VAT update

November 2017

In this month's update we report on the Office of Tax Simplification's first report on VAT; the draft regulations concerning the fulfilment house due diligence scheme; and HMRC's revised guidance on input tax deduction for funded occupational pension schemes. We also comment on three recent cases involving a judicial review challenge concerning the exemption of care home supplies; the validity of HMRC information notices; and the conclusion of the long-running *Littlewoods* compound interest case.

News

Office of Tax Simplification publishes its first review on VAT

On 7 November 2017, the Office of Tax Simplification (OTS) published its first report on VAT, setting out a range of proposals for simplifying the tax. The report contains 23 recommendations. more›

Draft fulfilment house due diligence scheme regulations published for comment

On 23 October 2017, HMRC published draft regulations concerning the fulfilment house due diligence scheme. more›

HMRC revises its guidance on input tax deduction for funded occupational pension schemes

On 1 November 2017, HMRC revised its guidance on input tax deduction for funded occupational pension schemes, which is found in the VAT Input Tax Manual (VITM). more›

Cases

Clarke and others – Upper Tribunal refuses permission for judicial review of HMRC's policy on prior misapplication of law

In *The Queen (on the application of R Clarke and others) v HMRC* [2017] UKUT 379, the Upper Tribunal (UT) refused an application for permission to judicially review HMRC's decision not to compensate the claimants beyond the scope of its published policy contained in Business Brief 28/04. more›

The Barty Party – HMRC information notice was invalid

In *The Barty Party Company Ltd v HMRC* [2017] UKFTT 697, the First-tier Tribunal (FTT) allowed the taxpayer's appeal against an information notice which HMRC had issued pursuant to Schedule 36, Finance Act 2008, on the basis that the information notice was invalid. more›

Any comments or queries?

Adam Craggs
Partner
+44 20 3060 6421
adam.craggs@rpc.co.uk

David Gubbay
Partner
+44 20 3060 6050
david.gubbay@rpc.co.uk

Michelle Sloane
Senior Associate
+44 20 3060 6255
michelle.sloane@rpc.co.uk

Nicole Kostic
Associate
+44 20 3060 6340
nicole.kostic@rpc.co.uk

Littlewoods – Supreme Court says "no" to compound interest

In *Littlewoods Ltd v HMRC* [2017] UKSC 70, the Supreme Court has concluded that Littlewoods was not entitled to compound interest on refunds of VAT which it had wrongly paid. more>

About this update

The VAT update is published on the final Thursday of every month, and is written by members of RPC's Tax team.

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

To subscribe to any of our publications, please click here.

News

Office of Tax Simplification publishes its first review on VAT

On 7 November 2017, the Office of Tax Simplification (OTS) published its first report on VAT, setting out a range of proposals for simplifying the tax. The report contains 23 recommendations.

The OTS's core recommendations are:

- the government should examine the current approach to the level and design of the VAT registration threshold, with a view to setting out a future direction of travel for the threshold, including consideration of the potential benefits of a smoothing mechanism;
- HMRC should maintain a programme for further improving the clarity of its guidance and its responsiveness to requests for rulings in areas of uncertainty;
- HMRC should consider ways of reducing the uncertainty and day to day administration of VAT;
- HM Treasury and HMRC should undertake a comprehensive review of the reduced rate, zero-rate and exemption schedules, working with the support of the OTS; and
- HMRC should consider further ways to simplify partial exemption calculations and improve the process of making and agreeing special method applications.

The report is available to view here.

Back to contents>

Draft fulfilment house due diligence scheme regulations published for comment

On 23 October 2017, HMRC published draft regulations concerning the fulfilment house due diligence scheme.

The scheme is to be introduced with effect from 1 April 2018 (other than the provisions concerning obligations and penalties which will come into force on 1 April 2019), by measures included in the Finance (No. 2) Bill 2017 to combat tax evasion by overseas suppliers selling goods through online market places. It applies to businesses that store any goods imported from outside the EU for, or on behalf of, someone outside the EU.

Fulfilment houses will be required to register and submit to specified record keeping and due diligence.

The draft legislation sets out the approval process, obligations and restrictions and the penalties which will apply for failure to comply with the scheme.

The scheme will be of particular interest to businesses concerned with warehousing, storage, fulfilment, importing goods as well as those involved in e-commerce.

HMRC has invited comments on the draft regulations by 15 December 2017 and any comments can be emailed to: indirecttax.projectteam@hmrc.gsi.gov.uk. Emails should be marked 'FHDDS'.

A copy of the draft legislation is available to view here.

Back to contents>

HMRC revises its guidance on input tax deduction for funded occupational pension schemes

On 1 November 2017, HMRC revised its guidance on input tax deduction for funded occupational pension schemes, which is found in the VAT Input Tax Manual (VITM).

The guidance confirms that the so-called 70/30 split concession will not be withdrawn and will be available to employers indefinitely. Under this concession, employers may treat 30% of the VAT element of a third party invoice for the provision of administration and investment services provided in connection with a defined benefit pension scheme as attributable to the administration element and as its input tax.

The VITM also provides guidance on alternative arrangements that may be adopted by employers and scheme trustees, including tripartite contracts between the third party service provider, employer and scheme trustees and the inclusion of the corporate scheme trustee in the employer's VAT group.

The indefinite retention of the 70/30 split concession, will be welcomed by many employers and scheme trustees.

The VITM and the update published on 1 November 2017, is available to view here.

Back to contents>

Cases

Clarke and others – Upper Tribunal refuses permission for judicial review of HMRC's policy on prior misapplication of law

In *The Queen (on the application of R Clarke and others) v HMRC* [2017] UKUT 379, the Upper Tribunal (UT) refused an application for permission to judicially review HMRC's decision not to compensate the claimants beyond the scope of its published policy contained in Business Brief 28/04.

Background

The claimants ran residential care homes for profit. Until 2002, HMRC erroneously treated the supplies of services provided by residential care homes as being exempt from VAT under what was then Group 7, Schedule 9, VATA 1994. The exemption meant that the claimants were not registered for VAT, they did not charge VAT to their customers and they could not reclaim any VAT on the inputs they acquired in order to provide their services.

In *Customs and Excise Commissioners v Kingscrest Associates Ltd & another* [2002] EWHC 410 (Ch), the High Court confirmed that the exemption conferred by VAT did not cover the supplies provided by the care home which had brought the appeal after being refused registration. The care home was therefore entitled to be registered.

In Business Brief 28/04, published in 2004, HMRC said that care homes did not have to register for VAT for the period prior to the *Kingscrest* decision because HMRC was prepared to remit any output tax that care homes were liable to pay on the fees that they had charged their residents. However, a care home could register if it so wished and it would then have to account for VAT to HMRC.

The claimants chose not to register for VAT. However, in 2011, they registered for VAT for the past period and claimed HMRC should forgo all output tax and repay all input tax (a position which was more generous than the policy set out in Business Brief 28/04).

HMRC rejected the claims.

The claimants challenged HMRC's decision arguing that following an erroneous application of the law by HMRC, they had a legitimate expectation that they would be treated more favourably than HMRC's published remedy.

The proceedings began by way of application for permission to seek judicial review to the Administrative Court. They were then transferred to the UT by the Administrative Court.

UT's decision

The UT dismissed the application for permission to commence judicial review.

The UT found there was no representation that HMRC would apply a more favourable policy than had been published. The only legitimate expectation created was that supplies made before *Kingscrest* would be treated as exempt. That expectation had been fulfilled by HMRC's

policy of not insisting that care homes register for VAT for the period prior to the *Kingscrest* decision. Accordingly, there was no legitimate expectation and no conspicuous unfairness.

The UT also considered whether the application had been made in time. The application should have been made within three months of the publication of Business Brief 28/04, as this was the reviewable decision and accordingly, the application was made substantially out of time.

Comment
This decision is a timely reminder that an application for judicial review must be made 'promptly' and 'in any event within 3 months after the grounds to make the claim first arose'. In this case, the individual letters the claimants received were critical to the UT's conclusion on the timing issue. The UT considered the letters were simply reiterations of HMRC's previous conclusion and commented that "claimants cannot manufacture a reviewable decision by a public authority by repeatedly writing to the authority asking for a different decision". In the view of the UT, the application should have been made within three months of publication of Business Brief 28/04.

A copy of the decision is available to view here.

Back to contents>

The Barty Party – HMRC information notice was invalid

In *The Barty Party Company Ltd v HMRC* [2017] UKFTT 697, the First-tier Tribunal (FTT) allowed the taxpayer's appeal against an information notice which HMRC had issued pursuant to Schedule 36, Finance Act 2008, on the basis that the information notice was invalid.

Background
The Barty Party Company Ltd (the taxpayer) runs a public house business in Bath.

In May 2016, HMRC selected the taxpayer for a VAT check and made arrangements to visit the taxpayer's premises. After two postponements, the visit eventually took place on 12 July 2016. During the visit the taxpayer was unable to produce the specific information requested by HMRC, including a current drinks price list and set of purchase invoices for the 04/16 VAT period.

An information notice was first issued to the taxpayer, pursuant to paragraph 1, Schedule 36, Finance Act 2008, on 21 July 2016. This notice was withdrawn on 9 November 2016, due to what HMRC described as an administrative error – no schedule setting out the information required had been attached to the information notice.

A replacement notice, including the missing schedule, was issued to the taxpayer on 10 November 2016 (the Information Notice). The Information Notice requested statutory records for the period 1 February 2012 to 30 April 2016. The taxpayer appealed the Information Notice on the basis that: the information requested was not reasonably required by HMRC (paragraph 1(1), Schedule 36, Finance Act 2008); the VAT periods covered by the Information

Notice went beyond the four year enquiry window (section 77, VATA 1994) and the requirement to provide non–statutory information, ie the drinks price list.

As at the date of the hearing, none of the information requested by HMRC had been provided by the taxpayer.

FTT decision
The appeal was allowed and the Information Notice was treated as invalidly issued.

The FTT noted that in normal circumstances HMRC can only go back four years to issue an assessment, therefore the only information which could reasonably have been requested, as at 10 November 2016, was information relating to VAT periods starting after 1 November 2012. However, as the Information Notice requested records for a period commencing on 1 February 2012, HMRC needed a specific reason to justify requesting information relating to this earlier period. HMRC was unable to provide an explanation as to why information was required beyond the normal four year period.

In the circumstances, the FTT said that it would have expected HMRC to allege careless or deliberate conduct on the part of the taxpayer in order to justify seeking information beyond the four year time period. However, no such suggestion had been made and the taxpayer had already been subject to a VAT check for earlier periods (up to April 2012) which HMRC had failed to take account of when issuing the Information Notice for a period commencing with VAT period 1 February 2012.

In the FTT's view, requesting information for periods outside the normal four year assessment period and for which a VAT check had already been made, without providing a specific reason why information was required for those periods, was a sufficiently fundamental flaw to render the Information Notice invalid in its entirety.

Comment
HMRC can only go back four years when raising a VAT assessment unless there is an allegation that a loss of tax has been brought about due to careless or deliberate conduct on the part of the taxpayer, in which case it can go back six years or 20 years, respectively. If HMRC request information to "check the taxpayer's VAT position" for more than the normal four year period, it will need to provide a specific explanation as to why the information is required, or risk rendering the whole information notice invalid.

A copy of the decision can be found here.

Back to contents>

Littlewoods – Supreme Court says "no" to compound interest

In *Littlewoods Ltd v HMRC* [2017] UKSC 70, the Supreme Court has concluded that Littlewoods was not entitled to compound interest on refunds of VAT which it had wrongly paid.

Background

The case will be familiar to many readers. Between 1974 and 2000, Littlewoods over accounted for VAT on the payment of commissions to catalogue sales agents. It submitted repayment claims to HMRC under section 80, VATA 1994. Between 2005 and 2008, HMRC repaid £205m, together with simple interest, under section 78, VATA 1994, in the sum of £268m.

In 2007, Littlewoods commenced proceedings seeking additional interest, calculated on a compound basis.

The claims were made on the following grounds:

1. restitution of the 'use value' of the money mistakenly paid was due at common law (applying the principle established in *Sempra Metals Ltd v IRC* [2007] UKHL 34); and
2. HMRC was obliged to make restitution on the basis that it had been unjustly enriched (applying the principle established in *Woolwich Equitable Building Society v Inland Revenue Comrs* [1993] AC 70).

Littlewoods contended that its common law claims were not excluded by sections 78 and 80, VATA 1994, as a matter of statutory construction. In any event, it argued that it had a right under EU law to compound interest on any tax that had been levied contrary to EU law.

The proceedings have taken over 10 years, during which time the matter has been considered by the High Court, the CJEU, the Court of Appeal and most recently the Supreme Court.

There were two issues for consideration by the Supreme Court. The first was whether sections 78 and 80 excluded common law compound interest claims under English law and the second issue was whether, if the common law claim was excluded, was that incompatible with EU law.

Supreme Court's judgment

The Supreme Court dismissed the claim.

With regard to the first issue, the Supreme Court concluded that Parliament's intention was to create a complete regime through sections 78 and 80, and a specific right to interest on the repayment of VAT, subject to certain limitations. In the view of the Supreme Court, relying on the common law, as Littlewoods sought to do, would circumvent section 78 and render it effectively meaningless and that could not have been Parliament's intention.

On the second issue, the Supreme Court observed that the CJEU had not expressly stated that compound interest must be awarded, merely that interest in some form was required. It was at the discretion of the member state to determine the method of calculation, subject to the EU principles of equivalence and effectiveness. The Supreme Court further noted that the award of

simple interest is widespread practice among EU member states and it was of the view that, if the CJEU had been seeking to prohibit such an approach, it would have stated this clearly in its 2012 judgment.

In reaching its conclusion, the Supreme Court was influenced by the fact the CJEU had specifically referred to the amount of interest received by Littlewoods and that this was more than 123% of the overpaid VAT. In the view of the Supreme Court, this was an indication that the CJEU considered interest paid on a simple basis to be reasonable redress.

Comment

This is a disappointing judgment for the large number of other taxpayers whose claims for compound interest were stayed behind *Littlewoods*. It is likely that those taxpayers whose claims related to overpaid VAT will decide to discontinue their claims. With regard to claims relating to the overpayment of other taxes, the relevant statutory provisions will need to be carefully considered in order to determine whether compound interest may be claimed.

A copy of the judgment can be found here.

Back to contents>

About RPC

RPC is a modern, progressive and commercially focused City law firm. We have 83 partners and over 600 employees based in London, Hong Kong, Singapore and Bristol.

"... the client-centred modern City legal services business."

At RPC we put our clients and our people at the heart of what we do:

- Best Legal Adviser status every year since 2009
- Best Legal Employer status every year since 2009
- Shortlisted for Law Firm of the Year for two consecutive years
- Top 30 Most Innovative Law Firms in Europe

We have also been shortlisted and won a number of industry awards, including:

- Winner – Overall Best Legal Adviser – Legal Week Best Legal Adviser 2016-17
- Winner – Law Firm of the Year – The British Legal Awards 2015
- Winner – Competition and Regulatory Team of the Year – The British Legal Awards 2015
- Winner – Law Firm of the Year – The Lawyer Awards 2014
- Winner – Law Firm of the Year – Halsbury Legal Awards 2014
- Winner – Commercial Team of the Year – The British Legal Awards 2014
- Winner – Competition Team of the Year – Legal Business Awards 2014

Areas of expertise

- Competition
- Construction & Engineering
- Corporate/M&A/ECM/PE/Funds
- Corporate Insurance
- Dispute Resolution
- Employment
- Finance
- Insurance & Reinsurance
- IP
- Media
- Pensions
- Professional Negligence
- Projects & Outsourcing
- Real Estate
- Regulatory
- Restructuring & Insolvency
- Tax
- Technology

17832

Tower Bridge House
St Katharine's Way
London E1W 1AA
T +44 20 3060 6000

Temple Circus
Temple Way
Bristol BS1 6LW
T +44 20 3060 6000

11/F Three Exchange Square
8 Connaught Place
Central Hong Kong
T +852 2216 7000

12 Marina Boulevard
#38-04 Marina Bay Financial Centre Tower 3
Singapore 018982
T +65 6422 3000

RPC