

VAT update (Lecture B1460 – 23.28 minutes)

Hair loss treatment

Summary - The supply of the taxpayer's Kinsey System did not qualify for zero-rating under Group 12 Schedule 8 VATA 1994 as 'significant hair loss or baldness in women is not, in itself, a disability'.

Mark Sharp worked as a hair extension technician and created the Kinsey System for hair loss, named after his friend, Glenn Kinsey.

The pair co-founded Mark Glenn Ltd, trading from premises in London and was registered for VAT from 12 July 2001.

The Kinsey System involves fitting a custom-made wig over the hair loss area together with an additional wig mesh with natural hair drawn through the mesh, thus appearing alongside the wig hair. The hair is then styled and cut, with customers returning for hair maintenance roughly every six weeks.

Based on advice received from their VAT advisors, the company treated the hair loss treatment as zero rated under Schedule 8, Group 12 (Drugs, medicines, aids for the [disabled,] etc) VATA 1994. This covers the supply to a disabled person for domestic or his personal use of certain goods. Subsection 3 extends this to the supply to a disabled person of services of adapting goods to suit their condition and subsection 5 allows the repair or maintenance of such goods. Note 4 confirms that wigs were specifically deemed to be included as a medical appliance.

In 2020, HMRC opened a compliance check and in August 2020, sought information as to whether or not any of the staff were medical practitioners.

The company replied, confirming that none of the staff were medical practitioners but that referrals were received from medical practitioners, with the NHS sometimes paying for the service provided by the company.

In September 2021, HMRC wrote, advising that the company's treatment did not fall to be included as zero-rated under VAT Group 12, which was upheld on review.

The company appealed.

Decision

The First Tier Tribunal found, and both parties agreed, that the supply of the Kinsey System was a supply of services, so the issue was whether item 3 of Group 12 applied – 'The supply to a disabled person of services of adapting goods to suit his condition'

Note 3 states that this section only applies to a 'person who is chronically sick or disabled' which, according to VAT Notice 701/7 means a person with a physical or mental impairment which has a long-term and substantial adverse effect on their ability to carry out everyday activities.

The First Tier Tribunal rejected the argument that significant hair loss in women should be considered a disability. The company failed to produce any evidence that 'baldness in women is considered as a chronic sickness by the medical profession'. Significant hair loss or baldness 'does not necessarily have a long-term and substantial adverse effect upon the ability of an individual to carry out everyday activities.'

The Tribunal found that the Kinsey System was not designed solely for the relief of a severe impairment or severe injury, nor was it the supply of services adapting goods to suit a disabled person's condition. Rather, the Kinsey System was the labour-intensive supply of the fitting of a wig, which allowed for a semi-permanent transformation, with regular maintenance required. It was not the adaptation of a wig.

The Tribunal stated that:

'We find that to consider the Kinsey System as one of services of adapting goods to suit his condition would be to dissect artificially what the Kinsey System does.'

We find that the Kinsey System is a single supply of services and that it does not, therefore, fall within Item 3 of Schedule 8 of Group 12 VATA94.'

This was not the service of adapting goods for a disabled person but rather the supply of a single service followed by a regular maintenance programme. The sums charged were therefore standard rated.

Mark Glenn Ltd v HMRC (TC09255)

Overstated zero rated sales

Summary – The 'rough and ready' approach to calculating the split of sales between zero and non-zero-rated supplies was not accepted by the Tribunal who upheld HMRC's 2% best judgement assessment.

Mr. Babar Saddiq was the sole director and shareholder of B J Shere Khan Star City Limited, a company that operated a restaurant trading as Shere Khan at a leisure and entertainment complex in Birmingham.

In this case, HMRC sought to collect VAT and related penalties in relation to understated sales and overstated zero-rated sales from Shere Khan as well as omitted sales from a second restaurant, called Oodles.

Mr Saddiq stated that Oodles had been closed for refurbishment, with the intention that the modernised premises would operate a Pan-Asian restaurant as a division of B J Shere Khan Star City Limited. The company had been paying £160,000 rent per annum on an empty site that he had personally guaranteed. In order to avoid the rental payments, he had granted a two-year licence to Zahoor Malik and Zeeshan Hamid to run Oodles as an ethnic led concept. They paid the rent and overheads and completed the refurbishment. Mr Saddiq stated that Oodles then traded through two companies, Star City Noodle Bar Limited and Recoverage Limited, with which he was not involved.

On whether there had been suppression of takings at Shere Khan, HMRC argued that a review of bank statements and annual accounts suggested there was such a suppression.

Finally on the zero-rated sales, the Tribunal was told that the restaurant tills did not distinguish between zero rated and standard rated goods. This split was determined at the end of each day by staff members who went through the till receipts to calculate the split, which was claimed to be consistently 12%. Following the calculation, the receipts were destroyed. Mr Saddiq supported the 12% used by stating that:

"The majority of the time, our zero-rated sales came very close to 15% but in order to be careful we used 12% of our total sales as zero rated."

Decision

On whether sales had been omitted sales from Oodles, the First Tier Tribunal found against HMRC. While the Tribunal appreciated that HMRC could have thought that this was the case, based on the evidence supplied, this was no more than a suspicion. The Tribunal found Mr Saddiq's explanation to be credible and plausible.

The First Tier Tribunal did not accept HMRC's assertion of understated sales at Shere Khan. Periods where bank deposits were greater than gross sales declared was not evidence of suppressed sales. These differences were shown to be miscalculations by HMRC and the fact that money was not always regularly banked. HMRC did not challenge this evidence.

The First Tier Tribunal found it unlikely that staff members would calculate by hand the zero-rated supplies each day or twice weekly when the bookkeeper came in, as was alternatively suggested. The Tribunal found that the calculation was "most likely based on a rough and ready method of sampling: hence why the amounts were rounded down to avoid overclaiming."

The Tribunal stated that it was for the appellant to show that the supplies were zero rated, which they had failed to do. Consequently, the Tribunal accepted HMRC's best judgment assessment of 2%, stating that:

"Whilst this figure is quite likely too low, we find the appellant has not discharged the burden of proof, which is on it, to show that a higher figure is appropriate."

Moving to the penalties, the First Tier Tribunal reached the view that the behaviour was careless, rather than deliberate. Further, given the detailed correspondence and calculations provided to HMRC the Tribunal considered the reduction for helping as too little and increased the percentage from 10% to 20%.

Having found that the inaccuracy was not deliberate, the appeal against the Personal Liability Notice was allowed.

B J Shere Khan Star City Limited and Mr. Babar Saddiq v HMRC (TC09244)

Property purchase input tax recovery

Summary – With no indication that the converted flats would be sold, but rather they would be let out on exempt short-term leases, HMRC had been correct to deny the input VAT claim.

In February 2014, Abdul Ghafar bought the Kenthouse Tavern, a pub with residential accommodation upstairs. He paid £645,000 plus VAT, and was VAT registered at the time of the purchase.

In October 2015, he obtained planning permission to create six one-bedroom flats on the first and second floor of the property.

Two months later, Kenthouse Properties Limited was incorporated, with Abdul Ghafar as its sole director and the following occurred:

- March 2016, the property was transferred to the company, for £915,000 but no VAT was charged on the transfer as Abdul Ghafar thought it was a transfer of a going concern (TOGC) as he had opted to tax the building;
- May 2016, the company registered for VAT but this meant that the TOGC conditions had not been met – as the buyer need to be registered for VAT when the transfer took place;
- October 2018, the company opted to tax the property, more than two years after the transfer had taken place.

HMRC collected output tax on the sole trader's business, which Kenthouse Properties Limited reclaimed as input tax on its September 2018 return.

HMRC disallowed the claim, on the basis that the company made wholly exempt supplies of short-term rentals and not zero-rated supplies of the sale of freehold or long leasehold dwellings in a building that has not been used for residential purposes in the previous ten years (Group 5 Schedule 8 VATA 1994). Both its application to register for VAT and form VAT5L confirmed there was no intention to sell the properties but that the flats were to be let out on short leases.

The company claimed that the intention had always been to sell the flats which were taxable supplies, keeping just the ground floor commercial element. With the option to tax in place, these rents would have been standard rated. He claimed that market conditions meant that with no buyers, he was forced to change his plans.

Decision

At the hearing, the First Tier Tribunal commented the company was making submissions on the basis that the property transfer was a TOGC. As the appeal notice made no reference to this, the Tribunal could only consider the input tax reclaim issue actually referenced. The Tribunal commented that if the company considered that the transaction was a TOGC, it would not have made a VAT return claiming input VAT as no input VAT would have arisen.

From the evidence contained within the VAT application and Form VAT5L, the First Tier Tribunal found that the company had intended to make and had only made exempt short term lets. There was no evidence that the company had made 'any attempt to sell the flats' which would then have been zero-rated taxable supplies. The tribunal agreed with HMRC that the input tax claim was linked to exempt rather than taxable supplies and so the input VAT was not recoverable.

The appeal was dismissed.

*Kenthouse Properties Limited v HMRC (TC09250)***Sightseeing packages**

Summary – Visitor passes, combining transport with entry to London attractions, were multi-purpose vouchers rather than tickets, meaning they were outside the scope of VAT.

Go City Limited (formerly the Leisure Pass Group Limited) sold two types of passes, both of which entitled the buyer to enter various attractions at discounted prices and to use certain forms of transport in London without further payment.

The company had a history of appeals with HMRC to decide whether its pass was the supply of an outside the scope voucher at the time the voucher was bought, or a standard rated ticket. Following the implementation of the VAT Voucher Directive (effective from 1 January 2019), and wanting to avoid the disruption of further litigation, the company restructured its passes to ensure they continued to qualify as multi-purpose vouchers and were out of the scope for VAT. Under the restructuring the company believed that they were supplying credits, to be regarded as a preliminary transaction, which was not an aim in itself for customers, with the credits working as follows:

- the company sold a credits package to customers:
- when used for entry, the attraction supplied the company with a right of entry at a fixed rate, with the company making an onward supply of that right to the customer;
- the customer could use a set number of credits based on the standard gate price of the attraction;
- each customer could use a maximum number of credits, which protected the company against heavy users;
- The use of credits was the point at which VAT needed to be considered based on whether the credits had been used on standard-rated, zero-rated or exempt supplies.

HMRC challenged the treatment, raising four assessments in 2021 covering the VAT quarters 3/19 to 12/20 totalling some £9 million.

The company appealed and the parties agreed there were four issues in dispute:

1. Whether the First and Second Assessments were out of time because, when they were issued, it did not appear to HMRC that the VAT returns were incorrect;
2. Whether the supply of passes was outside the scope of VAT because they were Multi-Purpose Vouchers, or whether they failed as they were "instruments functioning as tickets";
3. Whether the supply of the passes was outside the scope of VAT as a result of the company's new contractual arrangements;

4. Where a pass expired without having been used up, whether the entirety of the money received by the company from customers should have been allocated as consideration for its supplies.

Decision

The first two assessments were found to be out of time. Based on the evidence provided, the assessments were issued to protect HMRC's position under the two-year time limit rule, rather than because HMRC had formed a view that the relevant VAT returns were incorrect before the assessments were issued. The assessments were invalid.

Under the rules applying from 2019, the credits were multi-purpose vouchers, outside the scope of VAT when initially supplied. The Tribunal found that the passes were not "instruments functioning as tickets". This was supported by the post Brexit decision in *DSAB* (Case C-637/20), where city passes were found to be multi-purpose vouchers. It would be wrong to class the credits as tickets rather than vouchers as they did not relate to a specific event. The use of the passes depended solely on the decisions taken by the customer.

On the third issue relating to the company's restructuring, the passes were also found to be outside the scope. VAT was not due until the credits were used to enter an attraction.

Finally, HMRC's claim that all of the consideration paid for the passes should be allocated as consideration for supplies, was inconsistent with the legislation and the case law. Where a customer did not use all of their credits, the unallocated part of the payment was not a consideration for supply.

The company's appeal was allowed.

Go City Limited (formerly the Leisure Pass Group Limited) v HMRC (TC09263)

Static caravan DIY builder

Summary – The Tribunal had no powers to consider whether HMRC's decision to refuse a VAT refund could be successfully challenged. Having relied on advice received from HMRC's helpline, the correct approach was through judicial review.

Gregory Sewell lived in the New Forest. Wanting to live close to his son to whom he had essentially given his main property, he decided that it would be easier to get planning consent if he constructed a substantial static caravan.

He contacted HMRC's helpline and was very clear on what he told HMRC over the phone:

- He wanted to build a static caravan on a concrete base;
- He understood the rate of VAT on constructing a building was 0% but on the construction of the caravan, it was 5%.

Having sought advice from a more senior colleague, he was told by the HMRC operator that this was a new build for VAT purposes and hence was zero rated. He was told that even though it was a caravan, it was a permanent structure "so as far as we're concerned that's classed as a new build... Under the VAT Notice 708, section 3 that is dealt with a (sic) new build so it's zero rated".

Following the call, Gregory Sewell made a claim for just over £16,000 under the DIY housebuilders scheme to recover the input tax that he had incurred.

However, there was no doubt that the advice given was wrong and so HMRC refused the claim as caravans were not within the scheme.

Gregory Sewell appealed arguing that HMRC should be required to stand by its advice.

Decision

The Tribunal stated that it was well-established that the correct way for him to challenge misleading advice by HMRC was through the judicial review process.

Despite sympathising with *Gregory Sewell*, *the appeal was dismissed* as the First Tier Tribunal had no jurisdiction to deal with this matter. In the Upper Tribunal decision in *HMRC v Hok Ltd*, the Upper Tribunal made it clear that the First Tier Tribunal “does not have a jurisdiction to enforce any common law duty of a public body to act fairly in administering its statutory powers.”

The case was struck out.

NOTE: The Tribunal stated that the taxpayer might consider pursuing a claim for legitimate expectation that HMRC would honour their advice. However, it was clear that *Gregory Sewell* did not rely on HMRC’s advice to his detriment; he would have constructed the caravan whatever the VAT position.

Gregory Sewell v HMRC (TC09269)