RPC

VAT update

September 2017

In this month's update we report on the Commission's evaluation of invoicing rules; revisions to VAT notice 700/50, concerning default surcharge; and details of the consultation on the Making Tax Digital reforms. We also comment on three recent cases involving the VAT treatment of the Tesco Clubcard scheme; an application to make a late appeal; and guidance on the correct approach to the penalty rules.

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Evaluation of invoicing rules

On 14 September 2016, the Commission published an indicative roadmap on the forthcoming evaluation of Directive 2015/45/EU, amending Directive 2006/112/EC on the common system of VAT and the rules on invoicing. more›

Updated VAT Notice 700/50

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Making Tax Digital

The Government has included proposed legislation in Finance (No.2) Bill 2017, in relation to the Making Tax Digital reforms. more›

Cases

Tesco Freetime – Tribunal applies economic reality to voucher scheme

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Ashington & Ellington Social Club – Tribunal dismisses HMRC's applications to strike out taxpayer appeals

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Any comments or queries?

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About this update

The VAT update is published on the final Thursday of every month, and is written by members of [RPC's Tax Disputes team](#).

We also publish a Tax update on the first Thursday of every month, and a weekly blog, [RPC's Tax Take](#).

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M J Hickey – Taxpayer successfully challenges HMRC's narrow reading of penalty rules

In *M J Hickey Plant Hire and Contracts Ltd v HMRC*, the Upper Tribunal (UT) allowed the taxpayer's appeal and set out the correct approach to the penalty rules applicable to "normal" and "delayed tax" cases, contained in Schedule 24, Finance Act 2007 (FA 2007). more>

News

Evaluation of invoicing rules

On 14 September 2016, the Commission published an indicative roadmap on the forthcoming evaluation of Directive 2015/45/EU, amending Directive 2006/112/EC on the common system of VAT and the rules on invoicing.

The evaluation will assess the impact of the invoicing rules which have been applicable since 1 January 2013 and in particular, will identify, quantify and assess, their impact on all relevant regulatory costs and benefits. It is likely that the evaluation will provide the foundation for the preparation of the Commission's report to the European Parliament, which they are required to present in accordance with Article 237 of Directive 2006/112/EC.

The Commission has invited taxpayers to submit their views on the effectiveness of the invoicing rules by 12 October 2017.

The roadmap, together with a link to the feedback form, is available to view here.

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Updated VAT Notice 700/50

On 1 September 2017, HMRC re-issued VAT Notice 700/50: default surcharge, which explains when a penalty for late payment of a VAT return may be charged and how it is to be calculated.

This notice cancels and replaces VAT Notice 700/50 (September 2016).

The updated notice is available to view here.

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Making Tax Digital

The Government has included proposed legislation in Finance (No.2) Bill 2017, in relation to its Making Tax Digital reforms.

As part of this process, on 13 September 2017, HMRC published a consultation seeking comments on secondary and tertiary legislation relating to income tax and VAT.

Anyone who wishes to comment should send their response to: makingtaxdigital.consultations@hmrc.gsi.gov.uk. The deadline for all responses and comments is 10 November 2017.

The consultation document is available to view here.

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Cases

Tesco Freetime – Tribunal applies economic reality to voucher scheme

In *Tesco Freetime Ltd and Tesco Plc v HMRC*[1], the First-tier Tribunal (FTT) confirmed that the taxpayer was entitled to recover, as input tax, the VAT on facilitation fees charged by third parties for the provision of goods or services to Tesco's customers on the redemption of vouchers under the Tesco Clubcard scheme.

Background

Under the Tesco Clubcard scheme, a member customer earned points on purchases from Tesco, or a third party partner (Reward Partners), when they presented their membership card. These points were converted into vouchers that could be used either to pay for goods in store or online at Tesco.com, or converted into a "reward token" which the customer could use to make purchases from Reward Partners. A typical example would be a free meal at a restaurant.

When tokens were redeemed with Reward Partners, the Reward Partners would invoice Tesco Freetime for a percentage of the value of the tokens redeemed. The question for determination in the appeal was whether Tesco Freetime could recover the VAT charged by the Reward Partners on the amount invoiced for redeeming the tokens as input VAT.

Tesco argued that the various agreements, when properly analysed, showed that the Reward Partners were making supplies to Tesco Freetime, leading to an input tax credit. It relied on the Supreme Court decision in *Aimia Coalition Loyalty UK Ltd (formerly Loyalty Management UK Ltd) v HMRC* (LMUK)[2], which considered the Nectar programme.

HMRC argued (1) that the Tesco Clubcard scheme was gratuitous, in that the Clubcard member paid nothing for the points; and (2) that the payments by Tesco Freetime to the Reward Partners were third-party consideration for the supplies of rewards to the customer.

FTT decision

The FTT allowed Tesco's appeal.

The underlying theme of HMRC's argument, that the Clubcard member was getting "something for nothing" and that there was correspondingly untaxed consumption, was rejected by the FTT.

The FTT recognised that the provision of points to a Clubcard member did not amount to a taxable supply and similarly, the conversion of points into vouchers did not amount to a taxable supply. However, in the FTT's view, that was not the question which had to be determined. The relevant question was whether the customers bore the economic burden of the scheme and in the view of the FTT they did. It was clear to the FTT that the scheme was funded by the customers' taxed payment, since a proportion of what the customers paid for their shopping went towards the cost to Tesco of operating the scheme.

1. [2017] UKFTT 0614 (TC).
2. [2013] UKSC 15.

Much of the argument before the FTT related to the similarities and differences between the Tesco Clubcard arrangements and those of the Nectar scheme. The FTT accepted that there was no meaningful distinction between the arrangements between *LMUK* and the redeemers on the one hand and Tesco Freetime and the Reward Partners on the other. On this basis, and in the light of the dicta of Lord Reed in *LMUK*, the FTT dismissed HMRC's contention that the payments were third party consideration.

Comment

Given the Supreme Court's judgment in *LMUK*, this decision is not surprising. However, due to the amounts at stake and HMRC's desire to distinguish *LMUK*, an appeal seems likely.

The decision is available to view here.

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Ashington & Ellington Social Club – Tribunal dismisses HMRC's applications to strike out taxpayer appeals

In *Ashington & Ellington, Ashstead and Darfield v HMRC*[3], the FTT dismissed HMRC's applications, under Rule 8 of The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (the Tribunal Rules), to strike out the taxpayers' appeals.

Background

This case involved three appeals by Ashington & Ellington Social Club & Institute Limited (Ashington), Ashtead Village Club (Ashtead) and Darfield Road Working Men's Club & Institute Limited (Darfield) (the Appellants). Each appeal concerned a claim for repayment of output tax which had previously been accounted for in respect of gaming machine takings.

Following *HMRC v Rank Group (Rank)*[4], HMRC repaid each of the Appellants together with statutory interest. In doing so, HMRC issued a protective assessment to each under section 80(4A), Value Added Tax Act 1994, to recover the tax and interest repaid in the event that HMRC succeeded in subsequent appeals.

Ashington applied to the FTT for permission to appeal out of time. Ashtead and Darfield argued that they had already appealed in time and only applied for permission to appeal out of time if that was found not to be the case.

HMRC objected to any of the Appellants being given permission to appeal out of time but if any appeal was in existence, it applied to have it struck out, under Rule 8 of the Tribunal Rules, on the ground of no reasonable prospect of success.

FTT decision

Following the recent Supreme Court decision in *BPP Holdings Limited v HMRC*[5], the FTT applied the three-stage approach set out in *Denton v TH White Ltd*[6] (Denton): i) seriousness and significance of the delay; ii) reasons for the non-compliance; and, iii) circumstances of the case.

3. [2017] UKFTT 612 (TC).
4. [2009] EWHC (Ch) 1244.
5. [2017] UKSC 55.
6. [2014] EWCA Civ 906.

Applying *Denton*, the FTT concluded that Ashington's delay of three years and five months to comply with a 30-day appeal time limit was serious. The non-compliance was caused by an administrative error on the part of its advisor who had failed to recognise that Ashington had not received an initial rejection of its claim and so no earlier appeal had been submitted. This was not a good enough reason for non-compliance and in the FTT's view a notice of appeal could have been provided within the 30-day time limit. Allowing Ashington's appeal to proceed would cause HMRC prejudice. On this basis, the FTT refused Ashington's application for permission to appeal out of time.

Ashtead and Darfield were not in the same position. They had appealed and then received a repayment from HMRC following the *Rank* decision. HMRC had then issued protective assessments, under section 80(4A), to recover the repayments in the event that HMRC succeeded in subsequent appeals. The FTT accepted that Ashtead and Darfield thought that their original appeals were still outstanding. It rejected HMRC's argument that it had been made clear to them that HMRC had conceded the original appeals and that they had to appeal the protective assessments.

Accordingly, the FTT decided to amend the original notices of appeal to include an appeal against the protective assessments. The FTT said that even if the original appeals were no longer extant, it would have allowed late appeals.

The FTT rejected HMRC's application to have the Ashtead and Darfield appeals struck out on the ground that they had no reasonable prospect of success. The FTT commented that HMRC had sought to concede the original appeals and it would not have done so had they had no reasonable prospect of success.

Comment

Although HMRC are increasingly making applications to the FTT to have taxpayers' appeals struck out under Rule 8 of the Tribunal Rules, given that HMRC had sought to concede the original appeals, it is surprising that in this case they chose to argue that the taxpayers' appeals against the protective assessments had no reasonable prospect of success.

The decision is available to view here.

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M J Hickey – Taxpayer successfully challenges HMRC's narrow reading of the penalty rules

In *M J Hickey Plant Hire and Contracts Ltd v HMRC*[7], the Upper Tribunal (UT) allowed the taxpayer's appeal and set out the correct approach to the penalty rules applicable to "normal" and "delayed tax" cases, contained in Schedule 24, Finance Act 2007 (FA 2007).

Background

The taxpayer used software to keep its records and prepare its quarterly VAT returns. It decided to adopt a "default" setting in relation to the return dates which stopped the period one day

7. [2017] UKUT 308 (TCC).

short of the required period and put that day at the beginning of the next period. The result was that tax which should have been declared for that last day was declared as part of the return for the next period. This was intended to help the taxpayer's cashflow. This shifting occurred in respect of 15 returns (from 1 December 2009 to 31 August 2013). Nine produced an underpayment of VAT and the remainder an overpayment.

On discovering what had happened, HMRC required the then current period to be dealt with properly and raised a separate assessment for the last day of the previous period (31 August 2013) which would otherwise not have fallen within any return. HMRC also issued a penalty in the final sum of £149,186.

HMRC imposed penalties under paragraph 5, Schedule 24, FA 2007 and took as a base for the penalty the tax that was under-declared for each period for which there had been an under-declaration and then aggregated those under-payments. This was done on a quarter by quarter basis, ignoring the fact that the tax under-declared in one period was declared in a return (and in substance accounted for and paid) in the next period.

The taxpayer disputed the method of calculation and therefore the amount. In its view, the penalty should have been imposed under paragraph 8, Schedule 24, FA 2007, to reflect the fact that the tax was delayed but not avoided.

The point in issue was whether the penalty should be assessed under paragraph 5 (standard penalty) or paragraph 8 (delayed tax).

The taxpayer appealed the penalty assessment to the FTT, which dismissed its appeal. It then appealed to the UT.

The legislation
So far as relevant, paragraphs 5 and 8, Schedule 24, FA 2007, provide as follows:

"Potential lost revenue: normal rule
5 (1) 'The potential lost revenue' in respect of an inaccuracy in a document [(including an inaccuracy attributable to a supply of false information or withholding of information)] or a failure to notify an under-assessment is the additional amount due or payable in respect of tax as a result of correcting the inaccuracy or assessment ...

Potential lost revenue: delayed tax
8 (1) Where an inaccuracy resulted in an amount of tax being declared later than it should have been ('the delayed tax'), the potential lost revenue is –

(a) 5% of the delayed tax for each year of the delay, or

(b) a percentage of the delayed tax, for each separate period of delay of less than a year, equating to 5% per year."

UT decision
The taxpayer's appeal was allowed.

HMRC argued that paragraph 5 referred to an "inaccuracy" in a "document". That meant that every inaccuracy in each separate return had to be considered in isolation. The correcting of the position in the next return was itself an "inaccuracy" in that "document", however, the fact that it was in a sense correcting the position was irrelevant for the purpose of assessing the level of penalties under paragraph 5.

In support of this argument, HMRC referred to various HMRC guidance and practice statements which supported its approach.

The taxpayer argued that the correct approach was that set out in paragraph 8 on the basis that there was one inaccuracy in each quarter which, owing to the nature of the inaccuracy, was split over two returns.

The UT accepted the taxpayer's arguments.

Whilst it was true that a strict reading of paragraph 5 in isolation would tend toward HMRC's interpretation, paragraph 8 existed as an alternative to paragraph 5 in circumstances where the facts made that paragraph relevant.

In the view of the UT, because there was a causal link between the errors between two returns which led to an under-declaration in one and declaration of the missing amount in the next, paragraph 8 was relevant.

Comment
Two important points arise from this case. The first is the specific point that the penalty regime operates in a way which is designed to fit the penalty to the factual and causative nature of events rather than the other way around. The causal connection in the error was critical to the application of paragraph 8 and in arriving at its decision the UT distinguished the case of *Miah v HMRC*[8], where no such causal link was present.

The second is a general reminder that HMRC's guidance and practice notes do not have the force of law. In this case, both before the FTT and the UT, HMRC attempted to use such internal documentation in support of its interpretation of the law. The circularity of such an argument will not be lost on readers and perhaps not surprisingly this argument was given short shrift by the UT.

A copy of the decision is available to view here.

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8. [2016] UKFTT 644 (TC).

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