HMRC Internal Theme Narratives (As at 29 July 2010)

Withdrawn

Fleming: Kretztechnik - general

Background

The European Court of Justice (ECJ) case Kretztechnik AG v Finananzamt Linz c-465-03 (26.5.2005) established that the issue of shares by a public limited company in return for capital invested is not a supply for VAT purposes. In that case the VAT incurred on associated costs was residual input tax because the share issue was carried out by Kretztechnik in order to increase its capital for the benefit of its economic activity in general. As Kretztechnik only made taxable supplies, the input tax was fully recoverable. The subsequent case of Securenta (C-437/06) indicated that a share issue was not automatically connected with taxable supplies, but could also be made to fund a non-economic purpose as well, and in that case a business/non-business apportionment was also needed. Where the business was partly exempt then a proportion, as determined by the partial exemption method in place at the time, could be recovered, HM Revenue & Customs (HMRC) BB12/05 S4 refers. HMRC BB 21/05 S3 subsequently confirmed that as well as cases identical to Kretztechnik the issue of other securities in return for investment capital should also follow the Kretztechnik ruling. For example:

- The issue of types of share other than ordinary shares for example preference shares, special rights issues, bonus issues or scrip dividends, where the purpose of the issue is to raise investment capital for the issuer's business.
- The issue of financial instruments or securities other than shares for example, bonds, debentures when the purpose of the issue is to raise capital for the issuer's business.
- The issue of shares or units in collective investment funds, in return for capital invested in the fund.
- The issue of shares/securities by a type of company other than a public limited company for example, a private company.
- Shares/security issues which take place in the context of wider arrangements for example a takeover or restructuring programme can still be considered to fall under Kretztechnik.

Fleming considerations

Kretztechnik could be relevant in any Fleming claim for input tax in respect of the transactions mentioned above. The claims could arise in any sector but can only be made by the entities issuing the relevant securities.

If you think a claim does relate to the Kretztechnik theme, evidence should be obtained to confirm the following:

- **The nature of the share/security transaction. Is it a first issue?** Examples of evidence could be the share prospectus, annual accounts.
- **That the judgment is being applied appropriately and not to other services**. Are any explicit or implicit charges for other services being

identified – for example, a fund manager's retained 'spread' when issuing units in the fund.

- **That no input tax claims have been previously made in respect of costs now being claimed.** Confirm by reference to historic accounts/VAT return.

Full consideration should also be given to the partial exemption implications to ensure the claim fully reflects both output tax and input tax adjustments.

An aide memoire on Fleming and Kretztechnik (annex A) gives a summarised history of the VAT liability of share issues and related input tax recovery position **N.B. Having considered the prevailing liability situation PE team consider that valid Fleming claims are most likely between 1 April 1987 - 31 March 1992 and 1 December 1994 - 30 April 1997.** Standard text (annex B) is available for use in rejection of claims for periods prior to 1 April 1987.

Withdrawn

Fleming: Kretztechnik – Authorised Unit Trusts

Withdrawn

Background and basis of claims

These claims by fund managers, or by advisers on behalf of fund managers, seek to disregard amounts treated as exempt turnover in their partial exemption calculations so that they can be regarded as fully taxable and deduct input tax previously restricted. The earliest date claimed from will be 1 April 1973 but the claims do not extend beyond 31 December 1990 when changes were introduced to the liability of fund management services.

All these claims concern the management of authorised unit trust schemes (AUTS) and may be broken down into a 'first claim' and alternative 'second claim' for a lesser amount. During the period of the claims, it was policy to treat the issue of units in an AUTS as an exempt supply by the manager as principal. Because the inclusion of the full value of the units was viewed as distortive for partial exemption, there was an industry agreement whereby the 'gross profit' on the issue of the units was used as the exempt value. This is largely derived from the income the manager makes on operating a bid/offer spread on the issue and redemption price of the units.

The argument is that the issue of the units is not a supply following the judgement in Kretztechnik and so the exempt value used in the partial exemption method should be disregarded. Alternatively (the 'second claim') if HMRC view the 're-issue' of redeemed units as a transfer of securities, then only the 'new issue' of units is disregarded, giving a reduced claim.

Policy line

We do not accept that it follows from Kretztechnik that the income retained by the manager from operating a bid/offer spread can be disregarded. Kretztechnik concerns the issue of shares in exchange for capital invested, but the manager's margin is not invested as capital in the AUTS. We do not need to address the 'second claims' as we agree that where redeemed units in AUTS are said to be 're-issued' they are in effect cancelled and new units issued rather than transferred.

Sectors affected

Banking and Insurance – either independent fund managers or investment management sectors of larger banking groups. Some may no longer manage AUTS but may have claims due to mergers/acquisitions over the years.

Action to take

- Claims made on this basis should be refused using this specimen draft letter (annex C), which has been produced following legal advice.
- A short email containing details of the Traders Name, VRN and amount refused should be sent to CT&VAT for policy evaluation purposes.

Kretztechnik Insurance v Investments

Background

Insurers are arguing that they have been incorrectly treating monies received from customers for investment as being exempt insurance income. They consider that the sale of investment products whereby the premiums are invested in units in collective funds, are investments in a fund for a defined ownership right and therefore do not represent consideration for supplies for VAT purposes.

There are investment and pension products that are sold to individuals that either have no insurance element for example Personal Investment Plans or will comprise an investment together with an element of insurance such as Endowments. Where a product contains an element of insurance and an element of investment, the investment element, they argue, should also be treated as a non-supply for VAT purposes.

They consider their view is supported by the ruling in Kretztechnik and businesses briefs 12/05 and 21/05.

Treatment of the investment income as a non-supply will lead to a reduction in the value of the exempt insurance supplies in the partial exemption method and a potential redistribution of the residual input tax to other sectors which may have a higher recovery rate.

HMRC do not agree with the Insurers' interpretation of Kretztechnik in relation to these investment products and this may become the subject of litigation.

Policy line

HMRC's response to these claims is being coordinated by Chris Birch and Keith Laney in AAG.

Sectors affected

This will primarily concern the Banking and Insurance Sectors.

Withdrawn

AB SKF C-29/08 - Input Tax Recovery on Disposal of Subsidiary

Withdrawn

Action to be taken

Claimants are to be advised:

Your claim to additional input tax will now be considered on its merits in the light of the evidence you can provide to support it

Overview of case

The above Swedish case is currently with the European Court of Justice (ECJ) to consider:

- whether the sale of shares in a subsidiary by a parent company is an economic transaction within the scope of the 6th Directive, and
- whether there is a right to deduct input VAT on costs directly attributable to the share disposal

AB SKF is of the view that the sale of a managed subsidiary should not be treated as a supply for VAT purposes, as similarly taken in the case of Kretztechnik. If accepted, it would then also follow that any input tax incurred in relation to the sale of these shares fall to be treated as a residual overhead of the business.

HMRC policy

Transfers of existing shares for a consideration continue to be exempt supplies provided that the supplies occur in the course of business activity. In such cases, the input tax that relates to the transfer will be exempt input tax and only recoverable to the extent that the shares have been sold to purchasers outside the European Union (EU). This was supported in the earlier ECJ case of BLP Group plc (1995) STC 424, C-4/94. There is no recovery of VAT in respect of transfers of existing shares which are not part of an economic activity.

Current developments (update 28 May 2010)

Our policy teams are now content for us to work on claims.

Danfoss/Astra Zeneca

Characteristics

Generally claims refer to business entertainment and claim that the expense is incurred by way of business or for business purposes or related to exports from the UK.

What it looks like/how to spot it

The European Court of Justice (ECJ) case in Danfoss/Astra Zeneca may be quoted

Key risk issues

Exports do not include intra European Union (EU) sales.

There may be no evidence that the relevant input tax was blocked in the first place and the input tax may have been fully recovered already.

Claims may fail to take into account the offsetting effect of any input tax relating to business entertainment where the input tax has incorrectly been reclaimed and the input tax block not applied.

Although there is a strong cross tax interaction between Corporation Tax and VAT, the business may not have carried out cross tax checks. Generally, CT disallowances for business entertainment tend to indicate higher levels of VAT should be blocked. (Business entertainment cannot be offset against Corporation Tax and the computations for CT usually show the amount that is disallowed which should include any disallowed VAT.)

Current policy line

Following the Danfoss/Astra Zeneca decision we have received a number of claims for input tax in respect of meals provided to staff and business contacts at meetings.

Taking each category in turn;

Staff meals

Please refer to the Staff Costs pen portrait which covers this area.

Meals provided to UK business contacts and overseas suppliers

The decision in Danfoss has no effect on the UK's block on business entertainment as it applies to UK business contacts and overseas suppliers. This tax remains blocked and no VAT should be repaid.

Any VAT that relates to UK business contacts and overseas suppliers should not be repaid.

Overseas business customers

Withdrawn

The decision in Danfoss may affect the UK's block on entertainment of overseas customers. We are consulting lawyers on the subject and hope to have our review finalised shortly.

Guidance on this element of the claims will be issued shortly.

Where we are with the precedent case

Not applicable

Future litigation:

Not known

Sector/industries affected

All

Withdrawn

Withdrawn

Catering (Compass)

Characteristics

All supplies of food and drink in the course of catering are standard-rated. Catering is defined (VAT Act 1994 Schedule 8 Group 1) as including supplies of food or drink for consumption on the premises on which they are supplied (as well as hot take-away food), but it is not limited to such supplies. Following the Court of Appeal decision in 2006 (Compass Contract Services Ltd) also colloquially known as 'the BBC case' HMRC changed its policy regarding the definition of 'premises' for sites with restricted public access. The impact of this was that some customers may have incorrectly accounted for output tax on supplies of cold take away food taken away from the supplier's premises for consumption for example a sandwich purchased in a canteen subsequently eaten at the employee's desk.

What it looks like/how to spot it

Most claims will probably be made on the basis of over declared output tax from canteen/cafeteria type outlets. However claims may also be seen on the basis of vending machine sales. There is also the possibility of claims being made for the sale of hot take away food pre 1984, when the VAT liability was changed to make all such sales standard rated.

Key risk issues

Agent/Principal: In the catering industry supplies can be made as agent/principal and in some circumstances a mixture of both. Only supplies made as principal carry the right to repayment. It is important to verify that the supplier status has remained constant throughout the period of the claim.

Earlier Repayments: The Court of Appeal decision was released in 2006. It is possible that payments have already been made for the later years of any claim.

Confirm the Correct Liability: Since 1984 hot food has been standard rated regardless of where it was consumed together with cold food consumed on premises.

Calculation of Claim: Claims may be based on a sample of current sales and extrapolated on a straight line basis back to 1973. The UK economy along with people's eating habits has changed significantly over this time & such extrapolation should be viewed with caution.

Current Policy line: At restricted access sites a retailer will now be considered to occupy only that unit from which the sales of food have been made rather than the larger overall premises. However, the 'premises' also includes any facilities provided to enable the purchasers to consume the food at the unit, such as areas of seating and tables within, and adjacent to, the retail unit, whether owned by the landlord or the retailer, but clearly for the use of the food retailer's customers. See Business Brief 12/06

Precedent case

HMRC has accepted the Court Of Appeal (CoA) decision.

Future litigation

Vending machine sales from within canteen areas (HMRC view this as a SR supply), numerous cases regarding the definition of hot takeaway food.

Sectors affected

Primarily catering but can be found in any sector if the employer makes supplies of food as principal to staff for example, canteens/cafeterias.

Withdrawn

Elida Gibbs (mostly auto)

Withdrawn

Characteristics

In 1996 the European Court of Justice (ECJ) released its decision in Elida Gibbs. The decision was that bonuses paid by manufacturers, to someone that wasn't their direct customer, were discounts. Although not specifically dealing with cars, the decision can be applied to certain bonuses paid by car manufacturers to car dealers and fleet buyers.

Previously the bonuses paid had been treated in various ways over the years some of which resulted in the recipient of the bonus over-declaring VAT.

Full background and basis for the claims for car dealers is on HMRC Internet site which sets out how each manufacturer paid its bonuses and whether a claim can be made. (Elida Gibbs guidance). Supplementary guidance from the UoE is also available (Annex D).

The HMRC Internet guidance is not applicable to fleet claims. These must be discussed with the theme expert or Unit of Expertise.

Key risk issues

Is there a claim – if there is no information in the motor dealer table on the Internet there is no claim unless the claimant has proof they declared output tax. HMRC do not expect to see individual invoices and/or credit notes (unless they are available) but do need to see sufficient evidence from the claimant to show he has a claim. It is for the individual claimant to demonstrate:

- They were paid a bonus direct from the manufacturer
- The bonus was paid in such a way that at the time it would have been seen as a supply of services
- The vehicles were purchased and not leased
- The input tax was required to be blocked on those vehicles
- How the business dealt with the VAT on the bonus in their records
- The amount of the bonus

Businesses need to answer each individual point on the balance of probabilities in order to establish that they have a claim.

Quantum – estimation of number of cars involved, value of cars and the bonus amounts paid where little or no records exist.

Unjust enrichment to be considered for claims from leasing or daily rental companies.

Current policy line

Claims are payable subject to evidence and checks on the quantum in light of the facts of the business and details on the Internet.

Precedent case

ECJ - Elida Gibbs

Future litigation

Not applicable

Sectors affected

Motor dealers - mainly automotive but other sectors also affected.

Fleet buyers exist in all sectors – the claims come from daily rental companies, leasing companies and businesses buying cars for their own use.

Withdrawn

Postal services (TNT)

VAT and postal services

Background

EU law provides a mandatory exemption from VAT for supplies of postal services made' by the public postal services'. In the UK, the application of this provision is limited to Royal Mail and covers all of Royal Mail's postal services. All other postal operators - both before and after full deregulation of the postal sector in the UK on 1 January 2006 – are required to charge VAT at the standard rate on their services.

Following a legal challenge to the scope of the exemption as applied in the UK, the European Court of Justice (ECJ) in the case of TNT Post UK Ltd has confirmed that Royal Mail, as the operator providing the public postal service, is the only postal body in the UK eligible to exempt postal services from VAT. However, it has also ruled that exemption applies to the public postal services (that is, Royal Mail) acting as such and does not apply to supplies made by Royal Mail for which the terms have been individually negotiated.

As a result, some postal services as supplied by Royal Mail – those which are individually negotiated or not subject to any price and regulatory control – which have been treated as exempt will become liable to VAT with effect from 31 January 2011 (see the Technical Note issued at Budget 2010). Legislation will be enacted as soon as possible in the new Parliament.

Basis of claims

Some of Royal Mail's customers are submitting claims for a refund of input tax which they claim is 'embedded' in charges made by Royal Mail for services which it has treated as exempt and which, the claimants argue, should always have been taxable.

Policy line

Claims have been held in abeyance by HMRC pending discussions about the impact of the decision. These discussions have now been concluded and, as announced in Budget Note 48, certain services previously treated as exempt from VAT will become liable to VAT at the standard rate with effect from 31 January 2011. As advised in Revenue & Customs Brief 19/10, HMRC will now begin considering these claims.

Action to take

Business Guidance Note 24/10 – VAT: Updated guidance for staff dealing with postal services input tax claims – provides guidance for staff dealing with claims.

The section on handling of claims sets out in detail the points officers will need to consider where a valid claim has been submitted on time.

Claimants should be advised along the lines of:

> 'I write with regards to your claim dated … concerning VAT and postal services supplied to you by Royal Mail (RM) which you have submitted

Withdrawn

following the European Court of Justice ruling in the case of TNT Post (UK) Ltd.

Following the recent announcement of the detailed policy changes resulting from this ruling (see the Technical Note issued on 24 March 2010), we are now in a position to consider your claim.

It is HMRC's understanding that RM's (including Parcelforce's) contract terms explicitly provide that charges made for supplies of postal services are exclusive of VAT and that any VAT, if due, is to be paid on top of the price quoted in the contract. In such cases, HMRC do not consider that customers can have valid claims that sums charged to them in the past by RM for supplies of postal services included VAT.

If you have reason to believe that your contractual arrangements with RM differ in some respect from the norm and can evidence that the price which you were charged by RM did include VAT, I would be grateful if you would provide such evidence within 21 days of the above date.

When we have received this evidence, we will give further consideration to your claim. Please note however that our request for you to provide such evidence should not be taken as our acceptance of the validity of your claim should the evidence support an argument that the price charged did include any VAT due. In such cases, your claim will remain subject to consideration of liability (i.e. whether the supply should in fact have been treated as taxable at the time when it was made). In addition, even where the liability issue is determined in a claimant's favour, we will require satisfactory evidence in support of any claim so as to satisfy the statutory requirements for input tax claims.

If you do not produce the evidence as requested within the timescale specified above, your claim will be rejected on the grounds that there was no charge to VAT included within the charges made to you by RM. At such time, you will be sent formal rejection letter, giving details of the appeals procedures.'

Withdrawn

Update 2 June 2010

Business Guidance Note 24/10 published on 31 March 2010 set out the line to take for valid claims. This took the form of a request to business to provide contractual evidence of tax inclusive charges made by Royal Mail.

In response to this request a number of materially identical responses have been received from businesses asserting that:

I. the European Court of Justice's (ECJ's) judgment in TNT does not support exemption for Royal Mail's supplies and that claimants can invoke directly effective rights to recovery of input VAT 'embedded' in the consideration paid to Royal Mail

II. HMRC and/or Royal Mail's error in treating the supplies as exempt ruled out the possibility of Royal Mail issuing VAT invoices; and

III. HMRC should exercise its discretion under regulation 29(2)(a) VAT regulations 1995 to accept alternative evidence in the form of records of expenditure on Royal Mail postal services

If you received a response in these terms we have provided the line to take (see annex E). If you have any queries regarding this update, please contact the theme expert.

Sectors affected

Non-sector/industry specific.

Withdrawn

GMAC HP and the treatment of re-possessed cars

Withdrawn

Key attributes of the theme

Historic treatment

Prior to the General Motor Acceptance Corporation (GMAC) appeal (generally referred to as GMAC 1, and culminating with the High Court decision (CH /2003/APP /0230) in February 2004) when goods were sold on HP contracts output tax was accounted for in full at the outset of the contract.

If the customer defaulted, the vehicle was usually repossessed and sold. Where supplies under hire purchase were made on or after 19 March 1997 a Bad Debt Relief (BDR) claim could be made by the supplier if any amounts remained outstanding.

If the customer voluntarily returned the vehicle at any time, there was no adjustment made in respect of the original supply of the goods.

In both cases, the onward sale of the repossessed/returned vehicle was de-supplied under SI/1992/3121 Art 4 The HP company did not reduce the output tax declared on the first supply, but offset the full sales proceeds, which were VAT free, against the original contracted amount.

GMAC 1 (High Court) - 2004 EWHC 192(Ch)) - established the following

- Where a car was returned voluntarily or was subject to default repossession, and the price actually required to be paid by the customer was reduced then there was a consequent decrease in consideration, which would give rise to an adjustment of the original output tax declared under VAT regulation 38 (SI/1995/2518).
- Irrespective of how the car came back into the possession of GMAC the return of the car constituted repossession for the purposes of Art. 4(1)(a) of the VAT (Cars) Order 1992 (SI/1992/3122). The sale of the repossessed car fell to be de-supplied, subject to all of the other conditions of the order. (In other words, same state etc).
- For unregistered customers, or for customers unable to recover the VAT charged as input tax, the level of documentation presented in the GMAC case was satisfactory for the purposes of Regulation 24 of VAT Regulations 1995 (SI/1995/2518). In the case of GMAC the business had to establish that they had suffered a reduction in the consideration, and normal accounting entries were accepted as evidence, (there is no requirement in law to issue either a tax invoice or a credit note to an unregistered customer).
- In reality all businesses had to submit two separate claims, one for hostile terminations and one for voluntary terminations.

GMAC 2 – [VTD19989] – (Fleming uncapped claims) - confirmed the following

- On 1 January 1978 Article 11C.1 of the 6th VAT Directive (Dir/77/388) was introduced. This is the first time that there was any right for adjustment to be made to the original transaction. At this point UK law remains silent on the issue.

- UK law first introduced BDR by the Finance Act of 1978. Relief was available on supplies made on or after 1 October 1978 and the customer had to be insolvent. This was subsequently amended in 1990 (six month rule introduced on supplies made on or after 1 April 1989) and 1997 (requirement for title to have passed removed for supplies made on or after 19 March 1997 and additional rules relating to input tax adjustment introduced on supplies made on or after 01 May 1997). There have been other amendments to the BDR regulations over the years, but these will not have any impact on GMAC claims. This is being currently (Nov 2009) being challenged at tribunal.
- VAT General Regulations 1980 and 1985 Regulation 58 allowed the correction of errors (following House of Lords decision in Fine Arts Developments (STC 246/1996)). However there was no recourse under this as there was no error.
- In 1984 the VAT leaflet 700/5/85 suggested that the price could be adjusted (although UK law is still silent). However, any resale of goods must be taxable.
- In 1989 SI/1989/2248 Regulation 7 was introduced. – Became Regulation 38 SI 1995/2518. This was the first time that the UK enacted ART 11C of the EC 6th VAT Directive. HMC&E did not agree that an early terminated HP agreement constituted 'a decrease in consideration for a supply' for the purposes of Regulation 38, hence the GMAC 1 appeal.
- If the reduction of output tax is made on the correct VAT return the adjustment falls under Regulation 38, but if the claim is not posted on the correct VAT return it is an adjustment under the VAT Act 1994 Section 80.

All GMAC 2 claims are being dealt with under S80 of the VAT Act 1994.

Applicable precedents, law

Applicable law and case-law is quoted above.

Key risks and issues

S80/Reg.38 claims can be paid for the period 01 January 1978 to the period ending on or before 04 December 1996.

[This text has been withheld because of exemptions in the FOI Act 2000]

In summary

- Claims for periods between 1 April 1973 and 31 December 1977 must be refused and the right of appeal given. Several mail order companies have lodged appeals – see separate Fleming theme report entitled 'Adjustments to value of supplies pre-1978'.
- Claims for Bad Debt Relief (BDR) in Fleming Periods should also be rejected. The BDR regulations during this period required title to have passed. However HMRC's refusal of BDR claims before 19 March 1997 if title has not passed is currently being challenged at Tribunal.
- If the claim is for tax periods ending after 4 December 1996 the normal assessment time limits apply. Please refer to the separate Fleming theme narrative on Scottish Equitable.
- Claims for refunds relating to the supply of goods to taxable persons where the Input Tax Blocking Order does not apply are to be refused.

Withdrawn

- S80/Reg.38 claims can be paid (subject to verification) for the period 1 January 1978 to the period ending on or before 4 December 1996.

Withdrawn

GMAC Adjustments to value of supplies pre 1978

Withdrawn

Characteristics

This subject concerns the capacity to adjust the value of a supply after the supply has been made. It only applies to supplies made before 1 January 1978.

The view of HMRC is that there was no legal authority to adjust the value of a supply after the supply was made until 1 January 1978, when the sixth Directive became law across the European Union (EU), and which had direct effect in the UK.

The corresponding authority in UK law was the Value Added Tax (Accounting and Records) Regulations which came into force on 1 January 1990. This is now included in UK law as Regulation 38 of the VAT Regulations 1995 (1995/2518).

Accordingly, before 1 January 1978 there was no legal authority applicable in the UK that required adjustments to be made to the value of a supply after the supply has taken place.

Applicable precedents, law

Article 11C.1 of the 6th Directive 77/388 – effective from 1 January 1978.

Reg 7 of the Value Added Tax (Accounting & Records) Regulations 1989 – effective from 1 January 1990.

General Motors Acceptance Corporation (UK) plc v HMRC [VTD19989].

Action to be taken

Claims from customers in the banking and automotive sectors for periods prior to 01 January 1978 that rely on adjusting the VAT where the underlying value of a supply was changed after the supply was made should be refused. This matter was litigated in the case of General Motors Acceptance Corporation (UK) plc v HMRC (VTD19989) and the decision supports HMRC's view as stated above and will not be appealed further. This means that Fleming claims seeking to recover overpaid output tax (or under-claimed input tax) as a result of retrospective adjustments being made to the value of a supply made before 1 Jan 1978 should be refused on the basis that there was no directly effective right in either EC or UK law that required such adjustments to be made.

Claims from customers in the retail sector who used a retail scheme to determine their gross takings for the tax periods before 1978 are still under review by HMRC. Several appeals have been lodged with the tribunal challenging the HMRC policy on this matter. As a result of various arguments received by HMRC the relevant policy team is currently seeking further legal advice as to the valuation of supplies within a retail scheme and a further update will be provided as appropriate in due course.

Linneweber

Characteristics/what it looks like

These claims stem from the European Court of Justice (ECJ) Linneweber case C453/02; Edith Linneweber won a judgement that German tax law exempting identical gaming machines within but not outwith licensed casinos breached the core EU VAT principle, the doctrine of fiscal neutrality. The doctrine states that similar supplies must be taxed similarly. Betting and gaming is exempt in EU law, as per Art.135(1)(i) of the 2006 Directive. Member states can depart from the exemption but must not breach fiscal neutrality in doing so. The UK enacts the exemption within Group 4 of Schedule 9 but has, since 1975, excluded 'gaming machines' from this. Until December 2005 the definition of gaming machines included the fact that 'the element of chance is provided by means of the machine'. From 5 December 2005 the VAT Act was amended to bring Fixed Odds Betting Terminals (FOBTs) within the scope of taxation. Linneweber claims are based on a perceived breach of neutrality if 'similar' gaming products delivered by apparatus outside the former 'gaming machine' definition were exempt whilst others were taxable.

There are also Linneweber claims lodged for both Mainstage bingo and 'Mechanised Cash Bingo (MCB)'- the latter is bingo played on boards within the intervals between main bingo sessions. Both types of claims are based on the fact that UK bingo becomes Vatable once certain prize and stake thresholds are breached. Businesses claim that as the supplies are identical, fiscal neutrality is breached and therefore the liability must be exempt.

Key risks and issues

Prior to 2005 certain types of machine/apparatus have been found by the VAT Tribunal to have existed, which qualified for exemption. There is debate as to when and indeed if 'similar' machines received different tax treatment at different times. If repaying VAT, consider full input tax implications - including residual tax and Capital Goods Scheme (CGS). Additional excise duty liability on value of repaid output tax on bingo products.

Current policy line

Gaming Machines: to be rejected pending the outcome of Policy consideration of recent Rank Tribunal. Further guidance will be given when available.

Mainstage Bingo and MCB: HMRC will repay claims following the recent High Court decision (subject to verification and in accordance with the guidance on Fleming and Scottish Equitable claims) however an appeal has been lodged with the Court of Appeal. Please see Revenue & Customs Brief 75/09.

Precedent cases

See R & C v Rank Group [2009] EWHC 1244 (Ch) (08 June 2009): Judge gives thorough recap on statutory and case law on both machines and MCB claims.

Future litigation

Withdrawn

Rank MCB judgement at Court of Appeal; Mainstage bingo now appealed to the Tribunal; Second VAT Tribunal hearing on Rank's Gaming Machines claim to be heard in October 2009. Thus far all decisions won by tax payer. Potential for all claims to escalate to ECJ.

Sectors/Industries affected:

Betting and Gaming, Pubs and Hotels, wider leisure industry for example, theme parks etc.

Withdrawn

Lennartz

Withdrawn

Characteristics

'Lennartz' accounting (named after an early European Court of Justice (ECJ) case in 1994) applies to new assets with mixed business use and non-business use (including private use). The taxable person must intend to use the assets for some business use that gives a right to deduct input tax in order to adopt the Lennartz mechanism. Taxpayers that wish to make a claim can choose whether to apportion the VAT up-front between business and non-business use, or to treat all the VAT incurred as 'business' input VAT and account for output VAT on the ongoing non-business use over the economic lifetime of the asset. This effectively gives the taxpayer a cost-free deferral of the irrecoverable VAT on the non-business use of the asset, over its economic life.

What it looks like/how to spot it

Typical claims will involve an upfront deduction on all of the VAT incurred on the purchase or construction of a business asset where that asset will be used for both business and non-business or private purposes. Such mixed use occurs mainly in the education and charity sectors (also possibly some sole trader use for VAT on house extensions provided the extension creates a new asset etc). Claims thus far have focussed on the purchase or construction of property but Lennartz is available for all business assets. The term Lennartz is commonly used to describe this mechanism and should appear in documentation.

Key risk issues

Contrived early exits from paying the Lennartz output tax charges can occur. Various routes are possible. Where the deemed supplies in para 8 of Schedule 4 won't bite the Lennartz business may simply deregister shortly after getting VAT recovery. Another possibility is the collapsing of leases.

Current policy line

Last year, the ECJ in the VNLTO case (C-515/07) considered whether or not Lennartz accounting can be used by a taxpayer who engages in activities that are not within the scope of VAT. As a result of this judgement, it is now clear that the EU VAT legislation does not give, and has never given, a right to use Lennartz accounting in circumstances such as those of the VNLTO case.

HMRC has set out its position on Lennartz accounting in Revenue and Customs Brief 02/10 which outlines the specific limited circumstances in which Lennartz accounting will be available. Other claims should be rejected.

A draft rejection letter is attached at annex F. Officers are reminded that the text should be checked in detail to ensure that the letter meets the specific case.

Future litigation

N/A

Sectors affected/industries affected

Mainly in the education (FE colleges and non-business research facilities such as HEIs) and charity sectors or potentially artificially in any partially exempt business.

Withdrawn

Property - 'Mirror Group' case

Withdrawn

Characteristics

The case involved the payment of inducements from the landlord to the tenant to accept a lease of land (known as a 'reverse premium'). There had been a series of cases before the Tribunal in the 1980s on this subject, the most notable one being Neville Russell (VATTR 194 (VTD 2484). where it was held that such payments were consideration for standard rated supplies by the tenant to the landlord. By contrast, it was held that very often a rent free period offered by a landlord to a tenant is not consideration for any supply by the tenant to the landlord – it simply being an adjustment to the value of the lease.

In the later case of Mirror Group, the appellant argued that reverse premiums were consideration for supplies which were exempt under item 1 Group 1, Schedule 9 to the VAT Act 1994. The case was referred to the ECJ which said that there is no supply if the recipient of the inducement does nothing more for it than become a tenant and pay the rent (the relevant part is paragraph 26 of the judgment). However, as was found in the Mirror Group case, if the tenant does do something more than this, then there is likely to be a standard rated supply by the tenant to the landlord.

What it looks like/how to spot a theme

One off payments between tenant and landlord, Reverse premiums tend to be a feature of large developments where landlords wish to attract prestigious tenants.

Although the Mirror Group case concerned reverse premiums, the principle is the same for other inducements paid to a customer to enter into a contract. However, we think this may be less common outside the property industry.

Key risk issues

Not all inducement payments will be outside the scope, they will be taxable if the tenant does something more for the landlord than to simply accept the lease. However, our experience of cases is that most reverse premiums are simply inducements to take up a lease.

Earlier Business Briefs (28/97 and 17/98) gave the customers the option of not accounting for tax, so evidence is needed that output tax was originally charged. Furthermore, given the disputes in the 1980s which led to Tribunal cases such as Neville Russell, and the arguments in the Mirror case that reverse premiums were exempt from VAT, it cannot be assumed that VAT was charged or accounted for in all cases.

Given the large value of many reverse premiums, if VAT has been accounted for it will most probably have been charged and explicitly referred to on a VAT invoice; and in many cases deducted as input tax by the landlord. The issue of unjust enrichment therefore needs to be considered.

There are input tax considerations.

Departmental policy has long been that most rent free periods are not consideration for taxable supplies by tenants to landlords, so we would not expect as a matter of course to see Fleming claims relating to these.

Current policy line

The majority of reverse premiums will be outside the scope as they relate to merely entering into the lease.

Where we are with the precedent case

The case has been completed

Future litigation

None expected

Sectors/industries affected

Potentially all sectors.

Withdrawn

JP Morgan Fleming Claverhouse (pension fund claims)

Withdrawn

Characteristics of the scheme

The scheme seeks to apply the principles of the European Court of Justice (ECJ) Claverhouse Decision C 363/05 to investment management services supplied in respect of defined benefit occupational pension schemes. HMRC does not accept that such claims have any validity.

What it looks like

Claims may be made by investment managers supplying the services or by the trustees of a pension scheme receiving the services from outside the UK. The latter would concern VAT previously accounted for under reverse charge rules on investment management services received from outside the UK. Claims for input tax on similar services made by employers, which do not dispute the VAT liability, would fall into the separate 70:30 Admin Cost and Pension Fund issue.

Key risk issues

- Claims for overstated output tax can only be made by the investment managers who charged the VAT or, as above, pension scheme trustees in respect of reverse charged services. The trustees cannot seek to recover from HMRC output tax which they believe was wrongly applied by their suppliers.
- Lack of direct evidence of tax involved, including historic Partial Exemption calculations.
- Lack of detail of the services provided and in respect of what type of fund/scheme

Current policy line

The Claverhouse judgment concerned the scope of the fund management exemption in items 9 and 10, Group 5 of Sch 9 to the VAT Act 1994. Following the judgment, changes were made to Group 5 from 1 October 2008 to include additional collective investment undertakings, such as the investment trust companies at issue in the case. Defined benefit occupational pension schemes are not collective investment undertakings and it is HMRC's view that there is nothing in the Claverhouse judgment to suggest that investment management services provided to such schemes should be exempt. On that basis claims in respect of such services, which usually quote the Claverhouse judgment, should be rejected. Customers can then appeal that decision.

Where we are with the precedent case

The front running case is 'Wheels and Others' (Trib ref LON/08/0720) which concerns Wheels Common Investment Fund, 3 Ford pension schemes and the National Association of Pension Funds (NAPF). This is at a procedural stage at the Tribunal and no dates have been set for a substantive hearing (unlikely to be heard before second half of 2010).

Future litigation

Similar claims are also possible in respect of other types of fund not covered by the exemption in UK law. These should also be rejected but claims may cover early periods under the Fleming case. It should be noted that any claim for exemption of these services before 1 January 1990 is baseless as the UK was not required to exempt any fund management services before that date.

Sectors involved

Not sector specific.

Withdrawn

Italian Republic cases – update 29 July 2010

Suspension of verification work

HMRC is reviewing its policy position regarding “Italian claims” to take into account the effect of the ECJ decision in Nordania Finans A/S v Skatterministeriet Case C-98/07. The Review is being led by CT&VAT and will consider the impact on claims that have already been paid as well as claims where decisions have not yet been made. Until the review is completed, verification officers should make no further payments in respect of these claims. No action is to be taken in respect of claims that have already been paid at this stage. We aim to keep any delay to a minimum and expect the review to last until mid - late August 2010

Withdrawn

EMI Samples

Summary

This precedent case is currently under litigation for hearing before the European Court of Justice (ECJ).

Withdrawn

Scottish Equitable

Background

Claims under this theme are for periods later than those covered by the House of Lords decision in Fleming/Condé Nast and may quote the lead case in Scottish Equitable.

In an Order handed down on 2 July 2009, the Court of Session overturned the 2006 decision of the VAT and Duties Tribunal in Scottish Equitable that the introduction of the three-year time limit without a transitional period in 1996 meant that it had never been lawfully enacted.

On July 17 2009 HMRC published Scottish Equitable ruling - Revenue & Customs Brief 41/09 (web) reporting the judgement and its implications for claims received.

Action to take

All output tax claims for accounting periods ending on or after 4 December 1996 are potentially covered by the time limits described in VAT Refunds Manual VR2800 (web).

The same approach should be taken for input tax claims in relation to accounting periods ending on or after 1 May 1997 (see time limits guidance in VR6700 and VR6800 (web)).

Claims should be refused where these time limits apply and the claimant should be invited to appeal to the Tribunal.

Where appellants make application for their appeal to be stood over behind another appeal, that application should be objected to unless the appellant can show that that other case concerns the consequences of not providing transitional arrangements when a new time limit is introduced or an existing one is shortened. Applications for stand over behind Alstom Power Hydro or BT Pension Fund Trustees are not appropriate. Whilst the former concerns the imposition of time limits, it is not concerned with whether time limits may be relied upon where they are introduced without transitional arrangements. The latter case has little or no argument on limitation.

Withdrawn

Claims based on Wellington Private Hospital [CA (1997) STC 445]

Withdrawn

Background

Wellington Private Hospital Ltd supplied drugs to private in-patients in the course of their treatment. In 1997 they successfully challenged the Commissioners' view that the drugs were part of the exempt supply of treatment under VATA 94 Schedule 9 Grp 7 Item 4. The Court of Appeal ruled the supply of drugs to be a separate zero rated supply under VATA 94 Schedule 8 Grp 12 Item 1.

An appeal to the House of Lords was refused and as a result, claims were invited at the time from bodies who made similar supplies.

The law was changed with effect from 1 January 1998 to ensure such supplies were exempt from that date.

Subsequent case law including *Card Protection Plan* (Case C-349/96), *Levob* (Case C−41/04) and *Dr Beynon and Partners* (HL 2004 STC 55) strongly suggests that the *Wellington* decision was wrongly decided. In *Dr Beynon*, the Court held that the administering of drugs by an NHS doctor was part of a single exempt supply of services.

In *Dr Beynon* various cases predating *Card Protection Plan* were quoted. Lord Hoffman stated at paragraph 19 of his judgement: '*In the course of argument your Lordships were also referred, as were the courts below, to a number of cases, both in this country and in the Court of Justice, which were decided before the Card Protection case. Submissions were made as to whether the principles upon which those cases were decided had application to this case. Their Lordships think that there is no advantage in referring to such earlier cases and their citation in future should be discouraged. The Card Protection case was a restatement of principle and it should not be necessary to go back any further*'

The cumulative effect of post *Wellington* case law means that the *Wellington Private Hospital* ruling can no longer be relied upon to determine nature of supplies to in-patients before 1 January 1998.

Current policy

Claims which rely on Wellington to support separate zero rated supplies of drugs or prostheses to in-patients (and the consequent effects thereof) should be challenged.

What to do

Anyone finding such a case should contact the Theme Expert who is part of the AAG Abusive one-sided claims project which is providing assistance in challenging such claims.

Where are we with precedent cases

A lead case is currently (10/09) being worked upon and HMRC is seeking legal advice.

Sectors affected

The predominant numbers of cases have been made by NHS trusts and lie within the I&PB customer group. However private hospitals are known to have made claims and could lie within any of the customer groups.

Withdrawn

Pensions 70/30 split

Withdrawn

Characteristics of the theme

The theme seeks to recover input tax in respect of admin/management costs and in some cases investment costs (see below) incurred by employers on funded pension schemes. Management/admin costs are allowable. Investment costs are not recoverable.

What it looks like

Five variations of the theme or combinations of one or more of these variations appear in claims:

1. Company seeking to recover input tax on fees for management services before 1 April 1982.
2. Company seeking to recover input tax on fees for management services after 1 April 1982.
3. Company is seeking to recover 30 per cent VAT on fees for third party services before April 1996.
4. Company is seeking to recover 30 per cent VAT on fees for third party services after April 1996.
5. Company is seeking to recover all of the VAT incurred, including on 'investment' services.

Key risk issues/Current policy line:

1. and 2. above: It is accepted that this is the employer's input tax that they are entitled to recover. The risk is that they may attempt to include investment costs or overstate the claim.

Burden of proof (as advised by the Fleming team) is on the claimant.

3. above: This is a policy decision and therefore can only be applied from the date the change was announced, 1 April 1996. These claims should be refused on the grounds that the business could recover input tax on fees for management services based on the previous published guidance, VAT Notice 700/17/83.

4. above: If the company has, in error, failed to recover input tax on fees for management services, they are entitled to recover their input tax. The policy has always been that the 30/70 split should only apply where a third party, for example fund manager, property manager or professional trustee is appointed to manage the scheme, their services include both management and investment services and they only issue an inclusive invoice for both services. Also see risk at **1. above**.

5. above: Recovery of VAT incurred on investment services is inconsistent with our policy. Where Redrow and similar cases are quoted in relation to these claims these issues should be referred to Supply of Services and Public Bodies team who have responsibility for this area. More detailed information is available at annex G.

Where we are with the precedent case?

Not applicable.

Future litigation

None

Sectors involved

Not sector specific.

Withdrawn

Construction (White Goods)

Withdrawn

Background

A number of VAT registered construction companies have used the opportunity afforded by 'Fleming' to submit claims for input tax that they had been prevented from recovering previously by the provisions of the Value Added Tax (Input Tax) Order 1992 (the 'blocking order') and its predecessors.

The 'Fleming' claims in question are in respect of VAT incurred on finished and pre-fabricated furniture; materials for the construction of fitted furniture other than kitchen furniture; domestic electrical and gas appliances other than those designed to provide space heating or water heating or both; and carpets or carpeting material. These items were incorporated into new dwellings that were subsequently sold at the zero rate of VAT.

HMRC's view is that there is **no legal basis for these claims**.

The sole or main argument put forward by these companies is that the application of the 'blocking order' to the above 'building materials' is *ultra vires*. Their reasoning is that the 'blocking order' that was in place at 1 January 1979 was extended in 1984 and 1987 to include these items. That extension is *ultra vires* because Article 176 of the Principal VAT Directive (formerly Article 17(6) of the 6th VAT Directive), which provides for the blocking of input tax deduction, states that 'Member States may retain all the exclusions provided for under their national laws at 1 January 1979'.

Some of the companies concerned had also put forward a secondary argument. They maintain that the 'builders' block' only affects 'goods other than building materials' that have been incorporated into a building. 'Goods other than building materials' that have been installed as fittings in a building have not been incorporated into a building. Such goods are not affected by the 'blocking order' and the companies are entitled to take credit for input tax in respect of them.

The companies appear to be basing their argument on the fact that the term 'incorporates' is not qualified for the purposes of the 'blocking order'. The companies contend that there can be no read across to Note 23 of Group 5 of Schedule 8 to the VAT Act which does qualify the term. Note 23 to the Group states that for the purposes of Note 22 to the Group, 'incorporation of goods in a building includes their installation as fittings'. However, given the context of Note 22, the goods referred to can only be 'building materials' and not 'goods other than building materials'.

Action to be taken

Claims should be rejected and standard responses sent as follows:

To the '*ultra vires*' argument:

'We do not consider that the post-1979 extensions to the scope of Article 6 of the VAT (Input Tax) Order 1992 (SI 1992/3222) and its predecessors (the 'builders' block') are *ultra vires*. Article 176 of the Principal VAT Directive does not provide the vires for the 'builders' block'. In our view, it is Article 110 of the Directive that provides the vires for the builder's block and the post 1979 extensions.

This view is supported by the VAT Tribunals. In the case of McCarthy & Stone PLC (VTD 7752) heard in 1992, the Tribunal considered whether the ‘builders’ block’, together with the subsequent extension made to it during the 1980s was lawful. The Tribunal found that the whole block was lawful since it considered the ‘builders’ block’ to be part of the zero rate transitional provisions (which provides for new dwellings to be zero-rated) in Article 110 of the Principal VAT Directive (formerly Article 28(2)(a) of the 6th Directive). This decision was not appealed nor has it subsequently been challenged.'

To the ‘not incorporated’ argument:

'We do not consider that Article 6 of the VAT (Input Tax) Order 1992 (SI 1992/3222) and its predecessors (the ‘builder’s block) applies only to goods that are incorporated into a building and not to certain goods that are merely installed as fittings. In our view, the ‘builder’s block’ must apply to these goods when they are installed as fittings because the ‘builder’s block’ in relation to the zero rate under Item 1 of Group 5 of Schedule 8 to the VAT Act 1994 should replicate the extent of the zero rate achieved by Item 4 of Group 5. Zero-rating under Item 4 does not extend to these goods when they are installed as fittings.'

Withdrawn

Update 22 Jan 2010

In correspondence, some claimants contest our view that Article 110 of the Principal VAT Directive provides the vires for the 'builder’s block' and the post-1979 extensions and have quoted a number of European Court of Justice cases in support.

They also maintain that the 'builder's block' does not apply to certain goods when they are installed as fittings in other words, that Notes 22 and 23 to Group 5 of Schedule 8 to the VAT Act 1994 cannot be read across to the ‘builder’s block’.

The claimants have also introduced a variant to the 'no read across' argument above by saying that even if there were a 'read across', fittings were not covered by those Notes until Note 23 was enacted (1 March 1995).

The following can be used in any response.

“Thank you for your letter of ****, in which you asked for a review of the decision to reject your claim for input tax previously blocked by virtue of Article 6 of the VAT (Input Tax) 1992 (SI 1992/3222), otherwise known as the 'builder’s block' and its predecessors.

In your letter, you have adopted two analytical approaches ('the standstill analysis' and 'the statutory interpretation analysis') and a variant of the latter so as to refute our decision.

Standstill analysis

Here you contend that Article 110 of the Principal VAT Directive cannot provide the vires for the 'builder's block' by arguing that measures adopted under Article 110 must affect the output tax liability and not the recovery of input tax.

We disagree. It is well known that Directives are binding as to the result to be achieved by national legislation but are not prescriptive as to the means that the

outcome is to be achieved. UK 'zero-rating' is a case in point. Although supplies subject to it are cast as taxable supplies, to which a zero rate of VAT is applied, the concept appears in EC VAT law as 'exempt' supplies that, unlike other exempt supplies, carry a right to deduct input tax incurred on supplies that are attributable to making such supplies.

In *McCarthy & Stone PLC (VTD 7752)* the Tribunal held that the 'builder's block', the scope of which had been increased after 1 January 1979, was effective in its wider form, despite ostensibly appearing to be an unlawful extension of permitted input tax blocks. The Tribunal accepted that, although cast as an input tax block, the provision was intended to maintain the integrity of a UK zero-rating provision.

In light of subsequent judgements by the ECJ, *(Norbury Developments Ltd v CCE (C-196/97) and Talacre Beach Caravans (C-251/05))*, we believe that a higher Court would follow the approach taken by the above Tribunal.

Whilst we agree that the ECJ cases referred to in your letter do set out restrictions on blocking input tax, we would point out that those cases relate to different factual circumstances from the case here. Those cases relate to a failure to allow recovery of input tax in relation to taxable transactions where output tax was payable. In the case here, we are considering a retained zero rate and the scope of the zero rate can be reduced, as has, in effect, happened here (albeit by a roundabout route), but, once lost, cannot then be reinstated.

As a general principle in EU law, the right to deduct relates to taxable transactions and no input tax is recoverable where output tax is not paid, except in a very limited number of circumstances set out or permitted by the Directive (cf Articles 168, 173 etc). One of these circumstances is a zero rate (which is permitted and continues at the discretion of Member States).

Statutory interpretation analysis

Here you maintain that Note 23 to Group 5 of Schedule 8 to the VAT Act 1994 only applies for the purposes of Note 22 and, by extension, to supplies of building materials eligible for the zero rate under Item 4 of Group 5. These Notes have no impact on the recovery of input tax.

We disagree. We believe that the intention behind the 'builder's block' is clear and that the extent of the zero-rating achieved by Item 4 of Group 5 should be replicated by the 'builder's block' in relation to the zero rating by Item 1 of Group 5. We would also argue that if the concept of 'building materials' used in the Order includes the expansion of the concept by Note 23 to Group 5 , the use of 'incorporates' in Article 6 of the Order must, by necessary implication, also include goods installed as fittings.

Variant

Here you maintain that, even if there is a 'read across' and the above Notes do have an impact on input tax recovery, goods installed as fittings would not be affected until Note 23 was enacted (1 March 1995).

Notes 23 and 22 were enacted together on 1 March 1995. Prior to the enactment of VATA 1994, the legislation provided for the zero-rating of:

Withdrawn

“The supply, in connection with a supply of services within Item 2, of materials or of builder’s hardware, sanitary ware or other articles of a kind ordinarily installed by builders as fixtures.
(Finance Act 1972, Schedule 4, Group 8)

“Ordinarily installed by builders as fixtures” was the phrase of choice in the legislation subsequent to the VAT Act 1994. The ‘builder’s block’ during the same period used the same phraseology.

Without further investigation, it is not possible to say that fittings were excluded from the scope of the zero rate and the ‘builder’s block’. For all practical purposes, I am not aware of any distinction being made between fixtures and fittings: 'fixtures' was a catch-all term for goods incorporated into the building or its site. Fittings would be such goods but were more easily removable.

If we are wrong in this and fittings were so excluded, I would agree that prior to 1 March 1995 input tax recovery in respect of such items is feasible. However I would also say that if such items are not seen as part of the building for the purposes of the 'builder’s block', then they are not part of the building for the purposes of the zero rate. As a result, output tax would be accountable on the disposal of such items on the sale or long lease of the dwellings concerned.”

In case of difficulty or if other arguments are advanced which are not included above you should consult the Construction UoE and/or the Property VAT policy team within CT & VAT.

Withdrawn

Construction (Soft landscaping - "Rialto")

Withdrawn

Background

A number of VAT registered property developers have used the opportunity afforded by 'Fleming' to submit claims for input tax that they had incurred on certain landscaping costs prior to 1 May 1997.

Prior to May 2000, HMRC maintained that the only soft landscaping that could be zero-rated as a supply in the course of construction of a building designed as a dwelling was the laying of turf within a house plot. All other supplies of landscaping i.e. the planting of shrubs and trees, would attract VAT at the standard rate. Property developers were prevented from recovering the VAT on the trees and shrubs component of these supplies by the provisions of the Value Added Tax (Input Tax) Order 1992 (the 'blocking order') and its predecessors.

In May 2000, following the VAT Tribunal's decision in the case of Rialto Homes plc, HMRC accepted that, as well as turfing, other types of planting could be zero-rated as supplies made in the course of construction and issued a Business Brief (07/2000) to this effect.

The Business Brief invited claims under s80 VAT Act 1994 from those businesses which had wrongly charged VAT on their supplies of soft landscaping to developers. Although VAT that is wrongly charged cannot be treated as input tax, the Business brief also allowed developers who had been charged VAT incorrectly and had been 'blocked' from recovering that VAT as input tax to recover the VAT wrongly charged as input tax. These claims could not be treated as claims under Section 25 of the VAT Act 1994 and Regulation 29 of the VAT Regulations 1995 but were allowed by concession. It is now our view that this concession should not have been offered to developers. However, we recognise that the Business Brief has created legitimate expectations that must be protected.

Action to be taken

Open claims may be repaid subject to i) checks on quantum and the evidence to support the claim ii) checks to ensure that a claim is not one of a pair of "double claims".

Double claims - As a result of the terms of the Business Brief it is possible that we will have had claims from those at either end of a transaction. That is to say, it is possible that, for the same series of transactions, we shall have had a claim both from the person who wrongly charged the VAT and the person to whom it was wrongly charged. With immediate effect, when dealing with Rialto claims, you should do your best to ensure that there is no competing claim from the other end of the transaction. Double claims should be dealt with as follows:

- where both claimants have already claimed and already been paid, there is little you can now do and no recovery action should be taken except for reasons unassociated with the mistake in Business Brief 07/00 (that is, inviting claims from those who have no legal claim against us)

- where a claim has been made by a developer and paid and we are now dealing with a claim by a landscaper, we cannot resist the landscaper’s claim and it should be paid subject, as ever, to verification

- where a claim has been made by a landscaper and paid and we are now dealing with a claim from a developer, you should reject the developer’s claim on the grounds that our liability in relation to the transactions in question has been discharged

- where we have ‘open’ claims from both the landscaper and the developer, you should process the claim from the landscaper and reject the claim from the developer on the grounds that we are only liable once on any given transaction

- clearly, where there has been no claim from the landscaper, a claim from the developer can be processed in accordance with this guidance

Closed claims

The theme narrative had previously advised that claims were to be refused and recovery assessments issued if amounts had been repaid. This theme narrative was introduced on 31 March 2010 and was suspended on 8 June 2010. We believe that all recovery assessments issued are likely to have been appealed. Where such recovery assessments were issued, these should now be withdrawn (assuming that you are satisfied that the claim was correctly quantified and backed up by sufficient evidence.)

Withdrawn

Cultural Exemption

For claims in the Public Bodies Sector only guidance can also be sought from the Public Bodies Unit of Expertise.

It is envisaged that most large business Fleming claims under the cultural exemption will be in the Local Authorities sector but this guidance also covers other cases which may arise.

Characteristics

Cultural exemption was introduced in the UK on 1 June 1996, giving effect to the mandatory exemption set out in Article 132(1) (n) of the Principal VAT Directive 2006/112/EC (formerly Article 13(A) (1) (n) of the 6th VAT Directive) for:

(n) the supply of certain cultural services, and the supply of goods closely linked thereto, by bodies governed by public law or by other cultural bodies recognised by the Member State concerned; *

* note the wording in the 6th Directive (the legislation extant for Fleming claims) differs slightly.

Its introduction followed amendments to the 1978 European Council agreements which had previously allowed the UK to tax all cultural services. Although the UK had believed that these amendments did not require any change to existing arrangements, we accepted, following legal challenge, that some supplies of cultural services supplied by public authorities or other eligible cultural bodies were required to be exempt. As the agreements were amended with effect from 1 January 1990, it was possible for cultural bodies to also backdate their exemption to this date. Fleming claims will therefore be considered for the period 1 January 1990 to 1 May 1996.

In a 2008 Technical Announcement policy provided advice that, for a claim for the 1990/1996 period to be valid, we required the cultural body in question to fall within the definition of 'eligible body' set out in Note (2) to Group 13, Schedule 9, VATA 1994. However, a challenge to this approach was made on behalf of a number of cultural bodies whereby it was argued that the conditions that were introduced into UK legislation with effect from 1 June 1996 should not be applied retrospectively. Following on from this challenge we have amended our policy in this area with the result that some claims that previously would have been rejected can now be paid.

Article 13(A)(2)(a) of the 6th Directive gave member states the right to impose certain discretionary conditions when they applied the exemption for cultural services to cultural bodies other than those governed by public law. The UK applied some of these conditions in Note (2) to Group 13 with effect from 1 June 1996. We now accept, however, that until the UK exercised its discretion to narrow the scope of the exemption by subjecting it to these discretionary conditions, no such conditions applied. We cannot therefore require cultural bodies submitting Fleming claims for the period between January 1990 and May 1996 to show that they would have satisfied the 'eligible body' requirements. If the only reason that a body is disqualified from exemption under UK law is because it fails to fulfil the discretionary conditions, it falls on the face of it within the scope of the exemption on the basis of the UK's existing approach to the definition of 'cultural services' and 'cultural bodies'. The

Withdrawn

basic test that now needs to be applied is to ask the question whether or not the body in question's supplies would fall within the scope of the exemption if it fulfilled the discretionary conditions. If the answer is yes, then the body can rely on the direct effect of the exemption in the period before the UK put the discretionary conditions in place. Fleming claims that have previously been rejected on the grounds that a body did not satisfy the Note (2) 'eligible body' conditions, or have been pending awaiting clarification of our policy, can now be repaid subject to the normal checks required for all Fleming claims.

It is important to note that this revision of our policy only relates to the status of the cultural body submitting a claim. In all other respects cultural exemption claims from cultural bodies must fall within the scope of the exemption as legislated for in Group 13. In particular the cultural services supplied must fall within the scope of the specific cultural services which the UK has granted exemption to in items 2 (a) and (b) of Group 13.

It should also be noted that a few claims have been submitted seeking direct effect of the 6th Directive for the period from 1978 to 1989. Our current position is that the 1978 European legislation contained a derogation which allowed us to tax cultural services and that there was no subsequent requirement for a cultural exemption to be introduced until 1 January 1990, albeit we did not introduce it until 1996. The advisor's argument is that the UK took no positive action to implement the derogation and therefore direct effect of the exemption should apply from 1978.

Withdrawn

What it looks like/how it spot it

Theatre Admissions and other cultural services recognised as falling within the exemption under the items in Schedule 9, Group 13, VATA 1994

Where a body's cultural supplies were exempt from 1 June 1996, it is likely, assuming the same circumstances prevailed, that there is a valid claim for direct effect of the exemption contained in Article 13(A)(1)(n) for the period 1 January 1990 to 31 May 1996.

However in respect of public bodies, Note (3) to Group 13 denies exemption where it 'would be likely to create **distortions of competition** such as to place a commercial enterprise carried on by a taxable person at a disadvantage'. We will not argue that this condition applied at a time when we had not specifically implemented it (pre June 2006). Note (3) to Group 13 of Schedule 9 may therefore be ignored when verifying claims.

We must however consider whether claims fail under the mandatory conditions of Article 134 (b) of PVD [formerly Art 13(A) (2) (b) of Sixth Directive]. This denies exemption 'where the basic purpose of the supply is to obtain additional income for the body in question through transactions which are in direct competition with those of commercial enterprises subject to VAT.' This test applies only to eligible bodies – it does not have to be applied to public bodies. Whilst it is likely that bodies will deny that their supplies fall within the description of Art 134 (b) it is clearly envisaged in the directive that cultural services will meet this description. It is recognised that the test in Art 134(b) may be difficult to apply but officers should require claimants to demonstrate that they meet this condition, if this situation applies, and should discuss with the VAT policy team in cases of doubt.

Other Claims

Some claims have been submitted in respect of activities that have not previously been regarded as falling within the scope of the exemption. Included among these are:

Farms

Claims that petting farms are zoos for the purposes of cultural exemption.

Gardens

Claims that gardens open to the public for a charge qualify as cultural exemption.

Wrestling (Professional Wrestling)

Claims arguing that Professional Wrestling is not sport and, as it is non-competitive with a pre-determined outcome, is in fact a 'live performance' qualifying for the cultural exemption.

Withdrawn

Key risk issues

Theatres run by local authorities

- Ensure supplies that are not covered by the exemption are not included in the income figures for example bar takings, programme sales (which were always zero-rated), confectionary, merchandise (T-shirts etc) and touring fees charged to theatres.
- Examine whether or not there is profit sharing and the consequent impact on the accounting arrangements.
- Unjust enrichment - The main factor to consider is whether or not the Council when determining prices for admission included the VAT element in their deliberations. Minutes of meetings, annual review of pricing reports may give a clue to this.

Additional considerations for non local authority cases

- Ensure that claims for over paid output tax are always net of exempt input tax. Exempt input tax should be calculated using the standard method. Please note that this was use based until 1 April 1992.
- Ensure that claims are continuous in other words it is not permissible to claim exemption by direct effect only for certain VAT periods while treating others (normally those where significant capital costs were being incurred) as taxable. Where claims do not start at 1 January 1990 and trading was going on in pre-claim periods then consider whether Capital Goods Scheme (CGS) items were created in the periods not subject to claim as adjustments may be due in claim periods.

Current policy line

Theatres

As outlined above

Gardens

Notice 701/47 paragraph 2.3. outlines the department's clear policy on this subject and states that 'for the avoidance of doubt, a botanical garden does not qualify for exemption'.

Farms and Professional Wrestling

Due consideration has been given to the issue of both petting farms and professional wrestling and it has been decided that neither activity is eligible for the exemption.

Where we are with the precedent case

See guidance and Notice 701/47 including Updates 1 and 2, (particularly important), which includes the effect of previous litigation on current policy.

Future litigation

One tribunal appeal has been received in relation to the 1978-1989 period. It is likely that this case will be stood behind other cases relating to a different group in the exemption schedule.

Sectors affected/industries affected

The vast majority of claims are expected to be in the public Bodies Sector.

Withdrawn

Opticians (D’Ambrumenil)

Characteristics of the theme

ECJ decision in the case of Dr Peter d'Ambrumenil resulted in a change of UK law with effect from 1 May 2007 (R&C Brief 06/07). Certain services supplied by health professionals are standard rated rather than exempt. SR applies where services are not intended primarily to protect, maintain or restore the health of an individual, for example eye tests conducted to provide fitness certificates for employees, pilots, drivers etc. Therefore input tax on the relevant medical equipment is residual rather than entirely exempt.

What it looks like/how to spot a theme

Fleming claimant quotes the d'Ambrumenil case and claims that the ECJ decision has 'direct effect', such as, the ruling has effect prior to 1 May 2007. Claimant re-categorises input tax on medical equipment, formerly treated as entirely exempt input tax, as residual input tax.

Withdrawn

Key risk issues

1. It is essential to establish what PE method was in use at all relevant times during the period of the claim. The standard method for PE years commencing on or after 01 April 1987 and ending on or after 31 March 1992 required the deductible proportion of residual input tax to be based on use. Under a use-based calculation, where the supplies are made on a profitable basis, the output tax on d'Ambrumenil supplies should exceed the related input tax. Therefore it is unlikely that there could be a valid claim for 1987-1992 where the optician used the standard method.
2. The standard method override provisions did not apply during these early years, therefore input tax recovery under standard method outside 1987-1992 is likely to be higher than would be the case under an apportionment calculation based on use. You may wish to check how they are treating this activity currently.
3. If a special method was in use, check whether it contained any provision for recalculation in event of liability errors.
4. Claimant may fail to offset claim by the output tax on the relevant supplies - although this is likely to be small in relation to the claimed input tax, it must be accounted for. It is not relevant whether this was deductible by the customer.
5. Inadequate evidence, for example input tax amounts poorly estimated, PE calculation based on poorly reconstructed or estimated figures.
6. Scope of activities - did the claimant supply these types of services at the time of the claim? If a chain of shops, is there evidence that all branches make such supplies? Classification as residual input tax only if there is actual dual use - potential dual use is not sufficient.

Current policy line

The d'Ambrumenil ECJ decision has direct effect. Need to check that the recalculations are in accordance with the PE method in force at the time.

Where we are with the precedent case

Not applicable.

Future litigation

Not applicable.

Sectors/industries affected

Opticians; potential for other health professionals.

Withdrawn

Utilities – Fuel and Power - Qualifying use by Universities

Withdrawn

These claims are specific to the Utilities Sector and have been made by the suppliers of gas and electricity. They relate to supplies charged at the standard rate of VAT to Universities.

Characteristics

Universities are entitled to receive supplies of fuel and power for a 'qualifying use' at the reduced rate of VAT. Qualifying use is 'domestic use' (for example, student residential accommodation) and 'charity non-business' use.

Many universities had not previously recognised charity non-business use where publicly funded research was carried out in the 1990's.
Therefore the universities had not certified their full entitlement to qualifying use and a reduced rate of VAT. They now wish to claim back the VAT that they were overcharged on fuel and power.

These claims have all been prepared by KPMG on behalf of the Universities. However, as it is the Utility Companies who have over declared the output tax, it is they who have had to submit the Fleming claims.

The Utility companies have stated that any amounts repaid to them as a result of these claims will be passed on to the universities under the reimbursement scheme.

Key risk issues

Although Utilities companies have correctly charged VAT based on the qualifying certificates they received at the time, the fuel and power guidance (VFUP2530) states that a change to a qualifying certificate can be backdated subject to the normal rules, Fleming claims may therefore be accepted subject to checks on evidence and quantum

If the claims are accepted then there are issues around evidence of original supplies and liability applied, and evidence of qualifying use. It is also important to check that the claim has been submitted by the correct Utility Company as many of the companies no longer exist, have been bought by a new company or subsumed into other VAT groups.

It is also possible that the VAT charged may have been claimed as input tax by the universities and there may be implications for their partial exemption methods. Under the reimbursement scheme, the Utility Companies must be able to show that the customer has borne the burden of the tax.

It will be necessary to liaise with the Public Bodies Group in Local Compliance who deal with the Universities to verify the claims.

Claims concerning management of investment trust companies (ITCs) and venture capital trusts (VCTs)

Withdrawn

Summary

Following extended litigation on the 28 June 2007 the European Court of Justice (ECJ) ruled that fund management services provided to investment trust companies (ITCs) were exempt from VAT. HMRC had previously treated the services as standard rated. We accepted the ECJ ruling and claims were invited under the terms of Revenue and Customs Briefs (RCB) 58/07, 65/07 and 35/08.

RCB 35/08 involved closed-ended funds which includes VCTs.

Whilst a number of Fleming period claims have already been received and processed prior to the Fleming deadline, a number may have been submitted where earlier claims were not made. These new claims should be assessed carefully ensuring there are no duplicate claims.

Key risk issues

The following risks should be taken into consideration:

1. Period: Claims applicable from 1 January 1990 when the exemption was first introduced.
2. Liability - the ruling only applies to specific fund management services. Claims for funds where the management is not exempt under items 9 and 10 of Group 5 Schedule 9 VAT Act 1994 should be rejected.
3. Verify claims to ensure they only relate to ITC's and VCT's under the terms of RCB 58/07, 65/07 and 35/08. RCB 35/08 concerns closed-ended funds which fall within the scope of the VAT exemption under the revised item 10 Group 5 Schedule 9 VAT Act 1994. The law was amended from 1 October 2008 but it was accepted that it was law as it should have been since 1990.
4. Claims should be net, in other words overpaid VAT less input tax to be restricted.
5. Partial Exemption (P/E) – a P/E calculation is required to account for input tax claimed for taxable supplies which are now exempt.
6. Assistance from Partial Exemption Liaison Officer (PELO) may be required.
7. Unjust Enrichment - should be considered, please refer to V1 – 33 for guidance.
8. If Unjust Enrichment applies, consider reimbursement procedures.
9. Check registrations of ITCs and VCTs as some may not be registered for VAT.
10. VAT Registrations and Companies: Ensure claims and payments are made by and to the correct entity and ensure where necessary authorisations obtained at appropriate levels.
11. For periods where full business records are not held, officers should ensure that appropriate and acceptable effort is made to ensure accuracy of the submitted claims. Such claims are generally driven by the investment trust companies and consequently there should be, between the parties a good deal of supporting evidence to these claims.
12. Simple interest to be paid.

Road Fund Licences

Withdrawn

Characteristics

Until 28 February 1993 HMCE's Public Notices on the margin schemes for second-hand cars (VAT notice 711), second-hand motorcycles (713) and second-hand caravans and motor caravans required that VAT was paid on the value of surrendered Road Fund Licences (RFL).

VAT was payable only where the surrender value of the RFL formed part of the profit on a deal under the special schemes. However some businesses adopted the practice of accounting for VAT on all surrendered licences (including commercial vehicles) even where the vehicle was sold at a loss.

From 1 March 1993 HMCE accepted that there was no need to account for VAT on surrendered licences (Business brief 13/1994 dated 16th June 1994 refers) and in VAT notice 700/59/94 invited claims back to 1 April 1973 in respect of output tax incorrectly paid on RFL surrenders.

Key risk issues

The change in policy was well publicised and it was clear to the trade how to submit a claim. It is therefore likely that affected dealers would have made a claim in 1994 and have no claim now.

The papers showing that a claim was made are often not available in Electronic Folder (EF) but an historical ledger print will show if a repayment was made at that time and that Statutory Interest (SI) was due which would be a clear indication that a repayment had been made.

If there is no record of SI being paid, you should also bear in mind that it is possible that claims may have been made and refunded through the dealer's VAT return under the voluntary disclosure rules, particularly if the original claim was less than £2,000 in value.

Current policy line

Claims should be refused unless the dealer can show that they had overpaid tax before 1994 and why they made no claim at the time.

Precedent case

No precedent case

Future litigation

None

Sectors affected

Automotive mainly but there are some motor dealers in other sectors.

Part Exchange (non monetary and open market)

Withdrawn

Characteristics

The claims seek to exploit the wording of the Finance Act 1972 and the VAT Act 1983 between 1 April 1973 and 31 July 1992 with regards to the non monetary consideration made when a customer trades in a used car in exchange for another and whether the value of the traded in car is 'subjective' (Community Law) or 'open market value' (UK Law)

The claims argue that the valuation is different where the transactions occurred prior to 1 August 1992 when the wording of the legislation in the 1983 VAT Act was changed. Originally, the Act stated that non-monetary consideration should be defined as the 'Open Market Value' (OMV). This was later amended following the European Court of Justice (ECJ) ruling in the 'Naturally Yours' case which established that the value of non-monetary consideration should be the subjective value. The claims argue that the OMV should be the value quoted in 'Glass's Guide' or a similar trade guide for the second-hand car trade and that by basing valuation on the higher, subjective, value of the non monetary consideration received towards the price of the new car for supplies made before 1 August 1992 the trader has overstated its output tax liability.

What it looks like/how it spot it

The majority, if not all the cases, have been received from an accountancy firm and refer to the difference between the EC Law reference to subjective value and the UK Law's reference to open market value.

Key risk issues

Lack of evidence dating from 1 April 1973 to 31 July 1992, therefore claims are based on recent sales figures pro-rata back using the Retail Prices Index.

Current policy line

It is our firm view that the use of the subjective value was not contrary to the UK legislation either prior to 1 August 1992 or since and there is no case for re-valuing the supplies or re-calculating the output tax.

Action to take

Claims should be refused using the response at Annex H

Where we are with the precedent case

N/A

Future litigation

Not known

Sectors affected/industries affected

Withdrawn

Retail related - Bespoke Retail Schemes (BRS) and Daily Gross Takings (DGT) adjustments

Withdrawn

Characteristics

Can include any adjustment to reduce DGT and/or adjustment to the calculations agreed in the BRS.

What it looks like/how to spot it

Claims will usually be for an adjustment reducing either the DGT or reducing the standard rated percentage within a published or bespoke retail scheme. A sampling exercise may have been undertaken and extrapolated going back over a period of time. There was a major overhaul of the retail schemes in 97 and officers need to establish whether the scheme methodology currently in use is the same now as it was prior to that date.

Key risk issues

- The claim may have no validity in that the commercial conditions in retail have changed considerably over the period and what happens now may not have happened in 1973. Our TSA is working to produce evidence to negate some of these claims including those covering:
  - own funded coupons
  - failed manufacturers coupon
  - head office refunds
  - product file errors
  - mix of products on sale
  - sales of gift vouchers B2B
  - car parking charges refunded

Please **do not proceed** with claims concerning these areas until you get a further briefing from the theme experts. **Please consult the theme expert** for guidance on whether to proceed with claims concerning other areas.

- The sample may not be representative of the whole period covered as historically the business may have been quite different. The sample may be too small; confined to one area or region with its own unique problems and not representative of the whole of the period covered by the claim.
- The adjustments may already be covered in the BRS that was in force at the time, and therefore the adjustment will be subject to the conditions of the scheme.
- DGT can not be adjusted for debit and credit charge backs: these must be dealt with outside the retail scheme through the bad debt relief provisions. Bad debt relief is not available on supplies made before 1 October 1978 and since its introduction the rules have varied.
- Petrol filling stations have their own specific problems such as drive offs.

Current policy line

Until further notice claims relating to pre-1978 periods should **not** be repaid because the same considerations apply as in GMAC in that we argue that there was no right to adjust past periods before the inception of the Sixth VAT Directive.

Where we are with the precedent case

Not known

Future litigation

Not known

Sectors/Industries affected

General Retail, Agriculture and Food, Leisure and Media, Oil and Gas and any business that accepts cash and credit/debit cards.

Withdrawn

Fraudulent card/cheque transactions

Characteristics of the theme

The claims are citing the tribunal decision in the Selfridges appeal (BVC 2013) concerning their arrangements with a company called Certegy Limited trading as Transax.

Transax guaranteed (subject to conditions) payment to Selfridges of an amount equal to the full value of all ‘qualifying’ cheques in the event that those cheques were dishonoured. It charged Selfridges a monthly fee plus a percentage of the value of ‘qualifying’ cheques for this service. The tribunal ruled that the consequent payments to Selfridges by Transax were not consideration for the supplies made to the customer and were not liable to VAT. The customers’ obligation to pay Selfridges for the supplies they had received was not discharged by Transax. Businesses are now/again seeking to apply this ruling on dishonoured cheques to fraudulent card transactions.

What it looks like

The wording used in the claims is along the lines of:

'As a result of the Selfridges decision we have reviewed the VAT treatment of monies received by X plc in similar circumstances. We believe that we have over declared VAT on monies received from our bank where credit and debit cards are used fraudulently. Where a card is being used fraudulently, there is in our view no supply to the customer for a consideration and that the payments from our bank are not being made on behalf of the fraudulent customer. We understand that this view is consistent with HMRC’s position that goods obtained by fraudulent means are not subject to VAT'

Key risk issues

1. Inappropriate extension of the Selfridges tribunal decision to encompass fraudulent debit\credit card transactions.
2. With regard to dishonoured cheque payments claims should not go back before August 1987 as Transax didn’t have a presence in the UK before that date. Company House information indicates that Transax was known as Cheque Point Guarantee Limited from 28 August 1987 until 16 July 2003 when it became Transax Financial Services Limited.
3. Claim not considered in conjunction with the relevant clauses in any bespoke retail scheme agreement.

Current policy line

HMRC does not accept that the Selfidges/Transax Tribunal decision can be extended to cover 'chargebacks' by credit/debit card companies.

Claims should be rejected where it is claimed that the Selfridges decision is authority to reduce DGT where a 'chargeback' is effected against the claimant by a credit/debit card company. Where there is any doubt, claims should not be repaid but referred to

Withdrawn

the Retail UoE and/or Supply of Goods Branch for further advice. Further advice on both types of claim is also available from the Theme Expert.

Fraudulent use of cards

HMRC does not accept that the Selfidges/Transax Tribunal decision can be extended to cover fraudulent use of credit cards.

The contracts between the retailer and the card companies make it clear that the card companies will pay for the retailer's supplies provided that the agreed checks were performed by the retailers on the cards. We therefore consider that the payment received from the bank is consideration for the supplies made by the retailer and the fraud is perpetrated against the bank and not the retailer. Any attempt to extend the Transax decision to fraudulent debit and credit card transactions should be rejected. However if the contracts indicate that the business may have a case, further advice from the Retail UoE and/or Policy must be sought.

Future litigation

Probable

Sectors

Retail Sector plus any businesses with retail outlets.

Withdrawn

Vouchers

Withdrawn

This note covers some risk areas in Fleming claims concerning face value vouchers or money-off coupons.

Characteristics

Fleming claims cover output tax over-declared in periods ending before 4 December 1996. This is before the current legislation on face value vouchers, Sch 10A VATA 94 which was introduced in April 2003.

Relevant legislation for periods covered by these Fleming claims was para 5 Sch 6 VATA 94 and para 6 Sch 4 VATA 83.

What it looks like/how to spot it

Many claims covered by this profile may relate to:

Face value vouchers

These may be issued and redeemed by the same person (for example Marks & Spencer Gift Vouchers). Where these have been sold at less than face value then redeemed at full value, the correct consideration is the actual amount they were initially sold for. For example, if a £1 gift voucher is sold for 95p then redeemed against goods, or services on sale for £1 we are due VAT on the 95p. This was determined by litigation in the **Argos** case, in 1996.

Should face value vouchers be given away – as a gesture of goodwill - enabling a product/service to be purchased at a lower price, this lower price is the consideration on which VAT should be calculated.

Where these are given away free to a customer who redeems them without making a further payment, VAT may be due on redemption subject to the business gift rules applicable at the time.

Money off coupons

These are used to offer the public a reduction in the price of a future purchase. They are commonly referred to as discount vouchers, and in a number of ways their treatment varies from that of face value vouchers. However, once again, where these are given, enabling a product/service to be purchased at a lower price, often as a gesture of goodwill. This lower price is the consideration on which VAT should be calculated.

Manufacturers promotions

Manufacturers may fund a reduction in the price the customer pays by means of a (third party) money-off coupon presented to the retailer and then reimbursed by the manufacturer.

In these cases the manufacturers are entitled to reduce their output tax in relation to their reimbursements, provided that they charged and accounted for VAT on their original supplies.

Retailers should initially account for VAT on the (reduced) payment received from the customer, in other words, monies actually received, but must include the value of any reimbursements from manufacturers in their DGT as third party consideration, on receipt of these payments. Retailers should not adjust their input tax to reflect the change in the manufacturer's deemed consideration.

The retailer may, by agreement, initially account for VAT on the full selling price, in anticipation of being refunded by the third party.

Where reimbursement is not forthcoming for such money-off coupons (for example for out of date coupons accepted in error) it is often also agreed that an adjustment may be made to reduce the retailer's DGT by the value of the non-refunded money-off coupons. Claims may be made by retailers relating to a failure to adjust for these non refunded money-off coupons, provided they had already accounted for VAT on the full selling price.

Retailer's own (money off) coupons – are a legitimate reduction to DGT

Key risk issues

- Sample used in extrapolation may not be representative of population, may be too small; confined to one area or region with its own unique problems (for example high turnover of staff in the south east); not representative of the whole of the period covered by the claim.
- Money-off Coupons and face value vouchers have a high non-redemption rate and claims must reflect this.
- Duplication of claims – may already/also be claimed as part of DGT adjustments.
- Retrospective discounts claims should not be confused with nor claimed as Elida Gibbs claims.
- As they did not start until after 1997 it is not anticipated that Fleming claims will be valid re LMUK/Nectar voucher based schemes

Current policy line

VAT Notice 700/7/94 Business promotion schemes issued 1 October 1994 and V1-12 paras 4.11.4 and 5.16 covered periods relevant to Fleming claims. If it is felt necessary to confirm the content of such guidance when dealing with claims please contact the Retail UofE who hold copies. Current policy line may be irrelevant since the legislation has changed.

Where we are with the precedent case

Not applicable

Future litigation

Not applicable

Withdrawn

Credit and Debit Card charge backs

Withdrawn

Characteristics

Claims incorrectly treat credit and debit card charge backs as an adjustment to daily gross takings or a retail scheme error. This should actually be treated as a bad debt relief item.

What it looks like/how to spot it

If a card has been used fraudulently, or there is a dispute regarding the supply/charge made, the bank will either guarantee the payment or make a charge back to the supplier in order to re-coup the money. The treatment the bank applies may well depend upon whether the retailer correctly applied specified security checks.

Charge backs may be included as an item in a claim for adjustments to Daily Gross Takings (DGT), bad debt relief or retail scheme errors, or as an item in its own right.

Key risk issues

DGT cannot be adjusted for debit and credit card charge backs, although an adjustment can be made under the bad debt provisions. There is a distinction between payment not being received (dishonoured cheque) and payment being received and subsequently withdrawn (charge backs) and this lies behind the ineligibility of charge backs as an adjustment to DGT.

Bad debt relief is not available on supplies made before 1 October 1978 and since its introduction the rules have varied.

Current policy line

- The policy on charge backs has only recently been reviewed and it is understood that there may be businesses including those with bespoke retail scheme agreements who will have been adjusting DGT for charge backs.
- We consider that the payment received from the bank is consideration for the supplies they made and that any fraud is perpetrated against the bank not the retailer.
- BUT if the contracts with the finance providers indicate that the business may have a case further advice from the UofE or policy MUST be sought.
- If the Bespoke Retail Scheme contains a clause which expressly permits the DGT to be adjusted for charge backs, we could only amend that clause with prospective effect.

Where we are with the precedent case

Not known

Future litigation

Not known

Sectors/industries affected

General Retail, Ag & Food, Leisure & Media and any business that accepts cr/dr cards.

Withdrawn

First National Bank of Chicago

Characteristics

Input tax not claimed in respect of foreign exchange (FX) activities.

How to spot it

- Prior to First National Bank of Chicago (FNBC), HMRC's policy was that the simple exchange of one currency for another by a FX dealer (or anyone else for that matter) did not involve any supply of services for VAT purposes. The value of the currency provided should therefore have been excluded from all Partial Exemption (PE) calculations, although any commissions or fees would have been included. HMRC considered that input tax incurred in speculative foreign exchange transactions was not incurred by way of any business activity and was non-recoverable. Any input tax incurred on foreign exchange transactions made to support other activities of the bank (for example, conversion of foreign currency loan repayments into sterling) was either treated as a general overhead of the bank, or it was reallocated to the other trading areas which it supported. An accurate apportionment between these activities was often not possible and could not be checked by HMRC, so attempts were made to identify input tax incurred in respect of FX dealing and rough percentage estimates were often used by the banks (and others) to split this input tax between 'speculative' and 'supportive'. Generally the relative percentages and the exact methodology of reallocation and recovery were recorded in PE methods.
- Since FNBC, FX dealing has been seen as a supply for VAT purposes, and consequently there has been no non-business restriction of input tax. Following a later Tribunal case (Willis), HMRC's view of FNBC is that to be a supply there has to be a spread position adopted over a period of time when buying and selling currency.
- Money brokers (and bureaux de change) have always been seen to have made supplies for VAT purposes if a separately identifiable commission/fee was charged. The FNBC decision meant that money brokers (who are intermediaries) charging the buyer and seller a commission could obtain additional recovery of input tax under the Specified Supplies Order when the underlying FX transaction became a supply for VAT purposes.
- More details are in the Finance manual.

Risks

- The business that makes a claim no longer exists (ceased trading, liquidated)
- The business that makes the claim was not dealing FX throughout the whole period of the claim.
- The business was allowed some recovery in respect of supportive FX activities prior to FNBC. It should be noted that some banks claimed that 90-95 per cent of their FX dealing was supportive whereas other banks considered it all to have been speculative.
- Input tax has already been claimed because input tax in respect of FX activity was not treated as irrecoverable for the period of the claim. Although it is possible that the input tax restriction was not applied robustly in the earlier periods back to 1973, it was always HMRC's position that there was not a supply for VAT purposes prior to FNBC. On a balance of probabilities basis it

Withdrawn

should be assumed (subject to evidence to the contrary, of course) that some restriction was made in respect of speculative foreign exchange dealing, where this was undertaken.

- A previous claim has already been submitted and paid. Following the FNBC decision, claims subject to capping were submitted by most banks. By a special concession the cap ran three years back from October 1995 which meant most banks submitted, and were paid, claims back to 1 October 1992; some businesses were paid back further if they had protective claims lodged prior to FNBC.

Policy line

- FX dealing with UK counter-parties is exempt from VAT and with EU counter-parties is outside the scope of VAT (with no input tax recovery) and no input tax can be reclaimed.
- FX dealing with non-EU counter-parties is outside the scope of VAT with input tax recovery if there is a supply for VAT purposes.
- If there is no supply for VAT purposes, normal input tax recovery rules will apply; input tax is residual subject to the partial exemption method used. In such circumstances there is no right of recovery in respect of FX transactions with non-EU counter-parties.
- Most FX dealing businesses have sectorised partial exemption special methods and residual input tax allocated to the FX sector is subject to a transaction count apportionment method that is number of FX transactions with non-EU counter-parties/total number of FX transactions.
- HMRC has insisted that residual FX input tax is apportioned using a transaction count and has not allowed principal FX traders to use apportionment calculations based on values. (Intermediaries such as money brokers who charge a commission may use a values calculation). The reason is that FNBC said that the value of the FX services provided was the net result of the supplier's transactions over a given period of time, but it is generally impossible to allocate this net result between recoverable and non-recoverable FX transactions.
- Outside of the financial sector, treasury dealings may have been treated as 'incidental' or insignificant and ignored for partial exemption purposes.

Precedent case

First National Bank of Chicago (C-172/96) decided 1998
Willis Pension Fund Trustees Limited (VTD 19183) decided 2005

Future litigation

None, settled litigation

Sectors

- Primarily Banking & Insurance but also any businesses with Treasury operations dealing FX.
- More details are in the Finance manual.

Withdrawn

Notice of Direction re selling via unregistered traders (Mail Order)

Withdrawn

Key attributes of the theme

This subject concerns the legality of a Notice of Direction issued to mail order companies requiring them to account for output tax on the open market value of supplies made to their customers as opposed to the value of the consideration actually received. Where the companies supply goods to persons who are not taxable persons (often referred to as 'agents') to be sold by retail, whether by them or others, the NoD requires the companies to account for VAT on the open market value of the supplies (typically the selling price as per the catalogue) as opposed to the price received by the mail order company (typically the selling price less the 'agent's' discount).

The legal authority for HMRC to issue a Notice of Direction has been challenged. This point turns on the construction of European Union (EU) law, and whether the derogation applied by the UK is legitimate.

Applicable precedents, law

VATA 1994, Sch 6, para 2

Key risks and issues

If the claim succeeds, then the additional output tax paid by companies upon whom a NoD was issued, may be output tax overpaid under s80 of VATA and the companies may be entitled to a refund of VAT overpaid.

Policy

HMRC is of the opinion that the relevant derogation has been correctly applied and that the legal authority exists to issue Notices of Direction under Schedule 6, paragraph 2 of the VAT Act 1994.

Therefore, claims solely based on the issue of such legal authority should be rejected and the claimant made aware of his right to appeal.

Construction Rebates

Characteristics

The main rebates seen in the construction industry are volume rebates where the supplier allows a contingent discount to a customer based on the level of purchases made over a set period.

What it looks like/how to spot it

Contingency discounts in this industry normally take the form of lump sum payments between the supplier and their customer.

Key risks and issues

Over the years a number of different practices have developed. The correct procedure is for the supplier to issue a credit note to the customer to formally reduce the value of the supply and the VAT charged in light of the contingent discount they are allowing. If customers are saying that they issue invoices to their suppliers we should point out that this is incorrect. What is happening is that the supplier is reducing the value (and associated VAT) of their supply: their customer is not making a supply (which would generate output tax due from the customer and input tax for the original supplier!) The credit note is the correct method of reducing the value of the original supply.

Where both parties are fully taxable, a credit note must still be issued but it is not essential for the VAT charge on the value of the original supply to be reduced where volume discounts have been earned and both parties agree to this treatment. The rationale for this is that tax neutrality is maintained and taking no action minimises the administrative burden on both businesses. However where the customer has limited recovery, for example, by reason of partial exemption or non-business use, the supplier must issue a credit note showing the adjustment to VAT on the original supply. Where the supplier does reduce their output tax there is an obvious danger that they reduce their output tax but their customer does not reduce their input tax – especially if the supplier reduces their output tax via their VAT account and does not actually issue a credit note to their customer. In respect of Fleming claims HMRC could then be out of time to take any action in respect of the customer. In many cases there will be little or no paperwork issued.

Whilst credit notes are the norm it is also possible for the customer to issue a debit note providing both parties agree to let that happen.

Current guidance

The guidance relating to the VAT treatment of contingency discounts and credit/debit notes is set out in paragraph 5.15.4 of V1-12, Section 13 of V1-24A and paragraph 18.2.1 of Public Notice 700.

Where we are with the precedent cases

There is no precedent case

Withdrawn

Future litigation

None expected

Sectors/industries affected

Mainly the construction sector but the same rules apply to any sector.

Withdrawn

Direct Tax – considerations

Withdrawn

Characteristics

Section 80 VAT repayments claimed by VAT group are treated as non-taxable income for Corporation Tax purposes.

What it looks/how to spot it

Tax comps/accounts show one of three versions:

1. VAT Repayment and interest are both untaxed.
2. Interest is taxable but not the VAT repayment
3. VAT is taxable but not the interest.

Key risk issues

Principal amount repaid is normally chargeable under Schedule D, Interest repaid is chargeable under Loan Relationship rules, Accounting principles determine timing of receipt, in a Group context need to consider which companies are chargeable.

Current policy line

Revenue and Customs Brief 14/09 outlines the policy line. Repayments of principal and statutory interest are normally taxable.

Where we are with the precedent case.

No current precedent case.

Future litigation

Existing cases are being moved towards litigation. Need to consider raising alternative assessments. Assessing deadlines now affect all earlier repayments resulting from Elida Gibbs, M&S and Italian republic claims.

Sectors/industries affected

Earlier claims were mainly in the Automotive sector. Later claims affect all sectors and Industries are affected.

Calculation of Claims – methodology

Characteristics

The use of some form of mathematical modelling method; either to fill in data gaps/extend periods covered. The use of the mathematical analysis of data in selective period(s) and then using ratios/relationships found, as a base for other unanalysed periods.

What it looks like/how to spot it

The use of some form of mathematical or statistical analysis of a data sample held and using the results on all periods. The use of mathematical or statistical analysis results on limited data and extrapolating it to a larger period where data is not held.

Key risk issues

Use of non representative periods. Inappropriate methods or modelling. Use of resulting ratio/trends on un-similar data/periods. Inconsistency of interpretation. An unfair method. No/inappropriate business rationale for the method.

Current policy line

We recognise that, in some cases, the passage of time may mean that there is no longer the documentation that we would normally expect in support of a claim. In such circumstances, we will accept estimated claims provided that the assumptions, on which the estimates have been based, are reasonable.

Where we are with the precedent case

Not applicable

Future litigation

None

Sectors/industries affected

Potentially all sectors and industries may be involved. Will be most relevant where estimates/extrapolations/regression analysis has been used when data is not available for the full period of any claim. Where statistic/statistical analysis/trend analysis is used either because the work involved is too great to carry it out on each period or as a method of filling in data gaps.

A list of audit specialists is available, which provides information on who to contact for advice on claim methodology.

Withdrawn

Staff costs

Characteristics of the theme

Claims refer to staff costs made up of some or all of the following: staff entertainment, subsistence, business mileage, staff expenses, secondment expenses (for example, legal fees, removal costs)

What it looks like/ how to spot it

Expense types listed above are mentioned in the claim.

Key risk issues

Generally

Businesses may be claiming input tax now in relation to the above expenses that was not deducted at the time, either due to an oversight on the part of the business or due to their own policy at that time not to claim input tax.

Staff entertainment

Input tax relating to the entertainment of staff is deductible – Ernst and Young (VTD 15100);

Input tax relating to the entertainment of staff and guests should be apportioned – KPMG (VTD 14962) unless guests make a payment and the payment is adequate. The payment does not have to equal the full expense required to host that individual – Ernst & Young [1997] VATDR 183 (VTD 15100), but should represent more than just a token amount.

History: HMRC (HMC&E as was) allowed full recovery of input tax from 1973 to 31 July 1993. Following issue of VAT Leaflet 700/55/93 input tax became restricted to 50 per cent on average from 1 January 1994 to 1997. In 1997, following E&Y and KPMG Tribunal losses, we accepted that the 50 per cent restriction was unsustainable by VAT law and reverted to full recovery inviting back claims to previously restricted amounts subject to the three year cap provisions.

Business Brief 25/97 was issued to advise businesses of the revised policy.

When input tax is not incurred solely for the purpose of entertaining staff but includes an element of business entertainment for example, employees' acting as hosts and not guests at a business function or entertaining of Directors, this is not deductible.

Non staff expenditure is not incidental to the staff costs (Thorn EMI 1995).

Evidence

There will probably be no historic documentation to support the claim, as there is no legal requirement to keep these records for more than six years.

Withdrawn

As a result of this and the fact that the overall claim will be made up of numerous records with relatively small amounts, the claim amount may have been deduced by taking a sample of current or recent period information and applying the results obtained to historic Annual Account figures or RPI adjusted figures.

However, where there was no restriction on claims for staff costs prior to the introduction of the three year cap the burden of proof lies with the claimant to prove the input tax was incurred and not deducted. The Central Policy, Tax, Admin and Advice team, with responsibility for capping law, advised that if prior to 1 May 1997 a claim for input tax could have been made, the question as to why it wasn't claimed at the time must be raised and evidence provided by the claimant in support of their claim.

Check Electronic Folder correspondence, visit reports, assessments or voluntary disclosures as these documents may mention historic action regarding Staff expenses or Entertainment. A recent Tribunal case applied information obtained from these documents as follows: HMRC argued that if an assessment/corrective action was instigated by HMRC, in 1978 and 1986, to correct the position the business had taken regarding non deductible employee expenses; this therefore inferred that employee expenses had been deducted in the past. It was then down to the business to prove otherwise.

Withdrawn

Please Note: Separate claims challenging our current policy on Business Entertainment have also been received. See the Danfoss/Astra Zeneca theme for further details

Current policy line

We will only consider allowing claims where there is sufficient evidence to satisfy the officer that the tax being claimed is due and has not already been paid.

Where we are with the precedent case

N/A

Future litigation

Related issue – Danfoss/Astra Zeneca ECJ

Sectors/industries affected

All taxable persons

Travel agents

Characteristics

Claims are Elida Gibbs claims for VAT on travel agent funded discounts not advised to tour operators some of whom may be associated

What it looks like/how to spot the theme

European Court of Justice (ECJ) decisions in respect of CCE v Elida Gibbs (C-317/94), Commission v Germany (C-427/98) and an unnamed German Tribunal case may be quoted.

In 2005 following a reference to the ECJ, the CCE v First Choice PLC case (C-149/01) was decided in favour of CCE. The decision determined that tour operators could not reduce the price of holidays in respect of discounts offered by travel agents to the public. The current theme is a follow on from that litigation.

Key risk issues

- Claims must take account of VAT paid by tour operator within Tour Operators Margin Scheme
- Any claims pre 1.4.1988 are invalid as package tours were treated as 54% VAT zero rated, 45% outside the scope of VAT, 1% VAT exempt.
- Any claims in respect of non EU holidays are invalid as these are zero rated for VAT.
- Any claim relating to packages on which no VAT was paid (E.g. certain flight only packages) are invalid.
- Travel agents required to produce evidence of VAT paid by the tour operator

Current policy line

Any similar claims should be referred to the LBS theme expert to ensure a consistent approach.

Where we are with the precedent case

Not applicable

Future litigation

Expected

Sector/Industries affected

Travel agents/Tour operators

Withdrawn

Caravan contents

Withdrawn

Characteristics

The claims involving caravans seen so far cover the following areas:

- Removable contents – see 701/20 3.1. Possible errors involving the liability of contents that is steps, wall mounted heaters, smoke and fire alarms etc. but **not** verandas.
- Method of accounting for Vat on removable contents on the sale of new and used caravans that differ from the recognised methods – see Notice 701/20 section 8.
- Discounts applied to caravan sales – applying only to zero rated caravan or as part of a package to include standard rated elements?
  Supplies of bottled gas – can be reduced rate if supply can be measured (that is amount of gas in a full bottle) but may have been standard rated in error. Caution – if gas is supplied from a bulk tank this may not be measurable to individual caravans (that is not metered) and in this case the reduced rate cannot apply.
- In addition to the above there may be attempts to circumvent those caravans sold under the margin scheme by wanting to use global accounting. This is specifically ruled out in margin scheme guidance (see VATMARG03100).

How to spot it

Claims involve caravan contents.

Key risks and issues

- Liability (gas/removable contents etc.)
- Entitlement to make a claim – covered in published guidance.
- Attempts to move away from published guidance especially involving the VAT treatment of removable contents in the sale of new or used caravans.
- Methodology used to calculate the claim – heavy use of sampling and extrapolation.

Current policy/precedent case/future litigation

Current policy is covered in Notice 701/20 and V1-8 section 21.

There are a number of litigation cases awaiting hearing. These principally involve the definition of removable contents post Talacre Beach and have been submitted by one of the main accountancy firms.

Where verification officers believe repayments to be due, they should consult Property VAT policy team in CT & VAT before making payment to confirm the circumstances are consistent with current policy.

Sectors affected

Mainly leisure but there could be implications for Real Estate (Land and Property).

Annex A - Fleming Claims and 'Kretztechnik' Share Issues Aide Memoire

Note - This aide memoire expresses the opinions of the Partial Exemption UoE and is for departmental use only. It does not override anything in the law, or in published notices or guidance

Withdrawn

Dates	C&E view of liability of share issues at the time	Standard method	Likely recovery of input tax on costs relating to share issue
01/04/73 - 31/03/84	Issues to UK/EC exempt. Issues outside EC zero-rated.	No direct attribution. All input tax residual. Residual claimed on outputs basis. Option to reclaim I/T on goods for resale in same state and treat balance as residual. **Businesses issuing their own shares must exclude the value of the share issue from their exempt and total supplies.**	I/T on share issues will have been treated as residual and claimed in line with the standard method in place at the time. Valid Fleming claims unlikely.
01/04/84 - 31/03/87	Issues to UK/EC exempt. Issues outside EC zero-rated.	No direct attribution. All input tax residual. Residual claimed on outputs basis. (No longer an option to reclaim I/T on goods for resale in same state and treat balance as residual.) Direct attribution permissible with C&E approval. **Businesses issuing their own shares must exclude the value of the share issue from their exempt and total supplies.**	If a business was otherwise fully taxable it would have achieved 100% recovery of its input tax relating to a share issue. A partly exempt business would automatically have treated the input tax on such a share issue as residual. Valid Fleming claims unlikely.

Dates	C&E view of liability of share issues at the time	Standard method	Likely recovery of input tax on costs relating to share issue
01/04/87 - 31/03/92	Issues to UK/EC exempt. Issues outside EC zero-rated.	Direct attribution to taxable and exempt. Residual claimed on basis of 'use' - any method acceptable except multiple calculations or outputs-based which required C&E approval. **Notice 706 example PE calculation was based on ratio of taxable input tax to total input tax.**	Possibility that fully taxable and partly exempt businesses could have directly attributed input tax relating to the issue of shares to 'exempt' and not reclaimed it. Valid Fleming claims possible, although very difficult to identify what the calculation used would have been.
01/04/92 31/12/92	Issues to UK/EC exempt. Issues outside EC zero-rated.	Direct attribution to taxable and exempt. Residual claimed on outputs basis. Certain incidental transactions could be excluded from the values calculation including share issues. Note: Businesses using the previous standard method could continue to operate it if they wished - C&E would automatically approve it on next visit.	If any of the shares were issued to non-EU counterparties for example U.S. bank, Channel Isles investment fund etc. then tax would have been treated as residual and recovered at 100% if fully taxable or residual rate if not. Valid claims possible, but evidence of shareholder register at issue should be sought.
01/01/93 - 30/11/94	Issues to UK/EC exempt. Issues outside EC outside scope with right to recover (specified supply). (Change in liability of supply w/e/f 01/01/93 to bring UK legislation fully into line with EC place-of-supply rules..)	(No change to the standard method.) Direct attribution to taxable and exempt. Residual claimed on outputs basis. Certain incidental transactions could be excluded from the values calculation including share issues.	If any of the shares were issued to non-EU counterparties for example U.S. bank, Channel Isles investment fund etc. then tax would have been treated as residual and recovered at 100% if fully taxable or residual rate if not. Valid claims possible, but evidence of shareholder register at issue should be sought.

Withdrawn

Dates	C&E view of liability of share issues at the time	Standard method	Likely recovery of input tax on costs relating to share issue
01/12/94 - 30/04/97 (final date to which Fleming claims for unrecovered input tax can be made).	Issues to UK/EC exempt. Issues outside EC outside scope with right to recover (specified supply).	Reg 103 amended to include anti-avoidance measure to deal with share issues on basis of 'use'. Direct attribution to taxable and exempt. Residual claimed on outputs basis. Certain incidental transactions could be excluded from the values calculation including share issues.	Input tax on all share issues recovered on the basis of 'use'. As the issue of shares is not a supply, Reg 103 should not have been applied. Input tax on share issues should have been treated as residual. Valid Fleming claims possible. Although it is also possible that businesses could have *over*-recovered input tax in these circumstances.

Withdrawn

Annex B – Kretztechnik (periods pre 01.04.87)

Withdrawn

Standard Wording for Current Claim Rejection Letter

"Your claim submitted in a letter dated xxxxxx states that under the ECJ ruling in the Kretztechnik case, input tax that had not previously been recovered on costs incurred in connection with the issue of new shares [securities/others etc] by..... Ltd on [date] was now recoverable.

It is clear from the then public notices that, neither legislation, nor the Department required direct attribution of input tax prior to 1 April 1987[1]. At the time a businesses should have treated VAT on the costs of a share issue as residual overheads and claimed it either in full or at the partial exemption recovery rate at the time. Accordingly, despite a mistaken belief that a share issue was an exempt supply, HMRC policy at the time was that a share issue would have no effect on the recovery of input tax. In the absence of evidence to the contrary a fully taxable business which followed HMRC guidance would have reclaimed the VAT in question at the time and your claim has now been rejected on this basis.

1 However input tax on goods for resale could be treated as wholly recoverable. If you applied to your local VAT office to use a direct attribution method after 1 April 1984, then you would have been required to directly attribute input tax both to taxable and to any exempt supplies."

For information/inclusion in the standard letter see below extracts from historic editions of VAT notice 706 relating to shares. The full version of the notice is held by the Partial Exemption Unit of Expertise.

What Notice 706 said:

August 1972 (On shares):

2. Matters to be disregarded for the purposes of this Notice

"Securities or secondary securities within the definition in section 42 of the Exchange Control Act 1947 which are issued, transferred or received, or dealt with in the course of the business, should be disregarded for partial exemption purposes unless the taxable person concerned **is wholly or mainly in business** to negotiate or undertake transactions in securities or to make arrangements for such transactions.

If transactions in securities or land, as described above, are the only exempt outputs that a taxable person has, he is treated as a fully taxable person and this Notice does not apply to him."

3. If in any tax period a taxable person's exempt outputs (**excluding** any transactions in securities or land as described in paragraph 2) are negligible or insignificant in relation to his total outputs, he may reclaim the whole of his input tax for that period, as if he were a fully taxable person, without apportioning it. For this purpose, negligible or insignificant means less than £100 per month on average or less than 5 per cent of total outputs, whichever is the greater"

(On holding companies): No specific mention.

September 1973 (On shares):

2. Matters to be disregarded for the purposes of this Notice

"Certain exempt transactions are not part of the normal pattern of a taxable person's business and he may disregard the following for partial exemption purposes:

(a) Transactions in securities or secondary securities within the definition in the Exchange Control Act 1947, section 42, (including gross receipts of interest on securities held) **unless the main purpose** of his business is to negotiate or undertake transactions in securities or to make arrangements for such transactions;

If a taxable person has no exempt transactions but these, he is treated as fully taxable and this Notice does not apply to him."

"3. If in any tax period a taxable person's exempt outputs (**excluding** any transactions in securities or land as described in paragraph 2) are negligible or insignificant in relation to his total outputs, he may reclaim the whole of his input tax for that period, as if he were a fully taxable person, without apportioning it."

(On holding companies): No specific mention.

September 1975 (On shares):

Exempt outputs to be disregarded for partial exemption purposes

"3. A taxable person may disregard the following exempt outputs for partial exemption purposes:-

(a) Any issue, sale or transfer in the course of business of securities or secondary securities which are within the definition of section 42 of the Exchange Control Act 1947,or any interest received from holdings of such securities, unless he is **wholly or mainly** in business to negotiate or undertake transactions in securities or to make arrangements for such transactions;

……………………..If he has no other exempt outputs, he is treated as fully taxable and this Notice does not apply to him."

"4. If in any tax period a taxable person's exempt outputs (**excluding** any transactions in securities or land as described in paragraph 3) are negligible, or insignificant in relation to his total outputs, he may reclaim the whole of his input tax for that period, as if he were a fully taxable person, without apportioning it."

(On holding companies): No specific mention.

September 1978 (On shares):

Outputs to be disregarded from partial exemption calculations

"3. A partly exempt person must exclude from any partial exemption calculation the following exempt outputs which might distort the result and, if he has no other exempt outputs, he is treated as fully taxable:

Withdrawn

(b) Any sum receivable as consideration for any issue, sale or transfer in the course of business of securities or secondary securities which are within the definition of section 42 of the Exchange Control Act 1947, or the gross interest receivable from holdings of such securities, unless he is **wholly or mainly** in business to negotiate or undertake transactions in securities or to make arrangements for such transactions;"

Insignificant exempt outputs
"4. ………………In applying the above rules a partly exempt person should take note of paragraph 3."

(On holding companies): No specific mention.

1 April 1983 (On shares):

Securities

“10. If you are "fully taxable", you remain so if you undertake dealings in securities within the scope of item 4 of Group 5 of the Exemption Schedule provided you are not **wholly or mainly** in business to negotiate or undertake transactions in securities or to make arrangements for such transactions. If you are not **wholly or mainly** in business for this purpose, you must not take into account the value of these exempt dealings in securities or the value of similar dealings within the scope of item 6 of Group 9 of the Zero Rate Schedule when applying the "outputs" rule (paragraph 13); and the input tax related to these exempt and zero-rated security dealings is to be disregarded when applying the "inputs" rule (paragraph 14).

The values for these dealings in securities are the total consideration for the sale of each security and any gross interest (i.e. total amount of interest before any deductions are made) received in respect of any security held.

This relief is not available to you if you are **wholly or mainly** in business to negotiate or undertake transactions in securities or to make arrangements for such transactions."

(On holding companies): No specific mention.

1 April 1984 (On shares):

“13. If you are fully taxable you remain so if you deal in securities within the scope of item 6 of Group 5 of the Exemption Schedule (see the VAT Leaflet Finance) provided the dealings are **incidental** to any of your business activities. If the dealings are **incidental**, you must not take into account the value of these exempt supplies or the value of similar zero-rated supplies within the scope of item 6 of Group 9 of the Zero Rate Schedule (see Notice 741 VAT: International services) when applying the outputs rules. In applying the inputs rule you must disregard the input tax related to these exempt and zero-rated security dealings.

You cannot regard dealings in securities as incidental if you undertake them in the course of any of the following businesses:

- A bank or licensed deposit taker;
- An accepting house;
- An insurance company, agent or broker;
- An investment trust or unit trust;

Withdrawn

- An **investment company**, unless acting on behalf of a company which does not carry on a business specified by this paragraph and where the companies are eligible to be treated as members of a group for VAT purposes, as explained in the VAT Leaflet Registration for VAT-Group treatment;
- A stockbroker, stock jobber or share dealing company;
- A trustee of a pension fund;
- A unit trust management company
- A building society;
- A discount house;
- A finance house;
- A friendly society
- A business similar to any of the above;
- A business of a kind listed above which is a member of a VAT group trading through the representative member.

But the following must always be treated as incidental:

- Supplies by a company of its own shares (including issues of shares to employees);
- Supplies by a company of shares in an associate company with which it is eligible to be grouped for VAT purposes, as explained in the VAT Leaflet Registration for VAT – Group treatment.

(On holding companies): No specific mention.

1 April 1987 (On shares): No specific mention.

(On holding companies): No specific mention.

1 April 1990 (On shares): No specific mention.

(On holding companies):

Holding Companies

"13. Customs and Excise now accept that where a holding company incurs input tax which does not relate directly to a taxable or an exempt supply (e.g. input tax on acquisition costs) this can be treated as part of the general overhead costs of the VAT registration as a whole. Where the registration is partly exempt this input tax is part of its 'non-attributable' input tax (paragraph 19).

Any input tax which a holding company incurs in relation to a specific supply would be dealt with under the normal rules."

1 April 1992 (On shares): No specific mention, except as below.

(On holding companies):

Holding Companies

"12. Customs and Excise now accept that where a holding company incurs input tax on costs which do not relate to actual taxable or exempt supplies (for example input tax on acquisition costs), this may be treated as part of the general overhead input tax of the VAT registration as a whole. Where the registration is partly exempt this input tax is part of its 'non-attributable' input tax (paragraph 19).

Withdrawn

Where a holding company incurs input tax which relates to actual supplies (for example the sale of shares), the input tax will be claimable or not according to whether the related supplies are taxable or exempt."

Amendment dated December 1995 (On share issues)

Input tax on the costs of share issues

“12A If you are a company and you issue your own shares, the input tax on the related costs is deductible according to the liability of the issue. If the issue is wholly an exempt supply, the input tax is exempt and must be restricted subject to the normal de minimis limit. If all the shares are sold to persons outside the EC, the input tax is claimable in full. If only some of the shares are sold to persons outside the EC, you can only recover input tax according to their proportion of the total. In these circumstances, whether or not you have a partial exemption method in place, you must separately identify the input tax on the share issue costs and deal with it on the basis of the **use** of the relevant goods and services. Only that proportion attributable to the part of the issue sold outside the EC was claimable…………………”

The notice then went on to suggest an apportionment based on numbers of shares. This was side-lined as a change to existing treatment.

(On holding companies):

Holding Companies

"12. Customs & Excise now accept that where a holding company incurs input tax on costs which do not relate to actual taxable or exempt supplies (for example input tax on acquisition costs), this may be treated as part of the general overhead input tax of the VAT registration as a whole. Where the registration is partly exempt this input tax is part of its non-attributable input tax (paragraph 19).

Where a holding company incurs input tax which relates to actual supplies (for example the sale of shares), the input tax will be claimable or not according to whether the related supplies are taxable or exempt."

The next notice was dated February 1999

Withdrawn

Annex C – Kretztechnik and AUTS - Standard Letter

Withdrawn

Dear

VAT No:

'Fleming' claim for input tax in respect of unit trust management

I refer to your claim by letter dated…….. [on behalf of …….] for input tax totalling £…… in relation to unit trust management activities from [date] to [date]. [This letter concerns your 'first' claim only as the Commissioners agree that where units are said to be the 're-issue' of redeemed units then, in the particular case of authorised unit trust schemes (AUTS), this is effectively the issue of units in the scheme (the 'alternate' claim).]

Your claim is based on the premise that, following the ECJ judgment in *Kretztechnik* (case C-465/03), the issue of units in return for the investment of capital does not represent a supply of services for VAT. HMRC's revised policy in this regard was set out in Business Brief 21/05 which concerns a number of situations where securities issued for the raising of capital are no longer viewed as supplies for the purposes of VAT.

However, we do not accept that it follows from the *Kretztechnik* judgment that the income derived and retained by the manager from issuing and redeeming units in the AUTS can be so disregarded. This is quite clearly the consideration for a supply of services by the manager.

During the period covered by the claim, HMRC operated a policy which, following the *Kretztechnik* judgment, was incorrect. This policy was to treat all issues of securities (including units in AUTS) as supplies of securities and exempt under what is now item 6, Group 5 of Schedule 9 to the VAT Act 1994 ('item 6') The consideration for the issue of securities was seen as the full amount received. Because it was recognised that inclusion of the full value in partial exemption calculations might be distortive, it was agreed that the manager's gross profit from issuing the units should serve as a proxy value to replace the full value for the purposes of partial exemption calculations.

Neither the full value nor the amount retained as income by the manager (the gross profit) is consideration for a supply of securities which is exempt under item 6. But neither the *Kretztechnik* judgment nor Business Brief 21/05 addresses how the manager's retained income, which is not invested as capital, should be treated for VAT purposes. As above, we take the view that this is the consideration for a supply of services by the manager.

On this basis, your claim must be refused in so far as it relies on the *Kretztechnik* judgment except to the extent that an exempt value has been used in the partial exemption calculations which does not equate to the income retained by the manager. Such retained income, which cannot be disregarded, is normally that derived from the operation of a bid/offer spread by the manager.

For completeness, you should note that, following the recent *Abbey National* ECJ judgment (case C-169/04), it is our view that the income retained from the spread on issuing/redeeming units in such circumstances is consideration for the manager's services of managing the AUTS. The issue and redemption of units in this context is

a function of management referred to at paragraph 13 of that judgment and, particularly when performed by the manager as part and parcel of the overall management of the fund, is currently exempt under item 9, Group 5 of Schedule 9 to the VAT Act 1994 (see also Business Brief 07/06, item 3 in this regard).

During the period of the claim, the management of AUTS was a taxable supply as the United Kingdom was under no obligation to exempt such services until the 18th Directive became effective on 1 January 1990. Accordingly, a claim for under claimed input tax could arise on a different basis from that currently relied on that is that the manager's income is consideration for taxable fund management services. However, in the event of such a claim, the output tax due on the management services which had previously been treated as exempt would have to be offset against any input tax claimed.

If you have any further information that you want me to consider, please send it to me now.

If you do not agree with my decision, you can

- ask for my decision to be reviewed by an HMRC officer not previously involved in the matter, or
- appeal to an independent tribunal

If you opt for a review you can still appeal to the tribunal after the review has finished.

If you want a review you should write to [name/team] at [address] within 30 days of the date of this letter, giving your reasons why you do not agree with my decision.

If you want to appeal to the tribunal you should send them your appeal within 30 days of the date of this letter.

You can find further information about appeals and reviews on the HMRC website What to do if you disagree with HMRC decision or you can phone the number on this letter. You can find out more about tribunals on the Tribunals Service website or you can phone them on 0845 223 8080.

Withdrawn

Annex D – Fleming Claims - Motor dealer Elida Table - Further guidance on its use.

Withdrawn

This internal guidance for HMRC officers supplements paras 2.4, 2.5 and 2.6 of the centrally issued HMRC:Fleming guidance and is to be read in conjunction with it.

1. Statutory interest.

The reason for the tables being divided into Elida (columns 1 and 2) and non Elida (columns 3 and 4) or showing where the line of supply is not known, is for the calculation of any SI. SI is notionally payable from the date of the departmental error: The dates will be different for Elida and non Elida cases.

2. Evidence.

The table itself is evidence of the way the manufacturer or dealer documented the bonus payment and the VAT liability they applied. It is also evidence of the line of supply where the information is known. The information in the table is then used to help establish, on a balance of probability, (in the absence of actual records), whether a claim should be paid.

A claim should be paid when the balance of probability indicates that

- the input tax block was required on the initial purchase invoice for the car **and**
- it was blocked **an**d
- the VAT on the bonus was posted to the VAT account.

3. The balance of probability that the input tax block was required.

In the majority of cases, the dealer would have ordered the car, or initially adopted the car, as a demo. The initial balance of probability is, therefore, that the law required the dealer to block the input tax on a demo car. The only alternative was the use of the self-supply provision.

The law required the self-supply provision to be used as an alternative to the input tax block only when the demo car was taken from adopted new car stock. This is considered to be a less common occurrence, **[This text has been withheld because of exemptions in the FOI Act 2000].**

4. The balance of probability that the input tax was blocked.

Failing to account correctly for VAT on demonstrator cars was seen as a risk. This would normally be checked when visits were performed and reports should confirm that the dealer did block the input tax or, where applicable, apply the self supply provision.

5. The balance of probability of the VAT on the bonus being posted to the VAT account:

a. Where invoices were issued by the dealer or self billed invoices were issued by the manufacturer.

Where the evidence of the documentation of the bonus payment shows a standard rated invoice or a self-billed document, the initial balance of probability in the context of a compliant business is that the dealer would have posted the VAT as output tax. This is not affected by whether the case is Elida or non Elida.

Each case will, however, be affected by any other information which alters that balance of probability, some of which will be manufacturer specific. If there is no other information, the balance of probability for a compliant business is that the tax was posted. Bear in mind, however, that failure to declare output tax on self-billed invoices was seen as a common risk.

Withdrawn

b. Where credit notes were issued by the manufacturer.

i. Elida (i.e. indirect line of supply) and credit notes.

In this situation, the standard rated credit note issued by the manufacturer was probably (at the time) a form of unauthorised self billing. The credit notes would not, however, have had the statement that the tax shown was the dealer's output tax which should be shown on his VAT return. This gives rise to the possibility that, in the absence of specific directions from the manufacturer or VAT officer, dealers would have processed the vehicle invoices and bonus credit notes in the same way as outlined in the "non Elida" section below.

To have a claim repaid, they would have to demonstrate that they a) did post the VAT on the bonus and b) they did block the input tax on the initial invoice for the car.

ii. Non Elida (i.e. direct line of supply) and credit notes**.**

In this situation, the credit notes were always discounts on the price of the car.

Under normal VAT rules, a credit note reduces the cost of items shown on an invoice. Where the VAT on the invoice is deductible, the VAT on the credit note reduces the amount deducted. Where the VAT on the invoice is blocked, the VAT on the credit note should not be entered in the VAT account either: there is no VAT to reduce.

If a dealer blocked the VAT on the initial purchase invoice, then the VAT on the credit note should not have been entered to the VAT account. **[This text has been withheld because of exemptions in the FOI Act 2000]** The dealer should not have posted VAT, and would have no claim for any VAT on the bonus to be repaid.

For a claim to be repaid, they would need to show a) they did post the VAT and b) they did block the input tax on the initial invoice for the car.

The posting of VAT does not always give rise to a claim for the VAT on the bonus which should be repaid. If they used the self supply provision, there should be no claim for VAT on the bonus.

iii. **Cases where the table does not identify the line of supply.**

The balance of probability is the same as for those where the line of supply is known.

A claim should be repaid only where the dealer both a) blocked the input tax on the initial invoice and b) posted VAT from an invoice, self bill, or credit note for the bonus.

However, the treatment for statutory interest is the same as for the Non Elida claims.

Summary

a. If a business cannot evidence (on a balance of probability) that the VAT on the bonus was posted to the VAT account, then the claim should be refused.

b. If a business can evidence that the VAT on the bonus was posted to the VAT account, in the absence of information indicating that they were required to use the self-supply provision, the balance of probability is likely to be that they were required to block the input tax on the car.

c. If they did post the VAT on the bonus to the VAT account and they were required to use the input tax block, that will give rise to an over-declaration of VAT. Subject to quantum, the claim can be paid.

d. Finally, if a business is making a claim on the basis that they used the self-supply provision, they must first evidence they did use the provision before any claim can be considered.

Motor UoE

04/01/2010

Withdrawn

Annex E – Postal services (TNT) -

Postal services claims - response to challenge on contractual position

Withdrawn

I write in response to your letter dated … concerning [your/your client's] claim relating to VAT and postal services supplied to [you/your client] by Royal Mail (RM) which was submitted following the European Court of Justice ruling in the case of TNT Post (UK) Ltd.

Firstly, I acknowledge that, in the absence of a VAT invoice, HMRC does have the discretion to accept alternative evidence under Regulation 29(2) of the VAT Regulations 1995. However, this discretion is only to be exercised where HMRC is satisfied that VAT has in fact been charged and paid on a supply.

Secondly, I accept that businesses have the right to rely on the direct effect of EU law in principle and, as a result, to treat supplies as taxable which the UK has erroneously treated as exempt. However, this does not resolve the question of whether or not VAT was charged and paid on a particular supply.

The question here is whether any amounts which [you/your client] agreed to pay RM for supplies which were at the time treated as exempt supplies but which should have been treated as taxable supplies were VAT inclusive or VAT exclusive. If they were VAT inclusive, in principle, VAT would be included in the price and would be recoverable (subject to time limits and the provision of satisfactory evidence etc). If they were VAT exclusive, in principle, it would not.

Paying a claim in a case where the agreement was that the price was VAT exclusive would compromise the neutrality of the tax, as there is no requirement in such cases for the supplier to account for the corresponding output tax.

The Principal VAT Directive does not contain any provisions as to the circumstances in which payments are to be taken to include VAT or not. This will depend on what the parties actually agreed. Our understanding is that RM's standard contract terms provide that any amounts were to be treated as exclusive of VAT and that any VAT, if due, was to be paid in addition. If this is the case, this is what the parties agreed.

Where the contract is not so explicit and the parties to the contract take different views, the content of the agreement between the parties has to be analysed according to the rules of interpretation applicable under national law. This is why we have requested evidence of the contractual arrangements which [you/your client] rely on in support of an argument that the price agreed did include an element of VAT.

As you have not provided any such evidence as requested, your [your client's] claim is accordingly rejected. [Add details of appeals procedures.]

If you choose to pursue the claim, I would remind you that it will remain subject to consideration of liability (i.e. whether the supply should in fact have been treated as taxable at the time when it was made).

Annex F – Lennartz - Standard Rejection Letter

Withdrawn

Dear Sirs (decision to go to the customer, copy to tax adviser if there is one)

CUSTOMER'S NAME IN HERE

VAT REGISTRATION XXX XXXX XX

CLAIM FOR REPAYMENT OF INPUT TAX

With regard to the 'Fleming' claim for £xxx,xxx set out in a letter sent on behalf of [customer's name in here] by [agent name] dated xx xxxxx 200x. This letter sets out HMRC's response.

I apologise for the delay in providing you with a decision in relation to this claim but I hope you will appreciate that the department has received a large number of 'Fleming' claims. Furthermore, claims such as this raised legal and technical issues which required policy and legal advice and this took a little time to organise.

The claim relates to [input tax] said to have been [under-recovered] on [type of] expenditure incurred in the course of the [purchase/construction] of [details of property] over the period [put relevant period of time in here]. The claim relies on the decision in the European Court of Justice case of Lennartz (C-97/90).

Summary

The Commissioners have reviewed your claim and its underlying premise, and have concluded that the claim should be rejected in full. This is because it does not take into account more recent case law from the European Court of Justice (ECJ).

The correct approach to claims made under section 121, FA 2008 (or on the basis of earlier 'Fleming' case law) is to analyse them against the relevant case law as it stands today (i.e. in compliance with the declaratory nature of case law). You are referred in particular to the case of *Vereniging Noordelijke Landen Tuinbouw Organisatie* (or VNLTO) – (C-515/07).

In my view, in the period(s) under consideration, [the customer's] activities of [detail here about the nature of the activities that were previously considered to be 'non-business'] form part of the wider purpose of [the customer's] undertaking or enterprise.

Taking VNLTO into account leads inevitably to a conclusion that the activities undertaken by [name of customer] should properly be regarded as by way of "business" (as defined for the purposes of Lennartz accounting by the ECJ in that case). Accordingly, Lennartz accounting was never available, as there is no non-business/private use of the property.

As there is no claim which is repayable, the question of Statutory Interest does not arise. I have set out the Commissioners arguments in more detail below.

Basis of Claim

The claim is one of a great many received by the Commissioners following the ECJ case of *Marks and Spencer* (case C-62/00) [2002] STC 1036) and the House of

Lords judgment in *Michael Fleming* (HL [2008] STC 324), which effectively disapplied the UK three-year "time limits" for making claims for input tax under-recovered or overpaid output tax.

In making your claim you rely on the decision of the ECJ in Lennartz in support of your contention that input tax has been under-recovered. In this 1991 case, the ECJ ruled that the taxpayer, who had a genuine intention to use a car partly for business and partly for private purposes, had a right to a full and immediate input tax deduction in respect of VAT
incurred on the purchase of his car. Where this was done, he, as a taxable person, was then obliged to account for output tax in respect of any private or non-business use of the car.

This decision relied on Article 6(2)(a) of the VAT Sixth Directive (now Article 26(1)(a) of Council Directive 2006/112), which provides that the following shall be treated as supplies for consideration –

> *'the use of goods forming part of the assets of a business for the private use of the*
> *taxable person or of his staff or more generally for purposes other than those of his*
> *business where the value added tax on such goods is wholly or partly deductible'*

The European Court of Justice held that this meant that the taxpayer made full taxable
use of his car – actual use in business motoring and also deemed taxable use in connection with his private motoring. As all use was charged with tax it followed there was an immediate right to full deduction of VAT incurred as input tax.

It is clear that Lennartz accounting cannot be used in cases where goods (which include services where those services are used to create goods) are used wholly for business purposes. According to the ECJ in the VNLTO decision, "business" in this context extends beyond economic activities giving rise to supplies within the scope of VAT: it also includes use for any activity that forms part of the wider purpose of the taxable person's undertaking or enterprise, even those activities that are not economic activities, and so are not normally regarded as "business" for UK VAT purposes.

It follows therefore that EC law does not give, and has never given, a right to use Lennartz accounting in circumstances such as those of the VNLTO case. An extract from the decision illustrates this point:

> *"It is also appropriate to state that, unlike Charles and Charles-Tijmens, which concerned immoveable property allocated to the assets of the business before being attributed, in part, to private use, by definition completely different from the business of the taxable person, the situation in the main proceedings in the present case relates to transactions other than VNLTO's taxable transactions, consisting in safeguarding the general interests of its members, and not capable of being considered, in this case, to be non-business transactions, given that they constitute the main corporate purpose of that association.*
>
> *"Consequently, the answer to the first question is that Articles 6(2)(a) and 17(2) of the directive must be interpreted as not being applicable to the use of*

Withdrawn

goods and services allocated to the business for the purpose of transactions other than the taxable transactions of the taxable person, as the VAT due in respect of the acquisition of those goods and services, and relating to such transactions, is not deductible."

The Commissioners have not examined in detail any documentary evidence you have provided which demonstrates the extent to which past supplies made by you (or a predecessor) were 'on all fours' with those examined in Lennartz. Nor have they examined in detail the basis you have used to calculate the value of your claim, or considered whether the claim may be invalid for other reasons than that given above The reason for this is because it is clear in light of the more recent ECJ judgment that [customer name] has undertaken no non-business or private use in this context. The claim cannot therefore succeed on reliance of the Lennartz case.

I should however, for the sake of completeness, draw your attention to the Commissioners' published guidance on the burden of proof and the standard of evidence required to support claims made under section 121 of the Finance Act 2008 ('Fleming' claims). That guidance can be viewed at HMRC's website address below:

http://www.hmrc.gov.uk/menus/fleming-guidance.pdf

If, following any subsequent review or appeal that may take place as a result of this decision letter, the above reasoning is ruled not to apply to your claim or any part of it, the Commissioners reserve the right to examine further the factual basis underlying your claim and the means by which any relevant amounts claimed have been calculated so as to establish the correct amount repayable, and to consider whether the claim may be invalid for other reasons.

Case Law Precedent

One of the fundamental concepts of case law is that it is 'declaratory' in nature. In other words the judge declares what the law is and always has been.

The European Court of Justice (ECJ) is the final authority on the interpretation of Community law. Community law has supremacy over national law, even if they are contradictory. National courts are obliged to interpret national law so that it is consistent with any guidance given by the ECJ.

Accordingly**,** as a consequence of the ECJ case of VNLTO, the Commissioners have recently issued a Revenue and Customs Brief (02/10) announcing a policy change to implement the judgment. I attach this for your information.

Conclusions Regarding your Claim

It is clear from the above case law that what was previously regarded by HMRC as non-business activities for the purposes of Lennartz, whilst viewed as correct at the time, must now be considered in a different light.

Consequently, Lennartz cannot be relied upon when analysing claims submitted under section 121, FA 2008 (or on the basis of earlier 'Fleming' case law) where there is no non-business or private use of a property. The correct approach is to analyse such claims against the relevant case law as it stands today.

Withdrawn

The declaratory nature of case law in the UK means that in these circumstances Lennartz was never available. Accordingly, any input tax attributable to the non-taxable business element of the supply has always been non deductible.

Furthermore, where a customer took the decision not to adopt Lennartz accounting at the time the VAT was incurred, a 'Fleming' claim will not be permitted as this is not considered an error.

For all the above reasons your claim is refused. As there is no claim which is repayable, the question of Statutory Interest does not arise.

Right of Statutory Review and of Appeal

You have a statutory right to a review of this decision by an HMRC officer not previously involved in this case. That officer will review this matter to ensure that the decision is correct, is in keeping with HMRC's view of the law and properly represents HMRC's position on this issue. The reviewing officer may decide to uphold, vary or withdraw the decision.

If you would like a review, you should [insert appeal and review paras]

If a review has not been completed within the review period (and no extension is agreed), the original decision will be deemed to have been upheld. If you are not satisfied with the outcome of the review, you will have a period of 30 days from the conclusion of the review to appeal to an independent tribunal. Please note that, if you take up the offer of a review, you cannot appeal to the tribunal until the review period has ended.

You also have a right to appeal directly to an independent tribunal against this decision. You can appeal without requesting a review by HMRC but you should note that you will not be entitled to a review once an appeal has been made to the tribunal.

If you wish to appeal, you must do so within 30 days of the date on this letter (or the review conclusion letter, if relevant). You will find further guidance about appealing on the Tribunals Service website (www.tribunals.gov.uk - scroll down to tax).

Also, if you disagree with this decision and feel that there is either something that has been misunderstood or further information that should have been taken into account and you would like me to consider it further, then you should write to me, allowing me sufficient time to grant you an extension to the 30 day period for review or appeal, before it has expired.

Please note that I cannot grant such an extension once the 30 day period has expired and you could then be in the position of needing to make a belated request for a review or of making a belated appeal to the Tribunal. If you do want an extension to the time to seek a review or to appeal, it would be helpful if you could indicate to me when you expect to be able to provide the further information.

If you have any questions relating to this letter please contact me [insert telephone number].

Yours faithfully

Withdrawn

Annex G – Pensions 70/30 Split – More detailed guidance from CT&VAT

Withdrawn

Claims for Input Tax on Funded Pension Schemes

Recovery of VAT incurred by employers on funded pension schemes which is now the subject of 'Fleming' claims.

Summary of recovery

Our treatment of funded pension schemes has altered over the years as a result of developing case law and changes in policy:

1973-1978 – All employers were entitled to recover input tax on setting up the funded pension scheme and reviewing and restructuring existing schemes.

1978-1982 – VAT registered employers who were also sole trustees and corporate trustees who were entitled to group registration could recover input tax on day-to-day administration costs.

All employers were still entitled to recover input tax on setting up the funded pension scheme and reviewing and restructuring existing schemes.

1982-Present - All employers are entitled to recover input tax on 'management activities', which includes setting up the funded pension scheme, reviewing and restructuring existing schemes and day-to-day administration costs.

Please see below for details of the historical background which led to the above changes in treatment.

Claims

A number of Fleming claims have been received from businesses seeking to recover input tax with regard funded pension schemes.

The policy team dealing with Fleming claims have confirmed that a change in policy is generally not applied retrospectively. Changes in interpretation of law however which usually take place because the courts have found that that interpretation is incorrect are applied retrospectively.

Central Policy advise the burden of proof is on the claimant. They must provide evidence that the input tax was incurred, that it was not deducted and that the amount claimed is accurate. The level of proof in these cases is a 'balance of probabilities', however you are entitled to refuse a claim until you are satisfied.

1. Company is seeking to recover input tax on fees for management services before 01 April 1982.

We accept that this is the employer's input tax and therefore they are entitled to input tax recovery.

Employers have always been entitled to recover input tax on expenses incurred on setting up the fund and reviewing and restructuring existing schemes. Therefore, claimants will need to prove their claim does not include costs incurred on these activities and if it does that they did not deduct the input tax now being claimed, see comments at point 2(b).

Employers who were also sole trustee could recover expenses incurred on management activities, for example setting up the fund, reviewing and restructuring existing schemes and day to day administration costs, through their VAT registration and corporate trustees eligible for group registration could recover expenses incurred on management activities through their representative member. Therefore claimants will need to prove they were not a sole trustee or corporate trustee eligible for VAT registration and if they were that they did not deduct the input tax now being claimed, see comments at point 2 (b).

2. Company is seeking to recover input tax on fees for management services after 1 April 1982.

(a) All employers were entitled to recover input tax on management activities after this date. Therefore claimants will need to provide evidence that the input tax was incurred, that it was not deducted and that the amount claimed is accurate.

(b) Prior to 1 May 1997, when the 3 year cap on input tax was introduced, employers could make claims for input tax on fees for management services. Where HMRC do not accept that a claimant was denied entitlement to deduct input tax from a date prior to 1 May 1997 the onus is on the claimant to satisfy HMRC no such claims were made, in the absence of compelling evidence from the claimant the claim should be refused.

3. Company is seeking to recover 30 per cent VAT on fees for third party services before 1 April 1996.

The introduction of 30 per cent recovery on fees from third parties supplying both management and investment services was a policy decision to facilitate businesses and therefore can only be applied from the date the change was announced, 1 April 1996. These claims should be refused on the grounds that the employer could recover input tax on fees for management services based on previous published guidance in VAT Notice 700/17/83. This clearly advised professional trustees and administration companies that if they provided both administration and investment services separate invoices must be issued, otherwise the employer would not be able to recover their input tax because of insufficient evidence to establish the recoverable amount.

4. Company is seeking to recover 30 per cent VAT on fees for third party services after 1 April 1996.

If the company has, in error, failed to recover input tax on fees for management services, they are entitled to recover their input tax. However, our policy has always been that the 30/70 split should only apply where a third party, for example fund manager, property manager or professional trustee, is appointed to manage the scheme, their services include both management and investment services and they only issue an inclusive invoice for both services.

Withdrawn

It is for the claimant to satisfy us he has failed to deduct the input tax that he is now claiming, as per the guidance at point 2 (b). If input tax has been recovered on management services in the same period the claimant will need to satisfy us that the claim for further input tax is with regard to further management services received and not previously recovered.

5. Company is seeking to recover all of the VAT incurred, including on 'investment' services.

Recovery of VAT incurred on investment services is inconsistent with our policy as detailed in this document. Where Redrow and any similar direction of supply type cases are quoted in relation to these claims these issues should be referred to Supply of Services and Public Bodies team who have responsibility for this area.

History

1978

Following the Court of Appeal decision in British Railways Board and other developing case law Custom's revised their policy regarding what they considered to be the 'dual personality' of a VAT registered entity with beneficial and fiduciary duties.

Custom's previously required trustees to register separately, subject to eligibility, in respect of their trusteeship. Under the revised policy VAT registered entities who were also sole trustee of a trust and corporate trustees eligible for group registration were regarded as capable of acting in both their beneficial and fiduciary capacities under the beneficial business' VAT registration, when the trust's activities formed part of the activities of the beneficial business. Thus employers, who were also sole trustee or corporate trustees entitled to group registration, could recover input tax incurred on the day to day administration of the pension fund.

This led to disparity of treatment because employers whose pension funds had separate trustees could not recover input tax on the day to day administration of the pension fund in this way. This is because these supplies were regarded as made to the separate pension fund trustees and not the employer.

At this time we still allowed employers to recover input tax on expenses incurred on activities such as setting up the fund and reviewing and restructuring existing schemes because these supplies were regarded as received by the employer.

1983

VAT Notice 700/17/83, Funded Pension Schemes:

This was the first time a VAT Notice was issued regarding funded pension schemes.

This VAT Notice extended what we previously regarded as expenses incurred by the employer, allowing all employers to recover input tax on expenses incurred on setting up the fund and day-to-day administration costs, provided valid VAT invoices were held in the employer's name. Investment costs were specifically not recoverable. Entitlement to claim was backdated to 1 April 1982, the effective date broadly coinciding with the Manchester Ship Canal ruling.

Withdrawn

Professional trustees and administration companies were advised if they provided both administration and investment services separate invoices must be issued, otherwise the employer would not be able to recover their input tax because of insufficient evidence to establish the recoverable amount.

April 1996

Public Notice 700/17/96, Funded Pension Schemes updated (rewritten March 2002, technical content remained unchanged):

This introduced the use of the 30/70 split: where a third party managed the pension scheme and provided both management and investment services and issued one inclusive invoice the employer is entitled to recover 30 per cent of the VAT charged as input tax. However, if the third party apportioned their supply between investment and management services and issued separate VAT invoices then the employer is entitled to recover 100 per cent of the input tax on the management services only.

9 August 2005

Business Brief 15/05:

This was issued to address HMRC's concerns that businesses were applying the 30/70 business facilitation to gain a higher recovery of input tax than is fair and reasonable. The BB advised from 1 October 2005 third parties must genuinely be unable to provide a breakdown of their services and be administering the pension scheme fully or providing the bulk of the administration for the scheme in order for the employer to apply the 30/70 split. However, HMRC advised we 'will not challenge the use of the 30/70 split for invoices received for periods up to and including 30 September 2005.

18 August 2005

Business Brief 16/05:

This BB advised that, in order to allow third parties time to amend systems to comply with the new rules, HMRC agreed changes would not take effect until 1 January 2006.

10 October 2005

Business Brief 19/05:

HMRC withdrew BB15/05 subject to a full consultation with the industry. Employers were advised to continue as before until further announcement.

Current policy

While consultation with the industry did take place no resolution was achieved. Our current policy is that management of a pension scheme for employees is part of the employer's business activities; therefore VAT incurred on day-to-day management of the scheme is input tax. 'Management' services include: making arrangements for setting up a pension fund, collection of contributions and payment of pensions,

Withdrawn

accountancy and auditing relating to management of the scheme, general actuarial advice connected with administration of the fund.

Investment activities are not regarded as part of the employer's business activities and therefore the VAT incurred is not recoverable by the business. 'Investment' services include: advice re investments, rent and service charge collection for property holdings, brokerage charges and trustee services.

If the above services can be identified separately only the input tax on management services should be recovered. However if this cannot be done then the 30/70 split can be applied where the invoice received is for both management as well as investment services proper to the trust.

Withdrawn

Annex H – part exchange

Re: Valuation of vehicles taken in part exchange

Withdrawn

Thank you for your correspondence regarding the above. Although you write on behalf of your client [ ] the issue will affect other dealers in the same situation.

Your claim is that your client has overpaid output tax because of the way that a car taken in part exchange was, or should have been, valued under the VAT Act 1983.

Basis of the claim

To ensure our understanding of your argument, I will re-state it here.

The situation is that when your client (and, presumably, any similar dealer using the 'Margin Scheme') accepts a car from a customer in part exchange for a new car, it will often offer a valuation greater than that given in a trade guide, such as Glass's Guide. The car taken in part exchange is non-monetary consideration towards the price of the new car – the customer then has to pay the difference, either in cash or through a finance agreement. It is the value of this non-monetary consideration (NMC) that is the subject of your claim.

I think we are agreed then, that, when your client (and indeed, any dealer) accepts a car that, for example, is worth £1,000 according to a trade guide, and allows a value of £1,500 (that is, accepts the car as payment worth £1,500 towards the price of the new car) the value of the NMC is £1,500 being the value "overtly agreed and adopted by the parties".

Essentially, your argument is that the valuation is different where the transactions occurred prior to 1 August 1992 when the wording of the legislation in the 1983 VAT Act was changed. Originally, the Act stated that NMC should be defined as the "Open Market Value" (OMV). This was later amended following the ECJ ruling in the "Naturally Yours" case which established that the value of NMC should be the subjective value.

You argue that the OMV should be the value quoted in "Glass's Guide" or a similar trade guide for the second-hand car trade. Thus, consequently, if you are correct, your client has overstated its output tax (being based on the higher, subjective, value of the NMC received towards the price of the new car) for supplies made before 1 August 1992.

I trust my understanding of your case is correct.

HMRC's case

The VAT Act 1983 (at section 10 (5)) defines OMV as being the value under section 10 (2) as if the consideration was in money and payable by a person standing in no such relationship with any person as would affect that consideration (s.10 (2) states that the value is the consideration less the tax). In other words, as if money (rather than NMC) was paid and there was no relationship between the supplier and the customer that would affect the consideration to be paid, that is, an arm's length transaction.

So, all s.10(5) says is that the NMC would be the same as if the customer was paying cash in a straightforward, arm's length deal between unconnected persons (such as where there was no family, business or other connection between the supplier and the customer that would affect the price).

As with any selling/buying situation the supplier may offer, and the buyer may request, discounts or other incentives, and come to an agreement on price, etc.

A trade guide, such as Glass's Guide, is only a guide – it does not in any way set or fix the price at which a dealer must buy or sell a car. Every dealer, and every customer, is free to bargain over prices.
When a customer offers his own car in part exchange, it doesn't come with a pre-determined value. It is for the dealer and the customer to agree. The dealer could insist on a lower value for the part exchanged car, but give a discount on the new car (or a portion each way, or none at all). But, ultimately, whatever they agree to must be the value of the part exchange car, because, until then, there is no value.

The motor trade, with HMRC's (and previously HMC&E's) knowledge has always treated OMV as the subjective value. The 1983 Act merely defines OMV as that in a straightforward transaction where there is no relationship between the persons involved that would affect the consideration. In such a transaction the parties have always been free to negotiate and agree a value – in other words, the OMV has always been subjective.

HMRC's legal advice

HMRC has obtained legal advice on this issue. That advice confirms our view that the UK has always interpreted OMV in line with European valuation principles. All that "Naturally Yours" did was confirm that that interpretation was the correct one. It is clear that the motor trade made the same interpretation and the ECJ has made it clear that that was correct.

HMRC guidance V1-12 "Valuation"

Our guidance on NMC covers the pre-1992 position. It reads as follows:

4.8 Value of non-monetary consideration before 1 August 1992 - open market value

Before 1 August 1992, the VAT Act 1983 Section 10(3) required a supply for non-monetary consideration to be valued by reference to open market value:

"(3) If the supply is for a consideration not consisting or not wholly consisting of money, the value of the supply shall be taken to be its open market value".

"Open market value" was then defined in S10(5) of the VATA 1983:

"(5) For the purposes of this Act the open market value of a supply of goods or services shall be taken to be the amount that would fall to be taken as its value under subsection (2) above if the supply were for such consideration in money as would be payable by a person standing in no such relationship with any person as would affect that consideration."

Withdrawn

Section 10(3) was amended to the wording that can now be found in Section 19(3) of the VAT Act 1994 to clarify the position in UK law following the outcome of the Naturally Yours case. It should be noted that despite the previous use of the words "open market value" in the provision, the UK had been interpreting its law in a manner that had accorded with the European valuation principles.

Withdrawn

Conclusion

It is our firm view that HMRC's interpretation of NMC under the 1983 Act prior to the ECJ ruling was the same as it is now after that ruling – nothing has changed. It is also our view that the motor trade held the same interpretation. That interpretation was the correct one, as it is now, as made clear by the ECJ, and stated in our guidance, and reinforced by legal opinion. Consequently, the use of the subjective value was not contrary to the UK legislation either prior to 1 August 1992 or since and there is no case for re-valuing the supplies or re-calculating the output tax as suggested. Your client's claim is therefore refused.

If you do not agree with my decision, you can:

- ask for my decision to be reviewed by an HMRC officer not previously involved in the matter, or
- appeal to an independent tribunal

If you decide that you want my decision to be reviewed you can still appeal to the tribunal after the review has finished.

If you want a review you should write to me at the above office within 30 days of the date of this letter, giving your reasons why you do not agree with my decision.

If you want to appeal to the tribunal you should send them your appeal within 30 days of the date of this letter.

Where can I go for further information?

You can find further information about appeals and reviews on the HMRC website What to do if you disagree with HMRC decision (http://www.hmrc.gov.uk/complaints-appeals/how-to-appeal.htm) or you can phone the number on this letter.

You can find out more about tribunals on the Tribunals Service website (www.tribunals.gov.uk/tax/) or you can phone them on 0845 223 8080.