must be accounted for by the UK business under the reverse charge mechanism.

It is important to note that the German supplier does not have any liability to be registered in the UK. This applies irrespective of whether the UK business is registered for VAT or not.

VATPOSS14700

HMRC have updated the *VAT Registration Manual* to explain that they may set aside the four-year limit on voluntary retrospective registration, because the legislation gives them the power to allow this. However, they go on to say "*In principle, such cases are likely to involve compassionate circumstances, or the survival of the business, but we have not identified to date any case where such circumstances justify a departure from the normal policy.*"

VATREG21300

HMRC have also updated the *VAT Registration Manual* to emphasise that the recipient of a TOGC only takes on the transferor's turnover record for registration purposes if the transferor was a taxable person at the time of the transfer. This produces the following curious example in a section on successive transfers of a business:

A is a taxable person and transfers his business to B who registers for VAT following the transfer. B operates the business for five months and then transfers the business to C. To determine whether he has a liability to register, C must consider:

- *B's turnover for the five months during which he was trading, and*
- *A's turnover in the seven months before the transfer to B.*

Where the transferee of a business has an EDR which pre-dates the TOGC then, as there is no need to determine whether the transferee is liable to register for VAT, the provisions of VAT Act 1994, Section 49(1)(a) do not apply. This means that, for VAT registration purposes, the transferee is not seen as having carried on the business prior to the transfer, so none of the transferor's relevant turnover is deemed to be that of the transferee. This may have a consequential effect on any subsequent TOGC.

In the example above, if B was already registered for VAT at the time that A transferred his business, C would only have to consider B's turnover for the 5-month period to determine his liability to register. This is because B's liability to register was not determined by A's and B is not seen as having carried on A's business prior to the transfer.

VATREG29550

HMRC have updated the *VAT Deregistration Manual* with an example of how they apply the rules to re-register a trader who has misled HMRC into deregistering them. HMRC do not have the power in general to restore a previous registration without the trader's agreement.

On 22 April, a person deregistered but had misled the department when stating their liability to register had ceased. They did this despite the fact that their turnover was still above the VAT registration threshold at the date of deregistration. We will therefore not disregard their previous turnover when calculating their EDR.

If we have their agreement, the original VAT number can be immediately reinstated.

If we do not have agreement to reinstate, we must re-register the person subject to the normal rules.

Timeline	*Date*
Registration threshold exceeded (backward look)	*22 April*
Trader becomes liable to be registered	*30 April*
EDR will be	*1 June*

Schedule 1A and 3A both provide that the EDR is the day liability arose and there is no exclusion of previous supplies from the calculation. Therefore, immediate reinstatement using the original VAT number is permitted if registered under either of these schedules.

VATDREG15000

The above note is referred to from another updated section, where HMRC explain how the law applies to historical turnover tests when a trader has deregistered:

VAT Act 1994, schedule 1, paragraph 1(4) requires that, when determining a person's taxable turnover to establish a liability to register for VAT, any turnover from a period of previous registration is normally to be excluded.

This means that, once deregistered, a person continuing to trade must still refer back to their previous year's turnover at the end of every month. They can, however, disregard any taxable turnover from a previous period of registration.

A person who was previously registered for more than a year can disregard all of that turnover when calculating any future liability to be registered.

A person who was registered for a period of less than a year can disregard their turnover from a period of previous registration but will still have to include any turnover prior to the period of registration that falls within the last year, when calculating any future liability to be registered.

We will, however, not disregard turnover from a period of previous registration where a person has withheld any relevant information or misled the Department at the time of cancellation.

VATREG18150

6.2.2 Article

In an article in *Taxation*, Neil Warren discusses the need for detailed calculations in negotiations with HMRC. He gives three examples from recent dealings with officers:

- A problem with HMRC's systems leading them to incorrectly place a trader on the large payers scheme when turnover was below the limits;
- A client adopting new accounting software to comply with MTD and operating the FRS incorrectly as a result;
- A builder who had exceeded the registration threshold by a small amount, but was able to avoid registration because some of the turnover related to a job done in Ireland.

Taxation, 5 May 2022

6.3 Payments and returns

6.3.1 Late-payment interest rates

HMRC have increased the interest rates for late payments of tax following the Bank of England's decision on 5 May 2022 to increase the bank base rate from 0.75% to 1%, and again following the further increase on 16 June from 1% to 1.25%.

The rate of late-payment interest for most taxes increased to 3.5% from 24 May 2022, and again to 3.75% from 5 July. The repayment interest rate remains at 0.5%.

www.gov.uk/government/publications/rates-and-allowances-hmrc-interest-rates-for-late-and-early-payments/rates-and-allowances-hmrc-interest-rates

6.3.2 Non-standard periods

HMRC have updated the *VAT Guide* to add additional information on how to apply for non-standard tax periods:

"*If your accounting system is not based on calendar months, you can apply in writing to the VAT Registration Service to have tax periods which fit your system more closely.*

Non-standard tax periods can either be monthly or quarterly.

Monthly non-standard tax periods must end 14 days either side of a standard tax period end date.

Quarterly non-standard tax periods must end 20 days either side of a standard tax period date.

If you are already VAT registered and need to change to non-standard tax periods, you must apply in writing about your change of circumstances.

If you have been given approval to use special tax periods, HMRC will provide you with a new VAT registration certificate on your business tax account. Your VAT Returns will show the dates of the approved special periods.

Whatever your tax periods, you must not alter the dates shown on the return."

Notice 700

6.3.3 Updated Manual

HMRC have updated the factors to be taken into account when considering a request for retrospective use of the FRS:

"*The proper exercise of the power to allow retrospection means that we should be prepared to recognise there may be exceptional circumstances where the policy described in the previous bullet should be set aside. In principle, such cases are likely to involve compassionate circumstances, or the survival of the business, but we have not identified to date any case where such circumstances justify a departure from the normal policy. If you think that that there are such circumstances, the case should be sent via a Technical Advice Request with a clearly outlined recommendation.*"

FRS3300

6.4 Repayment claims

6.4.1 Postal claims

The Supreme Court has now given its final ruling on the lead case where a customer of Royal Mail claimed input tax on supplies that had been treated as exempt but were in fact taxable, according to the CJEU judgment in *TNT Post*. HMRC rejected the claim for two reasons, both of which were referred to the CJEU (after proceeding through the UK courts):

- Because the parties had treated the supplies as exempt, and only a net amount had been invoiced and paid, there was no "VAT due and payable" on the supply that could be reclaimed by the customer;
- The customer could only claim input tax with a valid VAT invoice, which Royal Mail had not issued.

The Advocate-General considered that it was the second of these two reasons that ruled out the claim, but the CJEU in its judgment adopted the first. The answer to the question was:

Article 168(a) [PVD] cannot be regarded as being due or paid, within the meaning of that provision, and is therefore not deductible by the taxable person, in the case where, first, that person and its supplier have mistakenly assumed, on the basis of an incorrect interpretation of EU law by the national authorities, that the supplies at issue were exempt from VAT and that, consequently, the invoices issued did not refer to it, in a situation where the contract between those two persons provides that, if that tax were due, the recipient of the supply should bear the cost of it, and, second, no step to recover the VAT was taken in good time, with the result that any action by the supplier and the tax and customs administration to recover the unpaid VAT is time-barred.

As a result of that ruling, the CJEU did not need to consider the necessity of holding a valid tax invoice, and did not answer the question. That meant that the Supreme Court still had to decide, as a matter of purely domestic UK law, whether HMRC should exercise their discretion under SI 1995/2518 to allow the input tax claim. The Supreme Court agreed with the Tribunals and CA decisions that such a repayment would represent a windfall profit to the claimant, and there was "no sound basis on which it would have been appropriate to use public monies to make any such payment". There were up to £1 billion of claims standing behind the lead case.

Supreme Court: *Zipvit Ltd v HMRC*

6.4.2 Second bite at the cherry

In TC07869, a group of claimants had made claims for repayment of output tax on sales of demonstrator vehicles made before November 1992. These had been settled on an estimated basis in about 2007 using what were known as "the Italian Tables" (after the *Italian Republic* case that established that the sales should have been treated as exempt). The claimants sought to make amended claims in about 2016 on the basis that the Italian Tables had contained an error arising from incorrect assumptions in relation to car tax, which had been abolished on 12

November 1992, which meant that the claims relating to sales before that date had been understated when they were first agreed.

The argument was based on a "legitimate expectation" that the claims would not be treated as closed on a materially incorrect basis. The group claimed that HMRC had agreed to pay similar claims made by another trader in July 2018, and this invoked the principle of equal treatment. HMRC argued that the FTT had no jurisdiction to consider claims based on legitimate expectation.

The judge considered the arguments about jurisdiction in detail, and commented that the taxpayers' contentions had some force. They had not been presented to the Upper Tribunal in the *Noor* case, but that did set a binding precedent that the FTT had no jurisdiction to hear an appeal based only on the EU principle of legitimate expectation; that could only be pursued by way of judicial review.

In case he was wrong on that issue, he went on to consider whether the appellants did have a legitimate expectation. In his view, the Italian Tables had clearly been prepared by HMRC to offer traders an alternative to adducing their own detailed evidence. They necessarily contained estimates and could have been inaccurate for any number of reasons. In accepting their use, the traders could not have an expectation that HMRC were giving an unconditional assurance that the result would be accurate.

Nevertheless, the judge was satisfied that the Tables were materially incorrect. There was evidence, including in guidance on the use of the parallel Elida Tables, that supported the argument that the figures produced by the Italian Tables up to November 1992 were wrong. The next question was whether the time for correcting that error had expired. The judge was satisfied that it had. Whether or not the claims were amendments of an existing claim or a new claim, the closure of the *Fleming* window on 31 March 2009 must have extinguished any legitimate expectation that further repayments could be due from periods before 1992.

On the question of equal treatment, the judge was not convinced that it was invoked by a single instance of a decision by HMRC in favour of another taxpayer. However, he did not need to decide that: the burden was on the taxpayer to show that the claim and the circumstances of the other taxpayer were materially identical to their situation, and they had adduced no evidence to show this. They had only shown that another trader had made an *Italian Republic* claim in 2003 and had later sought to claim more, and HMRC had agreed to compromise rather than conclude a Tribunal hearing in July 2018. It was not for HMRC to justify their actions in relation to the other trader, but for the claimants to show that it was unfair to treat them differently.

The appeals were dismissed, and the claimants appealed further to the Upper Tribunal. The judges considered the decision below, the claimants' criticisms of it, and the facts of the case. The decision includes a useful examination of the EU law principles of legitimate expectation, leading to the following summary of principle:

(1) Member states exercising powers given to them in pursuance of Community directives must respect the principle of the protection of legitimate expectations. That principle extends to the situations of

domestic tax authorities exercising the power set out in VAT directives to subject, or not to subject, transactions to VAT.

(2) The question of whether the requisite legitimate expectation exists involves the application of a two-part test.

(3) First, it must be established whether the administrative authority has given precise assurances that would have caused a reasonable expectation in the mind of a reasonably prudent economic operator. That involves the application of an objective test.

(4) Second, it must be established whether that expectation is justified.

The judges considered that they should not interfere with the FTT's evaluative conclusions on the absence of a legitimate expectation. The FTT had made a judgement that the margin of error implicit in the use of the tables was too broad to justify any expectation of the kind the claimants argued for; there were no "true" figures to which the tables could be compared, so it was not possible for them to be "materially inaccurate".

The UT also considered the argument about equal treatment, and agreed with the FTT that this was not engaged by a single instance of HMRC compromising with a claimant in a similar position. There is an interesting discussion of the difficulty of applying the doctrine to a class of traders in a similar position: given that all motor traders making *Italian Republic* claims would be in some ways comparable, it would be impossible for all HMRC decisions to be identical for each claimant. Some decisions were likely to be more favourable than others, but they would not be unequal in the sense required by the legal doctrine. A number of different aspects of the argument were examined, and none helped the claimants.

The appeal was dismissed on all grounds.

Upper Tribunal: *R.T. Rate Ltd and others v HMRC*

6.4.3 Reclaim ruled out

A company had claimed input tax on fees paid to investment managers in relation to a deposit in escrow it had made to reassure the Pensions Regulator about the stability of its pension scheme. In November 2014, HMRC raised an assessment for periods 11/10 to 05/14 to disallow £1.15m of input tax so claimed. The company appealed, but withdrew the appeal in March 2016. After a change of advisers, the company submitted a claim in September 2016 for repayment of input tax of £1.3m for periods 08/12 to 08/16; this was based on the revised understanding of the relationship between a pension scheme and a business following a number of decisions that suggested management costs should be regarded as overheads of the business activity, rather than costs directly associated with a separate non-business activity.

HMRC accepted that the input tax was in principle deductible, but ruled that the periods which overlapped the assessment (08/12 to 05/14, covering £855,754) would not be repaid because the withdrawal of the appeal meant that the parties were deemed to have come to an agreement that the input tax was not deductible, and this could not be reopened. The

company appealed against this decision, and HMRC applied to have the appeal struck out.

The application came before Judge Anne Redston, who considered a long list of procedural issues in detail. These included arguments for the claimant, both of which she rejected:

- That HMRC's case should be struck out because it was wrongly headed as concerning telent Ltd, when the appeal had been taken over by the new representative member of the group, TTSL – this included consideration of the consequences of a change of representative member, which the judge did not consider undermined the validity of the appeal;
- That HMRC were themselves estopped from arguing that the overlap periods were not eligible for repayment because they had conceded that this was not the case in correspondence.

The judge's reasoning on both issues involves a long and detailed examination of precedents on legal procedure, which will be of interest to those involved in litigation. She concluded that HMRC were not estopped from raising the issue of the Tribunal's jurisdiction and therefore applying for strike-out on the grounds that the matter had been determined.

The central issue for the appeal was the interpretation of VATA 1994 s.85(4) read in connection with s.85(1). Subsection (4) states that the withdrawal of an appeal means that the preceding subsections have effect as if the decision under appeal should be upheld without variation; subsection (1) deems an agreement of an appeal without a hearing to have the same effect as if the Tribunal had determined the matter. Both are therefore deeming provisions. The judge examined the interpretation of deeming provisions and the interaction between the various rules on appeals, and preferred HMRC's view – it made more sense if an appellant was prevented from relitigating something after withdrawing an appeal on the same point. She summarised her conclusions as follows:

(1) the Assessment was issued under s 73(1) and in accordance with HMRC's best judgement, it was made on the basis that input tax on the investment management services for the periods 11/10 to 05/14 was not allowable.

(2) the Appellant appealed against the Assessment under s 83(1)(p) on the grounds that the input tax was allowable, there was no dispute about quantum;

(3) the Appellant withdrew the appeal under s 85, the purpose of which is to prevent relitigation; and

(4) the Appellant was deemed by s 85 to have come to an agreement with HMRC that input tax on the investment management services for the periods 11/10 to 05/14 was not allowable and the Tribunal was deemed to have determined that this was the case.

The decision goes into further detail on the precedent case law and the difference between "cause of action estoppel", "issue estoppel" and "abuse of process", all of which resulted in findings for HMRC.

The judge allowed HMRC's application to strike out the part of the appeal against the refusal of the repayment for the overlap period.

First-Tier Tribunal (TC08478): *Telent Technology Services Ltd*

6.4.4 Unjust enrichment of public body

The London Mayor's Office for Policing and Crime (MOPAC) seizes illegally parked vehicles and charges a statutory fee to the owner to release them. In some cases, in particular where the fee is not paid, the car is sold in satisfaction of the fee. It may be auctioned or scrapped. MOPAC agreed the sale price with various dealers and then added VAT; after this had been the practice for some years, MOPAC and HMRC agreed that the transactions were not in the course of business and were therefore not VATable, and MOPAC reclaimed over £4 million in overpaid output tax. HMRC refused the claim on the grounds that it would unjustly enrich MOPAC: the VAT had been charged to VATable persons who would have recovered it as input tax.

MOPAC appealed, mainly relying on the argument that a public body could not be "unjustly enriched" as it would spend the money for the public good. HMRC and MOPAC were both public bodies, and moving money from one to the other would not enrich anyone. Judge Geraint Williams considered this in detail, including the context in EU law, and concluded that the argument could not succeed. There was no concept of "the body public" as a single entity in EU or UK VAT law; MOPAC and HMRC were separate and distinct, and the claim by MOPAC had to be considered in isolation. Viewed in that light, it was clear that MOPAC would be unjustly enriched by a repayment according to the terms of VATA 1994 s.80: it had charged VAT to dealers who would have recovered it from HMRC, which meant that no one was out of pocket. If HMRC repaid the money to MOPAC and MOPAC was entitled to keep it, it would have a gain at HMRC's expense.

The appeal was dismissed.

First-Tier Tribunal (TC08425): *The Mayor's Office for Policing and Crime*

6.5 Timing issues

Nothing to report.

6.6 Records

6.6.1 Domestic reverse charge

HMRC have issued a Brief to explain the ending of the requirement to report information about sales of mobiles or computer chips in the UK which is withdrawn from 1 July 2022. The requirement to use the reverse charge continues to apply, but there will be no need to complete a reverse charge sales list (RCSL).

HMRC explain that they no longer need the data provided through sales lists because the fraud risk has reduced significantly over the years since the introduction of the reverse charge. The department now has other,

more effective, ways of monitoring any residual risk through operational and intelligence activity.

A RCSL still has to be completed for supplies made up to 30 June 2022. This has to be submitted with the return that includes the end of June 2022, and must be done before 17 October 2022. From that date, businesses will no longer be able to access the RCSL system to submit returns or make corrections.

Revenue & Customs Brief 09/2022

HMRC have updated the Notice *Domestic reverse charge procedure* and their *VAT Reverse Charge Manual* to reflect these changes.

Notice 735; *VATREVCHG32000* and *VATREVCHG31000*

The *Value Added Tax (Reverse Charge Sales Statements) (Revocation, Saving and Transitional Provision) Regulations 2022* give legal effect to the changes by revoking SI 1995/2518 regs 23A to 23D which required businesses to compile and submit reverse charge sales lists in relation to supplies of mobile phones and computer chips.

SI 2022/548

6.6.2 MTD penalties

HMRC have published a compliance factsheet on how to avoid penalties for Making Tax Digital for VAT. It sets out the duties of a company under MTD. These are explained in some detail under the following headings:

- File VAT returns using functional compatible software
- Keep records digitally
- Use digital links to transfer or exchange data
- Use the checking functions within their software, and
- Sign up to MTD.

The factsheet describes what the penalties are under each heading:

- Filing – up to £400 per return
- Records and links – between £5 and £15 for every day on which this requirement is not met
- Failure to check – may result in error penalties of up to 100% of the tax lost.

There is no separate penalty for failing to sign up, but presumably that will lead to a failure to file using the appropriate system.

CC/FS69

The ATT has issued a press release criticising these penalties and urging the government to rethink its approach. The chair of ATT's Technical Steering Group said:

"It is disappointing that this is the first time HMRC, since the MTD for VAT rules were introduced over three years ago, have confirmed the penalties which taxpayers can face for getting things wrong. Even now, it seems that HMRC are still not publicising these penalties widely which means any business receiving a penalty could be in for quite a shock.

"The penalties in question are not new measures introduced specifically for the purposes of MTD but are based on existing penalty legislation which has been in place for some time.

"It is inappropriate to apply penalties first introduced over 25 years ago, and designed for a world of pen and paper, to the new digital era of MTD. They are penalties originally designed for an older system, and a new digital system needs new rules which reflect just how different the requirements are."

The ATT considers that the new penalty regime for late payment and filing, to be introduced on 1 January 2023, is a more appropriate and modern system, but the retention of old-style penalties for MTD is

inappropriate. Their main issue appears to be with the daily penalties for non-compliance with the record-keeping requirements.

www.att.org.uk/technical/news/hmrc's-mtd-vat-penalties-are-outdated-unfair-says-att

6.7 Assessments

6.7.1 Best judgement

A take-away business was assessed to output tax of £18,063 for periods from 03/16 to 06/17 on the basis that it had incorrectly treated some sales as zero-rated when they should have been standard rated. HMRC did not allege dishonesty, but said that the errors arose from deficiencies in the company's accounting system. The company accepted that errors had been made, but argued that the amount was excessive. Its accountant produced calculations to support a lower figure of £8,096.

The shop invested in a new coffee machine at the beginning of the period and as a result its business expanded significantly. The gross total sales rose from £27,882 in 03/16 to £82,570 in 06/17. There were a number of admitted deficiencies in the way the till was operated, resulting in the misclassification of SR supplies as ZR.

Judge Richard Chapman reviewed the history of the enquiry and the arguments of the parties. He concluded that the assessment was to best judgement: there had been no allegation of wrongdoing by HMRC, and there was a logical and evidential basis for it. Once that had been established, the burden of proof shifted to the taxpayer, who had produced alternative numbers based on broad assertions rather than evidence. There were no documents to support it and much of the witness evidence was anecdotal and insufficiently detailed. Its calculations were themselves not particularly logical, failing to recognise the possibility of a change in the make-up of sales over the period in spite of the considerable increase in volume.

The appeal was dismissed.

First-Tier Tribunal (TC08422): *Mangio Ltd*

6.7.2 More best judgement

A married couple (later divorced) who ran a convenience store in Blackpool were assessed to VAT and income tax, with associated penalties, in relation to undeclared turnover for periods from 2005 to 2012. The VAT and penalties amounted to nearly £160,000, and the income tax to just under £80,000. Because the period was so long ago, it straddled the changes of penalty rules, and the mitigation allowed is described in terms of both the "old rules" (up to March 2009) and the "new rules" (from April 2009).

Judge Aleksander reviewed the history of the enquiry, which included criminal prosecution and imprisonment of the husband. He did not believe the partners' explanations for the inadequacy of their records (their purchase invoices regularly "blew away when they were unloading their car after visiting the cash and carry"). He was satisfied that they had

acted dishonestly, and they did not have the evidence to displace the officer's best judgement assessments.

The only area where the judge reduced the assessments was in relation to the final period of trading, where he disagreed with the "presumption of continuity" applied by the officer. He considered it credible that the business could have been running down its stock in that period, and suggested an amendment should be made to reflect that. In other respects, the appeal was dismissed.

First-Tier Tribunal (TC08427): *Best On Convenience Store (a firm)*

6.7.3 Undeclared purchases

HMRC carried out an enquiry into a company that supplied food outlets, and noted that the company maintained separate accounts for purchases for some of its customers. Further enquiries were carried out on the customers, including the appellant in the present case. When the supplier realised this, it stopped cooperating with HMRC and refused to provide further information, making a formal complaint that HMRC were damaging its business by upsetting its customers.

HMRC considered that the second account was evidence of purchases that were not being declared by the customer, a takeaway outlet, thereby enabling it to make undeclared sales. The company denied knowledge of the second account, and the supplier offered a different explanation, claiming that the visiting officers had misunderstood what they had been told. However, Judge Anne Fairpo was persuaded that the first account was more likely to be correct, and the alternative explanations were unconvincing.

After detailed examination of the evidence and the basis of HMRC's assessments, she concluded that the assessments were raised to best judgement and the trader could not displace them. Penalties for deliberate and concealed conduct were added, mitigated to some extent for cooperation but not for "telling", as the taxpayer had never admitted wrongdoing. Corporation tax assessments and related penalties were also confirmed.

First-Tier Tribunal (TC08516): *Jin Fu Chinese Takeaway Ltd*

6.8 Penalties and appeals

6.8.1 FTT procedural guidance

The President of the FTT has issued a new Practice Direction explaining how cases will be allocated under Rule 23 of the Tribunals Rules to the four categories of appeal:

- Default paper cases – to be decided without a hearing
- Basic cases – where it is unlikely that there will be significant documentation to exchange before the hearing
- Standard – anything that does not fall into one of the other categories

- Complex cases – where it is likely that there will be voluminous or complex evidence, a lengthy hearing, an important principle at issue or a large financial sum

The fact that a case falls within the descriptions set out in the Practice Direction for a particular category does not mean that the case must, or will, be allocated to that category. A party to a case may make an application regarding its categorisation.

The main points to note are:

- Default paper cases – any dispute where the tax or penalties amount to no more than £500
- Basic cases – most appeals against penalties for late filing or careless error penalties, mitigation and reasonable excuse appeals, appeals against information notices and PAYE coding notices, and applications for permission to make a late appeal, for an appeal to be heard without payment of the tax (hardship), for postponement of tax or for HMRC to close an enquiry (direct tax)
- Complex cases – a hearing is considered "lengthy" if expected to last more than 5 days, and a financial sum is "large" if it exceeds £750,000 of direct taxes or £2 million of indirect taxes

In deciding to allocate a case to the complex category, the Tribunal will take into account all the circumstances, including the implications of the costs-shifting regime (subject to the right of the taxpayer to opt out) and the fact that cases allocated to the Complex category are eligible, subject to various consents, to be transferred to the Upper Tribunal.

www.judiciary.uk/publications/practice-direction-for-the-first-tier-tribunal-tax-chamber-allocation-of-cases-to-categories-in-the-tax-chamber/

The FTT has published guidance on the procedures to be adopted in relation to the issue of witness summonses. The FTT has the power to order witnesses to attend, but this should only normally be used where the witness has already been asked to do so voluntarily and has refused or seems likely to refuse. It should also only be used whether the evidence sought is relevant to the issues in the proceedings.

www.judiciary.uk/announcements/practice-statement-for-the-first-tier-tribunal-tax-chamber-witness-summonses-and-orders-to-produce-documents

The FTT has also published guidance for judges and parties in proceedings in the FTT about the procedure to be followed when a party to a case wishes to rely on oral evidence given by video or telephone by someone who is outside the UK. This follows a 2021 UT decision (*Agbabiaka*), where the judge noted that taking evidence from someone who was at the time in another nation state risked a breach of diplomatic protocols. The Foreign and Commonwealth Office policy is that the giving of oral evidence requires the permission of the other state; written evidence and submissions do not require permission, but there may be a risk that oral submissions would stray into giving evidence.

The guidance note sets out the procedure for seeking permission, and what to do if permission is delayed or refused.

www.judiciary.uk/wp-content/uploads/2022/04/FTT-Tax-Chamber-guidance-Oral-Evidence-from-Abroad.pdf

6.8.2 Upcoming changes to VAT penalties

HMRC have published new guidance on the changes coming to late payment penalties and interest. The new rules will apply to accounting periods starting on or after 1 January 2023. The key points are:

- Late submission on its own will be subject to financial penalties, which has not been the case under default surcharge;
- The penalty for late payment will be lower than under default surcharge, and will be linked to the quality of the lateness;
- Interest will be charged on late paid VAT, and credited on repaid VAT, which has not been the case up to now.

The guidance sets out the details as follows.

Late submission penalties will work on a points-based system. For each VAT return you submit late you will receive one late submission penalty point. Once a penalty threshold is reached, you will receive a £200 penalty and a further £200 penalty for each subsequent late submission.

The late submission penalty points threshold will vary according to your submission frequency.

Submission frequency	*Penalty points threshold*	*Period of compliance*
Annually	*2*	*24 months*
Quarterly	*4*	*12 months*
Monthly	*5*	*6 months*

You will be able to reset your points back to zero if you:

- *submit your returns on or before the due date for your period of compliance – this will be based on your submission frequency*
- *make sure all outstanding returns due for the previous 24 months have been received by HMRC.*

For late payment penalties, the sooner you pay the lower the penalty rate will be.

Up to 15 days overdue

You will not be charged a penalty if you pay the VAT you owe in full or agree a payment plan on or between days 1 and 15.

Between 16 and 30 days overdue

You will receive a first penalty calculated at 2% on the VAT you owe at day 15 if you pay in full or agree a payment plan on or between days 16 and 30.

31 days or more overdue

You will receive a first penalty calculated at 2% on the VAT you owe at day 15 plus 2% on the VAT you owe at day 30.

You will receive a second penalty calculated at a daily rate of 4% per year for the duration of the outstanding balance. This is calculated when the outstanding balance is paid in full or a payment plan is agreed.

Period of familiarisation

To give you time to get used to the changes, we will not be charging a first late payment penalty for the first year from 1 January 2023 until 31 December 2023, if you pay in full within 30 days of your payment due date.

How late payment interest will be charged

From 1 January 2023, HMRC will charge late payment interest from the day your payment is overdue to the day your payment is made in full. Late payment interest is calculated as the Bank of England base rate plus 2.5%.

Introduction of repayment interest

The repayment supplement will be withdrawn from 1 January 2023. For accounting periods starting on or after 1 January 2023, HMRC will pay you repayment interest on any VAT that you are owed. This will be calculated from the day after the due date or the date of submission (whichever is later) and until the day HMRC pays you the repayment VAT amount due to you in full. Repayment interest will be calculated as the Bank of England base rate minus 1%. The minimum rate of repayment interest will always be 0.5% even if the repayment interest calculation results in a lower percentage.

www.gov.uk/guidance/prepare-for-upcoming-changes-to-vat-penalties-and-vat-interest-charges

6.8.3 Strike-out

A company supplied and installed hot water systems and charged the reduced rate on some of the supply on the basis that the systems included some energy-saving elements. In line with the decision in *AN Checker Heating and Service Engineers* (UT 2018), HMRC ruled that the company was liable for the standard rate on the whole supply and raised an assessment. The company appealed, and while the appeal was outstanding, it appears that the company was sold to new owners who were unaware of the liability. They only found out when the Tribunal approached the company to find out whether it intended to continue with the appeal.

The case came before Judge Amanda Brown, who expressed sympathy for the new owners but had no choice but to strike the appeal out. Given the binding precedent on the issue, it had no reasonable prospect of success. The FTT could not be involved in what was in effect a dispute between the purchasers of the company and the previous owners.

The judge noted that HMRC had not levied a penalty, and suggested that they might "look favourably on exercising their discretion not to do so." However, that was a matter solely for them.

First-Tier Tribunal (TC08470): *50 Five (UK) Ltd*

6.8.4 Personal liability notices

On 2 November 2015 HMRC notified a company of a decision to deny the company's claim to zero- rating of 28 dispatches of mobile telephones in VAT periods 02/13, 3/13, 04/13 and 05/13 on the basis that the transactions were part of a tax fraud committed by the company's customer, the company knew or should have known of that fraud, and that the company had not taken every reasonable step within its power to prevent its own participation in that fraud. On the same day, HMRC notified an assessment to £2.959 million plus interest. The company was put into creditors' voluntary liquidation the next day. An appeal was lodged by the company on 2 December, but this was withdrawn by the company's advisers on 9 August 2016 due to lack of funds.

On 4 July 2017 HMRC issued a penalty calculation showing £1.76 million, and a month later issued personal liability notices to the company's officers. After a number of adjustments during the process, the PLNs appealed before the Tribunal by each of the two officers was £877,000.

The FTT considered whether it was appropriate to consider an appeal against the underlying liability of the company, given that its appeal had been withdrawn. HMRC applied for that part of the appeal to be struck out. Judge Tracey Bowler considered the arguments about this and concluded that it would be necessary to examine the same evidence in deciding whether the officers had knowledge or had acted dishonestly. Balancing all the issues, she concluded that it would be appropriate to consider the basis of the assessments on the company, and rejected HMRC's application.

The Tribunal considered HMRC's argument that the company's transactions were connected with fraud. The fraud was executed in Poland "on an industrial scale"; as a result, HMRC could not specify in detail the way in which particular participants acted or how each step of the fraud worked, but they alleged that, on the balance of probabilities, sales to the main company involved must be connected with fraud.

The appellants' defence rested mainly on the argument that they could not be held to have submitted "deliberately" inaccurate VAT returns because they had relied on the conditions of Notice 725 and were not aware of anything else that would deny them the relief.

The judge noted that *Kittel*, cited by HMRC, was not relevant to a case about denial of zero-rating. The key case (also cited) was *Mecsek-Gabona* (Case C-273/11), in which the CJEU held that "it is not contrary to European Union law to require an operator to act in good faith and to take every step which could reasonably be asked of it to satisfy itself that the transaction which it is carrying out does not result in its participation in tax fraud." If the national court was satisfied that the taxable person had not done everything that a reasonable person would do to make sure that it was not participating in tax fraud, then it could be denied relief.

After the usual exhaustive examination of the evidence and argument, the Tribunal concluded that HMRC had not discharged the burden of proof on it to show that the conditions existed for denying the zero-rating of supplies made by the company on the basis of *Mecsek-Gabona* principles, because HMRC have not shown that the transactions were connected to

transactions giving rise to fraudulent VAT losses: the connection was too indirect and circumstantial. If zero-rating could not be denied, the returns were not inaccurate and the penalties fell away.

The decision went on to consider a number of procedural points that had arisen during the course of argument.

First-Tier Tribunal (TC08494): *Sheth and another*

6.8.5 New arguments on appeal

In TC08249, the FTT held that a claimant was not entitled to interest on a repayment of VAT under VATA 1994 s.78 because the late repayment was not due to an "official error". The claimant had not claimed bad debt relief when it suffered bad debts on hire purchase business because, at the time, the UK law required property in the goods to have passed before a BDR claim could be made. This was subsequently found to be contrary to EU law, and HMRC settled retrospective claims for the relief, with interest from the dates BDR was actually claimed; they refused to pay interest from when BDR could have been claimed, and the FTT agreed that the error (the law being incorrect) was not "an error of the Commissioners" (required to engage s.78) but rather an error of Parliament. The company had not claimed BDR at an earlier date not because of a positive action by HMRC, but because it believed that the condition in the law was valid.

The company appealed to the Upper Tribunal on several grounds, and HMRC responded with a number of cross-appeal points. The company objected to HMRC's cross-appeal, arguing that it should have asked the FTT's permission to raise these arguments in an appeal to the UT.

The Upper Tribunal had to consider whether HMRC, having won in the FTT, required permission to appeal against aspects of the FTT decision that it did not agree with. There is a lengthy discussion about the principles that show that a successful party in the FTT cannot appeal, even if unhappy with part of the decision or even the reasons given – the appeal is against the decision itself, not against the reasoning or the contents. The UT summarised the principles as follows:

(1) Appeals lie against the decision, (as identified below).

(2) To identify the decision, one needs to look at the tribunal's jurisdiction and issues put before the tribunal.

(3) A party can only appeal against the decision when it is unsuccessful.

(4) A party who was successful in the decision cannot appeal reasons in that decision that went against it.

(5) It follows from 3) and 4) that a successful party to the decision, as properly identified, cannot appeal other findings or reasoning which were not even part of the reasons in that decision. This includes views of the tribunal on how it would have concluded the decision on the hypothesis that it was wrong in the decision it did make. By definition those are not part of the decision so it does not matter the party was unsuccessful on those.

Applying these principles to the facts of the case, the UT rejected the taxpayer's objections to HMRC's appeal. In respect of one of these

grounds, it was part of the FTT decision in favour of HMRC, so they could not have appealed until the taxpayer did so; in respect of the other, it related to a second issue on which the FTT did not express an opinion because it had already decided for HMRC, so it had not yet been fully argued. As the taxpayer wanted to argue that alternative case again in the UT, HMRC should be allowed to respond.

The appellants' application was dismissed.

Upper Tribunal: *HBOS plc and another v HMRC*

6.9 Other administration issues

6.9.1 Queen's Speech 2022

The Queen's Speech included the announcement of the Brexit Freedoms Bill, which is intended to make it easier for the government to amend or discard brought forward EU law and legal principles. This is likely to include a weakening of the principles that have been used to interpret VAT law, as already announced in relation to claims by a customer for repayment of overpaid VAT directly from HMRC (principle of effectiveness).

6.9.2 Mini umbrella company fraud

HMRC have updated their guidance on "mini umbrella company fraud", which is primarily aimed at exploiting the VAT Flat Rate Scheme and the Employment Allowance. It involves setting up many small companies to supply labour at a low level in the supply chain. The guidance is aimed at encouraging users of labour to carry out due diligence on their supply chains.

www.gov.uk/guidance/mini-umbrella-company-fraud

6.9.3 Tax avoidance arrangements

A UK company and an Isle of Man company with the same name appealed against applications by HMRC for an order under FA 2004 s.314A that arrangements they were promoting were notifiable tax avoidance arrangements for the purposes of FA 2004 s.306.

HMRC argued first that the evidence presented by the companies was no more than hearsay, because it was provided by a tax adviser who was neither an employee or a director of the companies at the relevant time. In the absence of evidence, HMRC considered that the companies could not resist the application. Judge Asif Malek considered this argument to have no merit. In the FTT, hearsay evidence was admissible, and would be given appropriate weight in deciding how reliable it was. On the other hand, the judge did not find the adviser's evidence particularly helpful, as it contained a mixture of submission and opinion, and was "altogether light on the facts".

The scheme was described by HMRC as a "contractor loan scheme", whereby contractors worked for the UK company which invoiced clients, then transferred the proceeds to the Isle of Man company which paid the contractors their national minimum wage entitlement and made a further amount available as an unsecured loan. This type of scheme has been used in the past to obtain benefits under the Flat Rate Scheme where many small companies are registered, but VAT is not mentioned in this decision.

The decision illustrates how the rules on notifiable arrangements and promoters work, including the breadth of the terms. The judge concluded that the application succeeded: the arrangements were notifiable and both companies fell within the definition of promoters.

First-Tier Tribunal (TC08477): *Smartpay Ltd*

Another case concerned a similar argument. The scheme in this case involved “split contracts”, where clients of the promoter worked through a company and received separate amounts for acting as a director (within PAYE) and performing services for the company (on a self-employed basis), as well as unsecured loans from an Isle of Man company. The operation of the scheme is illustrated in the decision with a specific example. The promoters took a fee of about 16% of the gross revenue, leaving the client with 84% rather than the 45% approximately that they previously retained after all taxes.

Judge Nigel Popplewell considered the meaning of “tax advantage”, and rejected an argument by the respondent that it was not possible to compare a situation in which a person received a salary and a person received a loan. In practice, the users of the scheme believed that the loans would never be repaid. After considering a number of arguments in detail, the judge concluded that HMRC’s application should be granted.

First-Tier Tribunal (TC08501): *AML Tax (UK) Ltd and another*

The UK company in the above case was also the subject of a separate application for a penalty for failing to comply with information notices in relation to its corporation tax affairs. The company had not filed tax returns on time and was issued by HMRC with “jeopardy amendments” imposing CT liabilities of over £3m for the 2014 and 2015 periods. The company failed to provide information demanded by HMRC in relation to appeals against those amendments.

The UT describes the procedural history of the dispute, in which the company failed to engage with the proceedings resulting in its being barred from disputing a number of points. The judges (Thomas Scott and Jonathan Cannan) examined the history of the dispute in detail and eventually concluded that an additional penalty of £150,000 should be levied on the company. This was approximately three times the amount that would have been charged based on mere daily penalties, and took into account the high level of uncertainty about the tax at risk.

Upper Tribunal: *HMRC v AML Tax (UK) Ltd*

6.9.4 Prosecutions

Three people have been sentenced to terms of imprisonment of between 8 years and 18 months (suspended for two years) for defrauding the public revenue of over £1 million, mainly by making fraudulent VAT repayment claims through a company after it had gone into liquidation. Some of the falsely claimed input tax was used to buy another business, which soon failed.

www.cps.gov.uk/cps/news/three-fraudsters-sentenced-scamming-taxpayer-out-over-ps1-million

A takeaway owner has been jailed for 18 months for carrying out multiple VAT frauds over many years from at least 2012 onwards, totalling an estimated £171,000. He consistently underdeclared his income and therefore understated his output tax, as well as making claims for tax credits to which he was not entitled.

www.cps.gov.uk/mersey-cheshire/news/take-away-boss-jailed-fraudulent-tax-returns-and-benefit-claims

Three people have been sentenced to terms of imprisonment (one suspended) for involvement in a £17 million missing trader fraud relating to a purported trade in scrap metal, based in Chesham.

www.mynewsdesk.com/uk/hm-revenue-customs-hmrc/pressreleases/17-pounds-million-scrap-metal-fraudsters-jailed-3175353

6.9.5 Consequences of MTIC fraud

The High Court has considered a claim by liquidators of a company that was alleged to have suffered losses through missing trader fraud. The liquidators sought damages against a company with which their company had had dealings in June 2009; that company argued that it was protected by the statute of limitations as the liquidators only attempted to join it in the proceedings in 2017. In very brief summary, it appears that the High Court agreed: the liquidators needed to have acted earlier, and could no longer bring an action against this counterparty.

High Court: *Bilta (UK) Ltd (in liquidation) and others v SVS Securities plc and others*

6.9.6 Private Members' Bills

Sir Christopher Chope MP has once again sponsored bills to try to remove the VAT from supplies of domestic energy and from a wider range of children's clothing. Both had their first reading on 20 June, and have second readings scheduled for 9 September and 24 February, but are extremely unlikely to become law.

https://bills.parliament.uk/bills/3272;
https://bills.parliament.uk/bills/2979