VAT update

July 2019

In this month's update we report on (1) the revocation of the VAT (Finance) (EU Exit) Order; (2) a recent HMRC Brief that clarifies HMRC's policy on the scope of VAT for transport services; and (3) new regulations which amend the rules on when VAT adjustments may be made following a change to the price of goods and services. We also comment on three recent cases relating to (1) the VAT treatment of 'free' wine supplied as part of a promotional offer; (2) the meaning of "deliberate" and "concealed" behaviour for the purposes of assessment time limits and penalties; and (3) whether investment management fees are recoverable as part of a university's overheads.

News

VAT (Finance) (EU Exit) Order 2019 revoked

On 12 June 2019, the Value Added Tax (Finance) (EU Exit) (Revocation) Order 2019 (SI/2019/1014) was made. The Order revokes the Value Added Tax (Finance) (EU Exit) Order 2019 (SI/2019/43) from 8 July 2019, to permit a change of commencement date using another instrument. more›

Revenue & Customs Brief 3 (2019): the scope of VAT for transport services

On 14 June 2019, HMRC published Revenue & Customs Brief 3/2019, clarifying its policy on the scope of the VAT zero rate for transport services following the Upper Tribunal's decision in *Jigsaw Medical Services Limited v HMRC* [2018] UKUT 0222. more›

New regulations amending the rules on when VAT adjustments may be made following a change to the price of goods and services

On 25 June 2019, the Value Added Tax (Amendment) Regulations 2019 (SI/2019/1048), amending the rules on when VAT adjustments may be made following a change to the price of goods and services, were made. The Regulations will come into force on 1 September 2019. more›

Cases

Marks & Spencer – 'free' wine supplied as a promotional offer was subject to VAT

In *Marks and Spencer plc v HMRC* [2019] UKUT 0182 (TCC), the UT has upheld the First-tier Tribunal's (FTT) decision that wine supplied 'free of charge' as part of a promotion was subject to VAT. more›

Any comments or queries?

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Anthony Leach – taxpayer's behaviour was "deliberate" and "deliberate and concealed" for the purposes of assessment time limits and penalties

In *Anthony Leach v HMRC* [2019] UKFTT 352 (TC), the FTT considered the meaning of "deliberate" behaviour, for the purpose of section 77, Value Added Tax Act 1994 (VATA) (assessment time limits) and the meaning of "deliberate and concealed", for the purposes of Schedule 24, Finance Act 2007 (FA 2007) (penalty provisions). more›

University of Cambridge – VAT on investment management fees were not recoverable as part of the university's overheads

In *HMRC v The Chancellor, Masters and Scholars of the University of Cambridge* (Case C-316/18), the Court of Justice of the European Union (CJEU) has confirmed that in raising and collecting donations and endowments the university was not acting as a taxable person. more›

News

VAT (Finance) (EU Exit) Order 2019 revoked

On 12 June 2019, the Value Added Tax (Finance) (EU Exit) (Revocation) Order 2019 (SI/2019/1014) was made. The Order revokes the Value Added Tax (Finance) (EU Exit) Order 2019 (SI/2019/43) from 8 July 2019, to permit a change of commencement date using another instrument.

The original Order was intended to remove inconsistencies between UK and EU law in relation to the VAT treatment of the management of pension funds and closed-ended collective investment undertakings.

The government still intends to make the changes contained in the original Order, however, it now intends to introduce the changes from a fixed date, expected to be 1 April 2020, rather than from the day on which the UK leaves the EU (exit day), as originally proposed. The reason for the change is to increase certainty (particularly given the uncertainty surrounding exit day) and to provide businesses with time to accommodate the changes.

The Order can be viewed here.

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Revenue & Customs Brief 3 (2019): the scope of VAT for transport services

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The *Jigsaw* case considered whether transport in certain types of 'blue light' emergency ambulances was zero rated. The UT decided that it was not zero rated. However, as a result of judicial comments in the decision (see in particular para 2(2)), HMRC has received a number of queries from service providers seeking clarification of its policy. HMRC has therefore issued Brief 3 setting out its policy and explaining when transport services will be exempt or zero-rated supplies.

Suppliers that provide transport services in emergency vehicles, or in passenger vehicles including those adapted for the carriage of one or more wheelchairs, are advised to review the Brief.

The Brief can be viewed here.

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New regulations amending the rules on when VAT adjustments may be made following a change to the price of goods and services

On 25 June 2019, the Value Added Tax (Amendment) Regulations 2019 (SI/2019/1048), amending the rules on when VAT adjustments may be made following a change to the price of goods and services, were made. The Regulations will come into force on 1 September 2019.

The Regulations amend Regulation 38 of the Value Added Tax Regulations (SI/1995/2518), to provide that a VAT adjustment may only be made following an increase, or a decrease, in consideration for a supply if the supplier provides a debit note, or credit note, containing the information specified in Regulation 15C.

The Regulations also provide, amongst other things, a discretion for HMRC to dispense with or relax the requirements in new Regulation 15C.

The Regulations can be viewed here.

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Cases

Marks & Spencer – 'free' wine supplied as a promotional offer was subject to VAT

In *Marks and Spencer plc v HMRC* [2019] UKUT 0182 (TCC), the UT has upheld the First-tier Tribunal's (FTT) decision that wine supplied 'free of charge' as part of a promotion was subject to VAT.

Background

The appeal related to a promotional offer by Marks & Spencer plc (M&S) described as: "Dine In for Two – £10 – with Free Wine", which allowed customers to purchase three specified food items for £10 and obtain a 'free' bottle of wine or an alternative beverage. To benefit from this promotion, customers were required to pay for the three food items plus the wine within one single till transaction.

The issue was whether the £10 should be apportioned between the food items and the wine, as HMRC contended, or whether, as M&S contended, the wine was supplied free of charge for VAT purposes.

The FTT concluded that the £10 should be apportioned between the food items and the wine. M&S appealed against this decision to the UT.

UT decision

The appeal was dismissed.

The UT agreed with the FTT, that the £10 should be apportioned between the food items and the wine.

The parties accepted that the supply was effected for consideration only if there was a *"direct link between the [goods or] service provided and the consideration received."* (C-16/93 *Tolsma v Inspecteur der Omzetbelasting Leuwarden*).

In the UT's view, the payment of £10 constituted consideration for both the three food items and also for the wine. The UT was of the view that there was a direct link between the provision of the wine and the payment of £10 as the customer would not receive the 'free' wine unless £10 was paid at the till.

The UT also agreed with the FTT that the economic and commercial reality was that M&S was offering a package of four items. Stating that the wine was 'free' was no different, in the same promotional sense, to 'buy two get one free'. M&S would only provide the wine if the customer bought the three food items for £10. The UT considered this analysis was not affected by the fact that a customer would have had to pay £10 for the food items even if the wine was not supplied (either through customer choice or lack of availability). In the UT's view, the position was similar to *National Car Parks Ltd v HMRC* [2019] EWCA Civ 854, where some customers paid £1.50, whereas others paid £2 to park for an hour. The services or goods supplied were the same but the consideration differed according to the particular transaction.

Comment

None of the decided cases on 'free' goods or services, nor HMRC's practice in this area, provides clear and consistent guidance which can be applied to determine the VAT position in any particular case. Each case has to be considered on its own facts.

In circumstances where there is a direct link between the provision of the 'free' item and the payment, it is likely the payment will be apportioned to all of the items, including the notional 'free' item.

The decision can be viewed here.

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Anthony Leach – taxpayer's behaviour was "deliberate" and "deliberate and concealed" for the purposes of assessment time limits and penalties

In *Anthony Leach v HMRC* [2019] UKFTT 352 (TC), the FTT considered the meaning of "deliberate" behaviour, for the purpose of section 77, Value Added Tax Act 1994 (VATA) (assessment time limits) and the meaning of "deliberate and concealed", for the purposes of Schedule 24, Finance Act 2007 (FA 2007) (penalty provisions).

Background

Mr Leach had registered a number of businesses over the years but the only VAT registered business in operation during the relevant period was Mr Leach's sole trader business.

In the periods 05/11 to 11/14, Mr Leach reclaimed VAT of £60,707. He made a reclaim in each quarter. In February 2015, HMRC officers visited Mr Leach and asked for documents to support his VAT reclaims. Mr Leach could not produce any supporting evidence for his input tax claims. He said that he did not keep any records and, after completing each quarter's VAT return, he routinely destroyed all related documents. He said he was unaware that he was required to keep his records for six years.

Following HMRC's visit in February 2015, the business continued to submit VAT returns, but retained the evidence to support the input tax on those returns. Mr Leach's input tax claims dropped significantly. The VAT input tax claim in 2014 was over eight times more than in 2015. Given this significant change, the VAT reclaims also dropped sharply. Taking this into account, HMRC decided that Mr Leach had overclaimed VAT in the past. In the absence of any other reliable evidence, HMRC used the 2015 returns as the basis for calculating the amount of input tax which should have been claimed in earlier periods.

On 7 February 2016, HMRC issued an assessment which was appealed. A penalty was later issued on the basis that Mr Leach's behaviour had been "deliberate and concealed".

Mr Leach appealed the assessment and penalty. He argued, amongst other things, that his behaviour was not "deliberate and concealed" and that he had provided all the evidence needed when requested to do so by HMRC.

Mr Leach failed to attend the substantive hearing. This failure was preceded by three postponement applications (two of which were granted). As the hearing had been postponed on two previous occasions, the FTT considered it was in the interests of justice to continue in Mr Leach's absence.

FTT decision
The appeal was dismissed.

In reaching its conclusion, the FTT considered the following points:

What is the meaning of "deliberate"?
The FTT noted that the meaning of "deliberate" is not defined in either section 77, VATA, or in the penalty provisions contained in Schedule 24, FA 2007. The FTT drew guidance from the *dicta* of the Court of Appeal in *Tooth v HMRC* [2019] EWCA Civ 826 and concluded that the Court of Appeal's analysis applied to section 77 with the effect that there is an extended 20 year time limit where a person knows that the return he is submitting contains an error, even when there is no intention to mislead.

As to the meaning of "deliberate" in Schedule 24, the FTT concluded that the decision in *Auxilium Project Management v HMRC* [2016] UKFTT 249 (TC), was correct. The FTT in that case said that "a deliberate inaccuracy occurs when a taxpayer knowingly provides HMRC with a document that contains an error with the intention that HMRC should rely on it as an accurate document". Thus, for the purposes of Schedule 24, "deliberate" does not have the wide meaning which the Court of Appeal attributed to the word in *Tooth*, for the purposes of the TMA, and which the FTT adopted for the purposes of section 77(4A), VATA.

Assessment
Having decided what is meant by "deliberate" for the purposes of section 77(4A), the FTT decided to uphold the assessment. Mr Leach destroyed the underlying records after completing each return and the FTT therefore inferred that he knew that the figures he was inserting on his returns were not supported by his records.

Penalty
With regard to the penalty, the FTT concluded that Mr Leach had acted deliberately. He knowingly included figures in his VAT return with the intention that HRMC would refund VAT which he knew was not due.

In the view of the FTT, an inaccuracy is "concealed" if the person makes arrangements to conceal the inaccuracy. By destroying the related records, Mr Leach hid the inaccuracy and prevented it from being visible to HMRC.

Special circumstances and proportionality
In his grounds of appeal, Mr Leach argued that the penalty was too high, in other words that it was "disproportionate". The FTT dismissed this argument and concluded that the penalty imposed was entirely proportionate.

Comment
Whilst the findings of the Court of Appeal in *Tooth* were not binding on the FTT because (a) they related to a different statutory provision and (b) they were *obiter*, the FTT considered it appropriate to consider the Court's analysis given the similarity of the statutory wording.

This decision provides helpful analysis on the meaning of "deliberate" and "deliberate and concealed", for the purposes of assessment time limits and penalties.

The decision can be viewed here.

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University of Cambridge – VAT on investment management fees were not recoverable as part of the university's overheads

In *HMRC v The Chancellor, Masters and Scholars of the University of Cambridge* (Case C-316/18), the Court of Justice of the European Union (CJEU) has confirmed that in raising and collecting donations and endowments the university was not acting as a taxable person.

Background

Cambridge University is a charity whose main activity is the VAT exempt supply of education. It also carries on certain activities (eg catering and non-term time accommodation) which are taxable. The university funds its activities by investing donations and applying the returns to its business activities. It pays investment managers to manage these investments and incurs VAT on their fees.

The university sought to recover this VAT by requesting the deduction of input tax incurred on the fund management fees. HMRC rejected this claim and the matter was appealed to the FTT.

The FTT found that the fees for the management of the fund concerned formed part of the university's overheads and accordingly it granted the university's application and held the amounts were deductible. That conclusion was upheld by the UT. HMRC then appealed to the Court of Appeal, who referred the matter to the CJEU.

CJEU decision

In the view of the CJEU, the university could not deduct input tax incurred on the investment management fees as part of its general overheads.

The CJEU observed that in raising and collecting donations and endowments the university was not acting as a taxable person. The donations into the fund were not consideration for an economic activity so that the raising and collection of the funds did not fall within the scope of the VAT Directive. The investment activity (as a means of generating income from donations) was a direct continuation of the non-economic activity and therefore should be treated in the same way for VAT purposes.

The CJEU commented that the fact costs are incurred in the acquisition of a service in the context of a non-economic activity does not, in itself, preclude a right to deduct if those costs are incorporated into the price of a particular output transaction or into the price of goods and services provided in the context of an economic activity (*Kretztechnik AG v Finanzamt Linz (Case C-465/03)*). However, in the present case, it was apparent from the documents that the fees were not so incorporated (nor was there a direct and immediate link between those costs and a particular output transaction, or the activities of the university as a whole).

Comment

This decision accords with the traditional position where a business cannot recover VAT on the costs of making its non-business supplies. Nevertheless, the decision will be disappointing for those taxpayers affected by it.

The decision confirms that establishing a link between expenditure incurred and taxable supplies is essential when it comes to VAT deductibility.

The decision can be viewed here.

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