[2018] UKUT 0409 (TCC)

Appeal number: UT/2018/0024

VALUE ADDED TAX – VATA 1994, sections 19(4) and 73(6) – opticians – separately disclosed charges – Information Sheet 08/99 – attribution of discounts – whether decisions issued more than four years after repayment returns submitted time barred – whether assessments out of time – appeal allowed in part

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

ON APPEAL FROM THE
FIRST-TIER TRIBUNAL (TAX CHAMBER)

DCM (OPTICAL HOLDINGS) LIMITED

Appellant

v

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

TRIBUNAL: LORD TYRE
JUDGE DEAN

Sitting in public at George House, 126 George Street, Edinburgh on 8, 9 and 10 October 2018

Roderick Cordara QC and Andrew Legg, instructed by Harper Macleod LLP, for the Appellant (DCM (Optical Holdings) Limited)

David Thomson QC and Elizabeth Roxburgh, instructed by the Office of the Advocate General for Scotland, for the Respondents (HMRC)

Introduction

1. The appellant ("DCM") carries on business as an optician under the trading name Optical Express, specialising in the sale of dispensed spectacles and the provision of refractive eye surgery. For the purposes of value added tax, DCM, in common with other opticians, makes both taxable supplies of goods and exempt supplies of medical services. This gives rise to complexities as regards both output tax chargeable and input tax recoverable. The current proceedings are concerned only with output tax related issues.

2. DCM appeals against a decision of the First-tier Tribunal ("FTT") which concerned six separate appeals. In accordance with the approach adopted by the parties in their written and oral submissions and by the FTT in its decision, we will not address the six appeals individually. Instead we will deal thematically in turn with the four disputed matters that are identified in the grounds of appeal, some of which relate to more than one appeal.

3. The original decision of the FTT was issued on 23 March 2017. Following the submission by DCM of an application for permission to appeal, the FTT decided that it was appropriate to review its decision. A revised decision bearing the original release date was issued on 30 October 2017. DCM submitted an amended application for permission to appeal which was granted by the FTT on 13 February 2018. One of the grounds of appeal raised the question whether the revised decision was wholly or partly outside the scope of the power to review permitted by rule 41 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. In the event no submissions were made to us in support of this ground of appeal, and it is unnecessary for us to address it. Our consideration of the appeal proceeds on the terms of the FTT's revised decision.

Opticians and VAT

4. As already noted, opticians make both taxable and exempt supplies for VAT purposes. In *EC Commission v UK* [1988] STC 251, the Court of Justice ruled that a supply of goods such as spectacles was physically and economically dissociable from the provision of medical care and should not therefore be exempted from VAT. Thereafter HMRC sought to treat the supply of spectacles as a single standard-rated supply to which the dispensing opticians' services were merely ancillary. This approach was rejected in *C&E Commissioners v Leightons Ltd* [1995] STC 458, in which it was held that in substance and reality there were two separate supplies: a taxable supply of spectacles and an exempt supply of services of the dispensing optician.

5. Section 19(4) of the Value Added Tax Act 1994 states:

"Where a supply of any goods or services is not the only matter to which a consideration in money relates, the supply shall be deemed to be for such part of the consideration as is properly attributable to it."

Applying this provision to supplies made by opticians has not proved to be a straightforward matter.

6. In 1999 HMRC published VAT Information Sheet 08/99 entitled "Opticians: Apportionment of charges for supplies of spectacles and dispensing". This information sheet consolidated guidance contained in previous information sheets and business briefs. HMRC noted, under a heading "Current position":

> "If a single charge is being made for supplies of spectacles and dispensing, opticians should now be apportioning this in accordance with a method that has been agreed with their local VAT Business Advice Centre. Alternatively, they may be making separate charges for spectacles and dispensing which should be disclosed to all patients at the time of sale. **Customs have no preference as to which of the above arrangements individual opticians adopt."** (Emphasis in original.)

7. One of the methods that opticians could choose to adopt was what is known as the full cost apportionment method ("FCA"). Annex A to the information sheet contained HMRC's technical guidance about a suggested full cost apportionment method, although it was open to opticians to propose other methods for approval. Alternatively, if an optician chose to use a method in which charges were separately disclosed to customers ("SDC"), Annex B contained guidance about the criteria that needed, according to HMRC, to be satisfied to establish a true separation of charges. Annex B stated *inter alia* as follows:

> "**Separately disclosed charges**
>
> Opticians will not be required to perform an apportionment of charges for spectacle sales if they make separate charges for the spectacles and the dispensing, thus establishing a separate consideration for each of the supplies. One of the normal criteria for establishing separate considerations is that customers should be able to obtain the supplies separately at the individual specified charges should they so wish. This is not usually possible with dispensing services which are normally 'tied to' the supply of spectacles. Customs have therefore relaxed this requirement and will accept that separate considerations have been established for the spectacles and dispensing if the charges for each are stated and made known to **all** patients at the time of the supply."

It was reiterated that HMRC did not require the charges to be disclosed by any particular method.

8. Information Sheet 08/99 does not have the force of law. It sets out guidance for taxpayers on HMRC's view of the law and was aptly described in the course of the hearing before us as a "safe haven" for taxpayers. For the purposes of the present appeal, parties were agreed that a method which met the description of SDC in the information sheet would be

regarded by HMRC as constituting a reasonable apportionment for the purposes of section 19(4) of the 1994 Act.

Background to the disputed assessments and decisions

9. Since at least 2000, DCM has been in dispute with HMRC over a variety of input tax and output tax issues. There have been previous tribunal and court decisions concerning the partial exemption method adopted by DCM for recovery of input tax. We were informed that the input tax issues which have been the subject of voluminous correspondence over a period of many years have now been resolved. None of these input tax issues therefore arises in the present appeal and we do not consider it relevant to rehearse them in this decision. It is however important to be aware of them as providing part of the explanation of why the matters that do arise for decision in these proceedings have taken so long to come before a tribunal for determination.

10. Some of the contentious output tax issues have also now been resolved or have fallen away. One of those, namely the VAT treatment of Careplan payments, was included in the grounds of appeal to the FTT, but by the time of the hearing it had been conceded by DCM that HMRC's treatment of these payments was correct. There remained – and still remain – two substantive output tax issues.

11. The first of these concerned the information that had to be provided by DCM to customers in order to comply with the requirements of Information Sheet 08/99 for a separately disclosed charges (SDC) method. This was the subject of correspondence during 2003 between DCM and its advisers PWC on the one hand and HMRC on the other. We will require to look at this correspondence in more detail later, but it is sufficient at this stage to say that DCM considered that the information being supplied was sufficient to be compliant, and HMRC disagreed. With effect from February 2004, DCM amended the layout of the order confirmations provided to customers, and HMRC have since accepted that the version as thus amended was compliant. There remained, however, a dispute as to whether the pre-February 2004 method had been compliant.

12. The second substantive output tax issue concerned the allocation of DCM's customer discounts as between (taxable) supplies of goods and (exempt) supplies of eye tests and dispensing services. This was a matter of importance because the greater the proportion of discounts allocated to taxable supplies, the less the amount of VAT chargeable. The FTT heard, and accepted, a great deal of evidence that over a period of years DCM persistently failed to respond to requests from HMRC for documentary vouching of the allocation of customer discounts. It appears from the FTT's findings that DCM's computer systems were not set up to provide this information, and that DCM considered that the amount of effort involved in extracting it from their records would have been disproportionate. No copy receipts or customer order confirmation forms were produced to HMRC at that time.

13. DCM's VAT return for the period 07/05 was a repayment return, ie it disclosed a repayment due by HMRC. In light of the ongoing dispute, HMRC's officers placed a "repayment inhibit" on the ledger preventing any repayment or credit to DCM pending investigation of the validity of the return. That repayment inhibit remained in force for subsequent returns. With the exception (due to an error by HMRC) of the return for period 10/05, it prevented any repayment being made in respect of every return thereafter up to and including period 12/08. At various dates in 2008 and 2009, HMRC made decisions purporting to amend (ie reduce) the amounts claimed as repayments. Revised decisions covering the same periods were subsequently made in 2013.

14. The various appeals which came before the FTT, and which are now before the Upper Tribunal are against:

    (i) assessments on "best judgment" of output tax underpaid for four periods prior to February 2004, namely periods 10/02, 01/03, 04/03 and 07/03 (appeal 1);

    (ii) the decisions issued in 2013 amending DCM's repayment claims for the periods between 07/05 and 12/08 (appeals 2 to 6).

Summary of grounds of appeal

15. The grounds of appeal to the FTT which remain alive for our determination may be summarised as follows:

    Ground 1 – The amendment issue

    DCM contends that HMRC had no power to "amend" the repayment returns submitted, without any applicable time limit. If HMRC wished to refuse repayment in full, this required to be done by assessment, which would be subject to the statutory time limits in VATA 1994, section 73. No timeous assessments were made. (We refer to this ground as the "amendment issue"; in the FTT decision it is referred to as the "quasi-assessment issue" but we prefer not to adopt this misleading label.)

    Ground 2 – The SDC issue

    DCM contends that prior to February 2004 it operated a SDC method of apportionment which complied with the requirements of Information Sheet 08/99.

    Ground 3 – The discounts issue

    DCM contends that the evidence demonstrates that all discounts offered to customers were given against taxable supplies of goods, and that HMRC were not entitled to substitute a pro rata allocation of discounts to taxable and exempt supplies.

Ground 4 – The time bar issue

DCM contends that, in any event, the assessments in respect of periods 10/02, 01/03, 04/03 and 07/03 were made out of time.

16. The FTT found in favour of HMRC on all of the above issues, and dismissed all six appeals.

Ground of appeal 1 – the amendment issue

17. We have already noted that the VAT returns to which this ground of appeal relates (07/05 to 12/08, under exception of 10/05) were repayment returns. HMRC were not satisfied that the amounts of output tax shown in the returns were correct and the officer (Boyle) dealing with DCM placed an inhibit on its account which prevented repayments being made. The FTT found that Officer Boyle did not understand the effect of the inhibit and, in particular, was of the view that the time limit in VATA 1994, section 73(6) for the making of assessments was running. For this reason, she purported to issue what she described as "protective assessments" in 2008 and 2009 because three years were about to elapse from the dates of submission of the returns. The FTT further found that Officer Boyle's confusion was shared by the senior officer (Rae) to whom she reported, who wrote to DCM in December 2008 to inform them that a decision notified to them on 27 November 208 in respect of DCM's repayment claim for period 10/05 had been out of time and was being withdrawn. The internal mechanics of the repayment inhibit procedure, and the uncertainties that it created in the minds of officers, are described in the FTT's decision, but we do not find it necessary to go into the same level of detail.

18. When another officer (Little) issued revised decisions on 1 February 2013 in respect of all of the above periods, HMRC were no longer describing their decisions as assessments (although the confusing phrase "quasi-assessment" has continued to be used up to and including the submissions made to us). With the exception of one period, the effect of Officer Little's decisions was to reduce the amount of repayment claimed while still leaving a balance due to DCM. In the exceptional case, the reduction was sufficient to produce an amount due to HMRC, but it was accepted that HMRC were too late to make an assessment and so the repayment was simply reduced to nil.

19. The issue that now arises for determination is whether HMRC had power in 2013, many years after the ends of the periods in respect of which repayments were claimed, to amend the amounts claimed by reducing them to lesser amounts or to nil.

The FTT's decision

20. The FTT accepted that when a repayment return was submitted, HMRC had the right to refuse it in whole or in part. HMRC were under a duty to conduct a reasonable and proportionate investigation into the validity of claims for repayment, and to take a

reasonable time to do so. What was reasonable depended upon the facts of a particular case: *R (UK Tradecorp Limited) v C&E Commrs* [2005] STC 138. In the present case the delays were in very large part attributable to DCM's failure to respond to requests for information. The remedy lay in DCM's hands: it could provide information or, alternatively, seek judicial review of HMRC's decision to inhibit repayment. The officers concerned had acted proportionately against the background of DCM's lack of co-operation.

21. The FTT further accepted HMRC's submission that there was no need to raise an assessment where no tax was due. The time limits in section 73(6) could only start to run where an error in a return gave rise to a debt due *by* the taxpayer. The officers had acted correctly in intimating their decisions as to the amount repayable. Those decisions were appealable, as had occurred. As there were no assessments, no issue of time bar arose.

Argument for DCM

22. On behalf of the appellant it was submitted that HMRC had no power to make "amendments" to a taxpayer's VAT returns without limit of time. VAT, like all taxes, is a creature of statute. The so-called amendments had no statutory basis. The time bar provisions in sections 73 and 77 were strongly worded so as to forbid assessments out of time: once four years had elapsed, the position was crystallised and could not be disturbed by either side. It was obvious that the reason why HMRC had purported to make amendments rather than making assessments in the ordinary way was to circumvent their failure to assess within the statutory time limit. But no sum could become due to the Crown other than by the making of an assessment. There was no statutory provision that created a debt due to the Crown outside the assessment provisions.

23. HMRC's approach, which was erroneously accepted by the FTT, was that (i) no sums due to the taxpayer were affected by amending the return because there was no right to repayment unless and until it was accepted by HMRC as correct; and (ii) that no debt was created by amending the return unless a net sum was due by the taxpayer. The first of those errors violated the principle of fiscal neutrality, which required that the right to deduct input tax and be paid any net sum owed arose when the return was submitted. Whilst such entitlement could be temporarily suspended pending a proportionate investigation, that did not mean that the right itself did not arise until the return had been verified and/or an investigation had been concluded. Both HMRC and the FTT had erroneously conflated the right to payment of a credit (which could be suspended during investigation) and the underlying right to the credit itself. A further difficulty with the FTT's approach was that it contravened the principle, affirmed by the Court of Justice, that there should be no distinction between payment and repayment traders. The approach accepted by the FTT had the effect that the latter remained at risk for an unlimited period of having recoverable input tax adjusted down to zero.

24. The correct statutory analysis was as follows:

- The VAT return evidenced a *prima facie* entitlement to be credited by way of repayment.

- Whilst HMRC could dispute and investigate the sum claimed, there was no authority for the proposition that they could do so for an unlimited period of time: they were obliged to act proportionately and to respect relevant statutory time limits.

- If HMRC found some aspect of a return objectionable, they had to follow the statutory requirements, ie make an assessment under section 73 or require the taxpayer to make a correction pursuant to regulation 35 of the VAT Regulations 1995. Both of these powers were subject to time limits.

- There was no statutory power to amend a taxpayer's VAT return and accordingly no legal basis for "reducing" a VAT credit.

25. In the present case it was accepted that HMRC were entitled to investigate the validity of DCM's repayment claims. But that entitlement was subject to the same time limits as applied to assessments. The clock began to tick at the end of the prescribed accounting period. If no decision was made during the three- or four- year time limit (as the case may be) following submission of the return, the matter was closed and repayment had to be made. The returns had not been amended by DCM, and HMRC had no power to amend them.

26. The FTT had further erred in law in accepting HMRC's argument that they had no power to assess where a sum was due *to* the taxpayer. The FTT had failed to appreciate the distinction between amount being due (determined by section 73(1)) and an amount being payable (determined by section 73(9)). Section 73(1) should be interpreted broadly: an amount "due" could either be a net sum due to HMRC or a component of a net sum, such as an excess incorrectly reclaimed. The only way HMRC could "re-write" a return was by way of the statutory assessment mechanism.

27. As a second and separate point, it was submitted that the FTT's analysis had been based on factual misapprehensions outside the range of conclusions properly open to them. This argument was founded upon what was said to be the FTT's misinterpretation of the terms of a letter sent by Officer Boyle to DCM on 28 July 2008. The misinterpretation had led the FTT to incorrect conclusions as to what was in fact being done by Officer Boyle prior to intimation of her decisions to DCM. In our view there is no substance to this point. We are satisfied that the FTT's interpretation of the letter was one that it was entitled to adopt. In any event, the proper interpretation of the letter does not seem to us to make any difference to the point of principle raised by this ground of appeal. The question for the FTT, and for this tribunal, is not what the HMRC officers believed they were doing (about which there was undoubtedly some confusion) but whether as a matter of law they had power to do what they did when they issued the decisions now appealed against.

Argument for HMRC

28. On behalf of HMRC it was submitted that the FTT had been correct to conclude that HMRC were entitled to verify a return before accepting it, and that there was no statutory time limit within which that process had to be undertaken. There was instead a requirement that HMRC act reasonably and proportionately. The fact that VAT is a self-assessed tax did not mean that, irrespective of the outcome of the verification process, HMRC became liable to make payment immediately upon receipt of a repayment return, with the onus being placed upon them to recover any overpayment by means of an assessment under section 73. To treat the submission of a repayment return as creating a debt due immediately to the taxpayer would represent a significant risk to the revenue, and was not in accordance with the analysis in the ECJ case law. The correct approach had been articulated by Lightman J in the *Tradecorp* case. A claim had to be admitted before a *prima facie* right to immediate payment was established. If the claim was refused, a right of appeal was available.

29. The time limits in section 73 did not apply to the investigation of a claim prior to acceptance or rejection of a return. They applied only to assessments, and an assessment could only be made where a sum was due to HMRC. That did not mean that HMRC were immune from judicial scrutiny in the carrying out of the investigation: if they acted unreasonably or disproportionately, the taxpayer's remedy was judicial review. That afforded significant protection for the taxpayer. Where the taxpayer co-operated, the appropriate time for verification would usually be significantly less than the two-year period mentioned in section 73(6). Nor did this analysis give rise to any distinction between payment and repayment traders: HMRC could investigate a payment return before accepting it, but protection of the revenue would often be best achieved by accepting the payment return while carrying out the investigation, with a view to issuing an assessment if HMRC considered that the amount due had been understated. In any event, any difference between payment and repayment traders was objectively justified by the need to promote fiscal neutrality by protection of the revenue, and was not therefore inconsistent with ECJ case law.

Decision

30. In *Garage Molenheide BVBA v Belgium* [1998] STC 126, the Court of Justice ruled that national laws which enabled the tax authorities to retain, as a protective measure, refundable amounts of VAT where *inter alia* there were grounds for suspecting tax evasion, or where a debt was due by the taxpayer, did not contravene the provisions of the Directive concerning the right to deduct. However, in accordance with the principle of proportionality, the measure must not go further than is necessary for the purpose of protection of the revenue. In the light of this authority it is common ground between the parties to the present appeal that HMRC are not bound to make immediate payment of a sum claimed to be due in a repayment return without taking reasonable and proportionate measures to verify that the sum is properly due.

31. The *Garage Molenheide* decision was considered and applied by Lightman J in *R (UK Tradecorp Ltd) v C&E Commrs* (above), in which the Commissioners had delayed making repayments to a trader pending investigation of suspected missing trader intra-community fraud. Lightman J made the following general observations (paragraph 18):

> "The Commissioners are under a duty to conduct a reasonable and proportionate investigation into the validity of claims for a refund and repayment and a duty to act proportionately both in respect of the investigation and in dealing with the taxable person's claims generally… The duty embraces an obligation to keep all investigations under review. The Commissioners are entitled to take a reasonable time to investigate claims prior to authorising deductions and repayments and what is a reasonable time within which to complete an investigation must depend on the particular facts... The availability and proper exercise of the Commissioners' powers of investigation are essential to maintain the fiscal neutrality of VAT and prevent refunds being made to parties not entitled to them. The postponement of repayment of input tax pending the outcome of the investigation is, as a matter of principle and subject to questions of proportionality, entirely compatible with the Sixth Directive. Whilst the burden of proof is upon the taxable person to establish that the investigation of his unadmitted and unadjudicated claim and the failure to make a part or interim payment is unreasonable or disproportionate, the burden is on the Commissioners to justify non-payment of it once the claim is admitted or established… "

Neither party to the present appeal sought to take issue with any of these observations.

32. Lightman J addressed the issue of failure by the taxpayer to respond to requests by the Commissioners for information, as follows (paragraph 24):

> "As it seems to me, the refusal does not obviate the obligation [ie to seek expeditiously to verify the return], but may delay the conclusion of the investigation and may oblige the Commissioners to reject the claim. The Commissioners cannot be criticised for affording time to the taxable person to consider carefully the implications of his refusal to answer (eg that adverse inferences may be drawn) and the other consequences (eg the consequent need on the part of the Commissioners to pursue other inquiries) and the potential impact on the outcome. But the duty of the Commissioners throughout continues to be to process the claim expeditiously."

33. At paragraph 25, Lightman J emphasised that the principle of proportionality required the availability at all times of effective judicial control over the actions of the Commissioners:

> "…The national legal system must afford to a taxable person at all times access to a court which can scrutinise, supervise and monitor the due performance by the Commissioners of their duties, and that embraces scrutiny both of the decisions made and the decision-making process… The Administrative Court's role includes ensuring that the Commissioners in accordance with their duty expeditiously determine the applications for refunds and reach fair and proportionate decisions whether (eg) to proceed with an investigation or whether to make part or interim payment…"

Again, we did not understand either party to this appeal to express any disagreement with these statements of general principle. We note, for the avoidance of doubt, that DCM has not at any time sought judicial review of the inhibit placed upon its repayment claims. The question of whether HMRC acted reasonably and proportionately in delaying and ultimately refusing to meet the repayment claims in full is not the issue before this tribunal for decision. In any event the FTT made a finding in fact that HMRC did act proportionately against a background of non-co-operation and there is no basis upon which we would be entitled to disturb that finding.

34. DCM argues instead that HMRC have no statutory power to "amend" their returns and that the only means provided by statute for HMRC to reduce the amounts reclaimed was by way of assessment, which they failed to do within the time limits in section 73(6) of the 1994 Act. In our opinion the FTT was correct to reject this argument. We accept HMRC's submission that the power to refuse to pay a sum claimed in a repayment return in full is implicit in the taxpayer's entitlement, in section 25(3) of the 1994 Act, to payment of a "VAT credit", ie to the excess of allowable input tax over output tax due from him, which calculation assumes that each component has been correctly calculated, and in HMRC's care and management powers in paragraph 1 of Schedule 11 to the 1994 Act. It is true that there is no statutory power to amend a return, but there is undoubtedly, in our view, a power to decide to refuse to pay a sum claimed in full, and to pay a lesser sum (or nil) instead. Reduction of the net sum reclaimed in the return is merely the arithmetical means of giving effect to the operative decision. If the taxpayer disagrees with the decision to pay a lesser sum, a right of appeal to the FTT is available.

35. We also accept HMRC's argument that there is nothing in the statutory provisions to require the reduction of a sum claimed in a repayment return to be effected by means of an assessment. HMRC's powers to assess are contained in sections 73(1) and (2). Section 73(1) applies where a person has failed to make returns required by the Act or where it appears to the commissioners that such returns are incomplete or incorrect. Section 73(2) applies where a person has been paid or credited with an amount which ought not to have been paid or credited to him. In both subsections the commissioners are given power to assess the amount of VAT *due from him*. In other words, the assessment provisions apply to circumstances in which an amount is due by the taxpayer to HMRC, and there is no provision for assessment in the contrary situation. We find support for this analysis in the judgment of Arden LJ (others concurring) in *BUPA Purchasing Ltd v C&E Commrs* [2008] STC 101 where she said at paragraph 38:

> "Section 73(1) states that an assessment under that section is of 'the amount of VAT due'. Accordingly, unless the assessment determines the net amount of VAT due it cannot be an assessment for the purposes of section 73(1). Similarly, in section 73(6) the assessment is described as an assessment 'of an amount of VAT due'. Thus there cannot be an appeal against an assessment under section 73(1) unless it assesses that there is a net amount of VAT due. If the taxpayer contends that he is entitled to a repayment of VAT, he will have to appeal on some other ground, such as against the

amount of input tax allowed, and VATA makes express provision for this in section 83…"

The point at issue was different, but Arden LJ's analysis clearly proceeds upon the basis that assessments are concerned only with amounts said to be due *to* HMRC. We also accept HMRC's argument, noted above, that this approach does not give rise to any distinction between payment and repayment traders capable of constituting a breach of community law principles.

36. We are not persuaded by DCM's contention that a distinction falls to be drawn between an amount due and an amount payable. Subsections (1) and (9) of section 73 are both concerned with amounts due by a person: the former with their ascertainment and the latter with their recovery. In all of subsections (1), (2) and (9) the references to an amount due are to a net amount produced at the end of a calculation and not to the component elements of that calculation.

37. In our view the FTT was therefore correct to hold that the time bar provisions in section 73(6) had no application to the officers' decisions to reduce the amounts of the repayments claimed, because those provisions apply only to the power to assess. It follows that no formal time limits apply to the power to investigate and decide whether a repayment claim falls to be paid in full. We see no unfairness or absurdity in this. Parliament could have chosen to impose a time limit in circumstances other than assessment but has not done so. Instead, it is settled by the case law to which we have referred that the power to investigate the validity of a repayment return and, consequently, to decline to make immediate payment of the sum claimed, must be exercised reasonably and proportionately, and that it is subject to judicial control. It would be unsatisfactory if, hypothetically, a taxpayer who had made an excessive repayment claim could shield it from investigation by refusing to respond to requests for information, with a view to asserting eventually that it was protected by time bar.

38. For these reasons we hold that the FTT correctly determined that HMRC had power to reduce DCM's repayment claims for the various periods between 07/05 and 12/08 to which appeals 2 to 6 related.

Ground of appeal 2 – the SDC issue

39. This issue, which arises only in relation to appeal 1, is whether the FTT correctly concluded that DCM's receipts before 1 February 2004 did not properly disclose separate charges and accordingly did not comply with the guidance in Information Sheet 08/99. It relates to periods 07/03, 10/03 and 01/04. As it is not being contended that DCM was operating a FCA method, it is accepted by DCM that failure to comply with the guidance regarding SDC would have the consequence that no method compliant with section 19(4) of the 1994 Act was in place at that time.

40. It is a remarkable feature of this aspect of the parties' dispute that at the time of the correspondence in 2003 and 2004 regarding the disclosure requirements of the information sheet, DCM had not supplied HMRC with samples of receipts actually provided to their customers. The FTT noted (paragraph 76) that on 25 November 2003, DCM's advisers PwC sought approval of documents which were described as DCM's sales receipt and order confirmation. It later transpired that these were only proposed samples, and not documents in use. Copies of documents actually in use at the material time were not provided to HMRC until 12 copy documents bearing dates between August 2003 and February 2004, and two further documents bearing dates in February and December 2004, were produced at 5.30 pm on the Friday before the FTT hearing which was due to begin on Monday 26 September 2016. HMRC objected to their late lodging as productions, and the FTT reserved its decision as to whether they should be admitted. DCM subsequently sought leave, on day 4 of the FTT hearing, to lodge a witness statement by Mr Graeme Murdoch, DCM's company secretary, explaining the provenance of the documents, together with the documents themselves. On this basis they were admitted to process.

41. Ten of the 14 documents lodged during the hearing bear dates between 10 October 2003 and 5 February 2004. Although described by the FTT and in parties' submissions as "receipts", they are headed "Order Confirmation". Each document bears the Optical Express logo, DCM's contact details, and its VAT registration number. As noted by the FTT at paragraph 98 of its decision, each carries the following statement for signature by the customer:

> "The separate elements of the total have been explained to me and I accept that the total payable is made up of those separate charges. I agree to the amounts for each supply shown."

As a representative example, an order confirmation dated 6 January 2004 contained the following entries; we have omitted lines with nil charges. The first entry refers to spectacle frames; the second to lenses:

"ORDER CONFIRMATION

Rayban 8502	130.00
Varilux Panamic Airwear 1	269.00
Extras:	
5% Frame Discount	-6.50
£30 Discount	-30.00
Sight Test (Private)	10.00
Discount	-10.00
- - - - - - - - - - - - - - - - - - - -	
TOTAL DUE	362.50

(E) Sight Test	10.00
(E) Services	279.30
(SR) Goods	119.70
(SR) Discount (on goods)	-46.50
- -	
TOTAL DUE	362.50

VAT ANALYSIS
- - - - - - - - - - - - -
Standard Rate (SR)
£73.20 VAT @ 17.5% 10.90
Exempt (E)
£289.30 VAT @ 0.00% 0.00"

By way of arithmetical explanation, the sum of £119.70 brought out for standard rated goods is a calculated figure, being 30% of the total cost (frames + lenses) of £399.00, before application of any discount.

42. The order confirmation documents bearing the dates 12 February and 17 December 2004 differed from the above in that all individual entries, including the entries for frames and lenses, were sub-divided into "product charge (SR)" and "dispensing charge (E)". In each of these documents, the product charge in respect of both frames and lenses was 30% and the dispensing charge 70% of the total for that item. This layout, it will be recalled, was regarded by HMRC as compliant with the guidance in the information sheet.

43. The FTT also found in fact (at paragraph 97) that there was a general notice in DCM's stores which told customers:

> "The total price you pay for spectacles will be made up of separately identified charges for: lenses and frames, dispensing services and eye test (where applicable), you will be given a full breakdown of these charges before you place your order. Your statutory rights are not affected."

The FTT's decision

44. The FTT held that the information provided by DCM before February 2004 was not compliant with the guidance in the information sheet. At paragraph 96 the tribunal observed:

> "It is undoubtedly the case that certainly since at least August 2003, there was a clear distinction on the receipts between supplies which carried VAT and those that did not. Whilst we can do the arithmetic to see how those figures are derived, firstly, it is not blindingly obvious on the face of the receipt, and, secondly, there is no reference whatsoever to 'dispensing'. The customer would simply know that goods were standard rated and services were not."

At paragraph 99 the FTT expressed the view, in relation to order confirmations in the above form, that "…it is [not] possible to identify the dispensing since the figure for 'services' does not directly relate to the items in the order". The tribunal concluded (paragraph 155):

> "As can be seen from the receipts, dispensing was not identified before the retrospective implementation date of 1 February 2004. Although the earlier receipts do make clear the different charges for an exempt supply and a taxable supply, Annex B of 08/99 makes it clear that **all** patients must be able to identify the dispensing charge. In our view all that a customer would have known was that they did not have to pay VAT on every part of the bill."

The FTT accordingly found that 1 February 2004 was the date from which DCM had implemented a SDC method compliant with the guidance in the information sheet.

Argument for DCM

45. On behalf of DCM it was argued that the FTT had erred in law in holding that the pre-February 2004 documents did not meet the criteria of a SDC method. The information provided to customers at the time of supply was sufficient to make known to them the separate charges that they were paying for the taxable supply of goods on the one hand and the exempt supply of dispensing on the other. The information sheet made clear that there was no particular method by which the separate charges had to be made known. It would be disproportionate to demand the express use of the word "dispensing" as a necessary requirement (cf *CR Smith Glaziers (Dunfermline) Ltd v C&E Commrs* [2003] STC 419 (HL), paragraph 25).

46. The FTT had found (paragraph 155, quoted above) that a clear distinction had been made between supplies carrying VAT and those which did not. Whether the arithmetic was "blindingly obvious" or not was not the test: it set the bar too high. Its view that dispensing could not be identified failed to recognise that references to services were equivalent to references to dispensing. If the FTT had taken the view that the word "dispensing" had to appear, that too would have been an error of law.

Argument for HMRC

47. On behalf of HMRC it was submitted that the FTT had been entitled to conclude that it was not possible to determine, at the time of the contract, what consideration had been agreed between DCM and its customer. The "receipts" did not constitute the contract. The issue was one of substance, not form. Although it was not essential for the word "dispensing" to be used, the customer had to be told what the consideration was for the supply of dispensing. The documents produced did not provide the customer with the amount of dispensing charges for either frames or lenses. The FTT had held that the order confirmations did not provide evidence of the parties' agreement, and in any event that the position on the face of the documents was unclear. Those findings should not be disturbed.

Decision

48. Looking at the "order confirmation" alone, the customer was told (i) the total price of the frames; (ii) the total price of the lenses; and (iii) the total amounts chargeable on services and on goods. The customer could not tell from the order confirmation alone that "services" meant dispensing, but we did not understand HMRC to suggest that there was any other candidate. The customer was not told how much of (i) or (ii) was attributable to services, but we are not convinced that this matters. The guidance in the information sheet does not require separate figures for lenses and frames. We note in any event that in the post-February 2004 documents the separate figures consisted of exactly the same 30%/70% split, and it is difficult to see that this added anything of real substance.

49. It is also important to note that the information in the order confirmation did not stand alone. The FTT found in fact that a general notice in DCM's stores told customers that they would be given a breakdown of charges for lenses and frames, dispensing services and eye test (where applicable). This appears to us to be a clear and unequivocal reference to, and description of, the lower part of the order confirmation, where "services" can only therefore equate to dispensing services. Taking the terms of the order confirmation together with the general notice, there could in our view be no room for doubt in the mind of a customer that the charge for dispensing was the amount stated in the order confirmation as the charge for "services". Nor do we consider that there is any issue regarding the time at which the order confirmation was provided. The information sheet requires the separate charges to be made known "at the time of the supply": in our opinion the order confirmation documents afford clear evidence of what was made known at that time.

50. For these reasons we are of the opinion that on the basis of the FTT's findings in fact in paragraphs 96, 97 and 98, the conclusion that the tribunal reached that it was not possible to identify the amount charged for "dispensing" is not supportable. Applying the analysis in *Advocate General for Scotland v Murray Group Holdings Ltd* 2016 SC 201 of the right of appeal to the Upper Tribunal on point of law, we consider that the FTT's conclusion is one "for which there is no evidence or which is inconsistent with the evidence and contradictory of it" (*ibid*, para 43, quoting from *IR Commrs v Fraser* 1942 SC 493, Lord President Normand at 497). We hold, on the basis of the FTT's primary findings in fact, that the information provided by DCM to customers during the periods in issue immediately prior to February 2004 did meet the guidance in Information Sheet 08/99 and accordingly, in that regard, that a SDC method falling within the guidance was being operated. It is most regrettable, to say the least, that appropriate evidence of this was not provided by DCM to HMRC until the eve of the tribunal hearing.

Ground of appeal 3 – the discounts issue

51. The discounts issue is to some extent bound up with the SDC issue, in that they are both concerned with allocation of the consideration paid by DCM's customers as between taxable supplies of goods and exempt supplies of services. This issue is, however, a live one in relation to all of the appeals except appeal 4. That means that it subsisted throughout a much longer period of time than the SDC issue.

52. We have already noted that the FTT found that DCM failed over many years to provide data requested by HMRC to enable the latter to reach a view as to the attribution of discounts. Eventually, on 11 December 2008, HMRC received what the FTT described as "four bundles of raw data for period 10/05". In DCM's covering letter sent with this material it was stated that the information was submitted without prejudice and did not constitute "our acceptance that discounts should be split in accordance with the taxable and exempt supply". On 15 January 2009, Officer Boyle requested data for various other periods (which was not provided). She also indicated that, on the basis of the information received on discounts, there had been a potential under-declaration of output tax. She subsequently sent the letters containing the decisions which we have already discussed in relation to the first ground of appeal. These were issued on the basis of her best judgment, using the data supplied for period 10/05. Although the FTT did not find so in terms, we take from the above that Officer Boyle's calculations proceeded on the basis of a pro rata attribution of discounts as between taxable and exempt supplies.

The FTT's decision

53. The FTT accepted evidence from Mr Murdoch that there were seasonal variations with differing promotions, but noted that neither it nor HMRC knew whether the period 10/05 had more or less discounts than in other periods. The tribunal commented that the fact that DCM's computing systems made it difficult to access data to support arguments on discounts was not HMRC's problem. While noting Mr Murdoch's unchallenged assertion that discounted healthcare was not an attractive marketing message, the tribunal did not accept that this was a sufficient basis for attributing all discounts to goods, especially as "DCM offered discounted sight tests".

54. The FTT's conclusion regarding discounts is set out in the following paragraphs of its decision:

> "169. DCM certainly have a problem with the discounts before the implementation of SDC in that, as we can see from the receipts, the customer certainly thought that the transaction involved free eye tests, albeit if the customer analysed the VAT part of the receipt that was not reflected there. We have no information as to the detail of the transactions thereafter other than in regard to DCM's VAT treatment of discounts.
>
> 170. We agree with Officer Boyle's point that if DCM establish that a discount is wholly attributable to goods then that should be the VAT treatment. That has not happened historically.

171. Unfortunately, the only information available is that furnished for 10/05. That may not be a typical period, if there is such a thing, but it is the only information that DCM have chosen to provide.

172. In our view, the words 'properly attributable' in Section 19(4) VATA imply an objective test which is appropriate, fair and reasonable. We do not think that the attribution of all discounts to goods, particularly goods intrinsically linked to the dispensing services and sight tests, is appropriate. It is arbitrary and falls clearly into the circumstances envisaged in *C R Smith.* The reality is that a free sight test is just that, as is a 2 for 1 offer.

173. We find therefore that the approach adopted by HMRC following the submission of the 10/05 data is a proper attribution in terms of the legislation and is to best judgment."

Argument for DCM

55. On behalf of DCM it was argued that the FTT had erred in law by applying an objective rather a subjective test in determining how the discount ought to be allocated. VAT fell to be applied to the transaction that was made, not to one that could have been made but was not. DCM was free to allocate the discount as it saw fit; there was no allegation of abuse. The order confirmations provided clear evidence of the allocation of the discounts by DCM as between taxable supplies of goods and exempt supplies of services, and demonstrated that they had been applied to the former. There was no legal basis to disturb that allocation. Reference was made to the speech of Lord Walker in *Lex Services plc v C&E Commrs* [2004] STC 73 at paragraphs 18-23.

56. The FTT decision contained no analysis of the situation on the face of the documents produced. No rationale was provided for the conclusion at paragraph 172 that attribution of all discounts to goods was not "appropriate". The decision was an expression of policy, ie what the FTT thought DCM ought to have done. In adopting this approach the FTT had misunderstood its function and erred in law.

Argument for HMRC

57. On behalf of HMRC it was submitted that the FTT's decision had not turned on whether the order confirmations properly reflected the attribution of discounts between exempt and taxable supplies. Rather it turned on whether DCM had proved either that HMRC's approach to apportionment was not appropriate or that the decisions had not been made to best judgment. Throughout the period before and during the appeal to the FTT, DCM had failed to provide evidence in support of the returns it had submitted. The FTT had been entitled to reject the proposition that Mr Murdoch's evidence was sufficient to establish that all discounts had been attributed to goods and that its returns accurately reflected the discounts given.

58. HMRC had always accepted that if DCM and its customer agreed, prior to entering into a transaction, that a discount was to apply in a particular way, then the VAT treatment

would follow that agreement. If, however, the discount was offered against the whole package, the discount was properly attributable to the whole package and fell to be apportioned accordingly. When DCM supplied data for period 10/05, HMRC used it to re-calculate the output tax payable in respect of the various returns outstanding, using the proportion agreed when settling litigation in relation to earlier periods. In the absence of other evidence, this was an appropriate methodology to adopt.

Decision

59. In *Staatssecretaris Van Financiën v Cooperatiëve Aardappelenbewaarplaats GA* [1981] ECR 445 (the *Dutch Potato case*), the Court of Justice stated that the consideration for a supply was a "subjective value" and not a value assessed according to objective criteria. The expression "subjective value" is to be interpreted as meaning the value which the parties to the contract have themselves recognised in the course of their dealings: *Lex Services plc v C&E Commrs* (above), Lord Walker at paragraph 19. The *Dutch Potato case* and *Lex Services* were both concerned with non-monetary consideration, but it is clear from Lord Walker's observations in the latter case at paragraph 18 that he similarly regarded the concept of "subjective apportionment" as achieving legal certainty and ease of administration of the VAT system. Where, therefore, the parties have agreed an apportionment of consideration as between a taxable element and an exempt element, that apportionment will, except in cases of abuse, be conclusive for VAT purposes. None of this is controversial.

60. Whatever may have been their position in correspondence with HMRC over a period of many years, DCM now found their case squarely upon the treatment of discounts in the order confirmations which, as we have already noted, were lodged in the course of the FTT hearing and had never previously been made available to HMRC. In the representative sample that we set out at paragraph 41 above, it will be noted that there were three separate discounts amounting to £46.50 in total, all of which were allocated in the VAT analysis to the taxable supply of goods and described collectively as a "discount (on goods)".

61. Despite the very late stage at which they were produced, the order confirmations were ultimately admitted as evidence and it was incumbent upon the FTT to take them into account, rather than, for example, simply reviewing whether HMRC's approach was reasonable in the light of information available to them at the time when the decisions under appeal were made. There remains, however, a question as to how far the order confirmations take DCM's argument. Their format varied, even over the relatively short period during 2003 and 2004 from which they date, and none fell within any of the periods of account to which appeals 2 to 6 relate.

62. The only reference in the FTT's reasoning to the order confirmations now relied upon by DCM is in paragraph 169, quoted above. The FTT stated that it had no information as to the detail of transactions thereafter (ie after implementation of SDC in February 2004)

other than in regard to DCM's VAT treatment of discounts. We understand the FTT to mean by this that although the order confirmations showed how discounts had been treated by DCM for VAT purposes, they did not of themselves constitute evidence that that treatment had been correct.

63. The FTT did not assemble in one place its findings in fact in relation to discounts. We can however identify the following relevant findings (references are to paragraph numbers in the FTT decision):

    - DCM always had ongoing promotions on its optical products, eg 2 for 1 spectacles and money-off vouchers, but not all sales would have been discounted (90).
    - DCM's computer systems were not set up to identify discount information (90).
    - In the earliest example of a receipt, dated 2 August 2003, there is no indication of the allocation of the discount from the pre-promotion price (95).
    - A customer who had a sight test would have thought that that had been discounted (100).
    - HMRC eventually received data for period 10/05 on 11 December 2008. Despite repeated requests no data were provided for any other periods since 04/04 (107, 108).
    - DCM offered discounted sight tests (165).
    - The customer thought the transaction involved free eye tests (169).
    - A free eye test is just that (172).

64. We consider that there is force in some of the criticisms made by DCM of the discussion in the FTT's decision. At paragraph 164, the FTT stated that it had difficulty with the argument that if an allocation was agreed with a customer then that dictated the VAT treatment. On one reading, paragraph 172, set out above, might suggest that the FTT considered that an objective test should be applied generally in attributing discounts in a fair and reasonable manner. Such an approach would, in the light of the authorities, constitute an error of law.

65. In the end, however, it does not appear to us that the FTT reached the conclusion it did because it misunderstood the law in relation to use of the parties' subjective apportionment for VAT purposes. The tribunal expressly agreed (at paragraph 170) with Officer Boyle's acceptance that if DCM established that a discount was wholly attributable to goods then that should be the VAT treatment. But the tribunal clearly did not accept that the order confirmations produced during the hearing afforded persuasive evidence of the terms of the parties' agreement. We have noted the express findings of fact that, contrary to what the order confirmations might suggest, VAT-exempt eye tests

were free and must therefore have been discounted. It was noted that in the August 2003 documents, no allocation was made of the discount from full price. In short, the FTT concluded that DCM had failed to prove that throughout the period at issue in appeals 1 to 6, the contractual arrangements which it entered into with its customers provided for all of the discounts to be applied only to goods. Having so concluded, the FTT did not, in our view, err in law in holding that HMRC had been entitled to proceed on the basis that a pro rata apportionment, applying the data supplied for period 10/05 and the percentages used in the settlement agreement for earlier periods of account, constituted a proper attribution for the purposes of section 19(4). We accordingly find no reason to interfere with the decision of the FTT on this ground of appeal.

Ground of appeal 4 – the time bar issue

66. This ground of appeal relates only to appeal 1 and concerns the four periods of account between 10/02 and 07/03. These are the only periods which included an output tax element in the assessment and ended more than one year before the contested assessments were made in October 2005. The first three periods were covered by the settlement agreement reached between the parties in May 2003. So far as these periods were concerned, the agreement provided that "[DCM] will voluntarily disclose any output tax underdeclared on the basis that 36% of the consideration received … relates to a taxable supply". At that time the return for period 07/03 was still in the future.

67. After the conclusion of the 2003 agreement, correspondence continued between HMRC and DCM's advisers, PwC. HMRC's Officer O'Pray was not satisfied that DCM's proposed form of order confirmation satisfied the requirements of the guidance in the information sheet for a SDC method. At a meeting on 29 January 2004, Officer O'Pray's position, as recorded in his note of the meeting, was:

    - that DCM's existing method of disclosure was not acceptable (although a method being put forward now appeared to be);
    - that until a SDC method was agreed, DCM were obliged to use a FCA method.

    The meeting, according to Officer O'Pray's note, "ended in deadlock over this issue". There is nothing in his note to indicate that there was any discussion of the percentage split produced by the method being operated by DCM.

68. The correspondence continued. By letter of 27 February 2004, PwC provided HMRC with a copy of a revised order confirmation which it was said was given to each customer along with a copy of the sales receipt, and sought confirmation that "with these slight changes to our client's Point of Sale disclosures, your department is comfortable with the slightly revised procedures". PwC also informed HMRC that DCM "intended to make" charges at the rate of 30% for the taxable elements and 70% for the exempt dispensing

service. For the next few months the attention of both HMRC and PwC focused on the detail of the order confirmations in use going forward. The dispute regarding the method of disclosure of charges in place prior to 1 February 2004 did not surface again until, in a letter dated 19 August 2004, PwC noted, following a discussion at their office, that Officer O'Pray would write to confirm the reason he felt that POS (ie SDC) disclosure was not properly in place prior to 1 February 2004.

69. No further reference was made in correspondence to the period prior to 1 February 2004 until after a meeting on 31 August 2005, at which HMRC were given copies of DCM's VAT account containing details of the calculation of output and input tax. The account showed that the percentage of output tax treated as taxable had been 38% in period 10/02 and 30% in each of the following three periods. In a letter dated 7 September 2005, Officer Boyle stated that HMRC did not consider that a suitable system had been in place until 1 February 2004, when "a system, which was broadly acceptable subject to further refinements," had been agreed. Officer Boyle's view was that best judgment required the 64/36 split agreed in 2003 for periods earlier than 10/02 to be applied to the periods in dispute.

70. On 20 October 2005, Officer Boyle issued assessments for a number of periods including 10/02, 01/03, 04/03 and 07/03. As well as seeking to recover output tax calculated on the basis of a 64/36 split, each of the assessments included an input tax element. PwC, on behalf of DCM, requested a reconsideration of both elements. In relation to output tax, PwC reiterated their contention that the methodology used before February 2004 had been a compliant SDC method. By letter dated 25 January 2006, HMRC declined to amend the assessments. As regards output tax, the letter stated:

> "It is a matter of fact that Mr O'Pray raised a number of concerns with your client regarding their attempts to implement an SDC method, particularly in relation to the means of disclosure adopted. These issues concerning disclosure were not finally resolved until 22 April 2005, at which time Moira Boyle exceptionally agreed to allow retrospective implementation with effect from 1 February 2004…
>
> The Commissioners do not agree that an acceptable alternative to Full Cost Apportionment had been in operation prior to that date. In the absence of such an alternative method, the Commissioners have relied on the agreed apportionment which was previously in place, that is 64% exempt and 36% taxable and the assessment was calculated on that basis."

71. In the present proceedings, DCM contend that, so far as these four periods are concerned, the assessments issued on 20 October 2005 were out of time in terms of section 73(6) of the 1994 Act, having been made more than one year after evidence of facts, sufficient in the opinion of the Commissioners to justify the making of the assessment, had come to their knowledge.

The FTT's decision

72. The FTT found itself "wholly unable to see any material fact which was known to HMRC prior to 31 August 2005 which would have justified making the assessment earlier". The tribunal accordingly found that the assessments made on 20 October 2005 were in time. In reaching this conclusion, the FTT took account of information obtained by Officer Boyle both in relation to input tax and output tax. With regard to the former, the FTT (at paragraph 187) "accepted Officer Boyle's clear explanation that before the visit it would have been impossible for HMRC to work out from the VAT returns that DCM were not using the standard method", contrary to what they had been told. At paragraph 190 the FTT observed:

> "Although this appeal deals only with output tax we have referred to the 'discoveries' in regard to both input and output tax because, as [counsel for HMRC] correctly argued, the assessment includes both and the issue for the Tribunal in the context of time bar is whether Officer Boyle was justified in making the assessment."

The FTT further stated (paragraph 191):

> "Officer Boyle was very clear that it was the information uncovered at the visit which enabled, and caused, her to calculate the figures underpinning the assessment. We accept that."

73. The FTT then addressed output tax, noting firstly that HMRC would reasonably have expected that DCM would adhere to the terms of the 2003 settlement agreement, and secondly that DCM were repeatedly told that in the absence of an agreed SDC method, FCA would have to be in place, which it was not. The tribunal rejected an argument that it should have been obvious to HMRC from DCM's returns and voluntary disclosures that DCM was not using the agreed 64/36 percentage split. It found, in relation to periods 10/02 to 04/03, that DCM had failed to implement its obligation to disclose any under-declarations that arose using that split. It concluded (paragraph 199) that Officer Boyle acted appropriately and quickly and that HMRC were not perverse in not raising an assessment earlier.

Argument for DCM

74. On behalf of DCM it was submitted that for the assessments to have been in time, HMRC had to identify facts that had come to their knowledge during the year ending on 20 October 2005. Since 29 January 2004 at the latest, HMRC had been aware that DCM was operating a point of sale system which, in HMRC's view, did not fulfil the description in the information sheet of a SDC method. No further relevant facts came to light thereafter. The assessment had been based on matters all of which were within HMRC's knowledge long before 20 October 2004. It was apparent from the correspondence that the percentage splits that were found to have been used by DCM were not a factor regarded by HMRC as material to the decision to assess.

Argument for HMRC

75. For HMRC, it was submitted that DCM's argument wrongly assumed that only facts relating to the output tax element were relevant to the question of time bar. There was no authority for that proposition; the converse was correct. The "assessment" for each period was the net position brought out after taking into account all input and output tax elements. It followed that facts coming to the commissioners' knowledge in relation to an input tax overclaim could open up an unconnected output tax under-declaration in the same period, even if the latter would, on its own, have been time barred.

76. In any event, taking output tax on its own, there was no reason to interfere with the FTT's finding that HMRC did not become aware of the last piece of the puzzle until the meeting on 31 August 2005 when they obtained the VAT account disclosing the percentage splits actually used in the periods in question. There was an express finding in fact that it was that information which enabled Officer Boyle to make the assessments. It was not appropriate to look only at the earlier correspondence with Officer O'Pray.

Decision

77. So far as material, section 73(6) provides as follows:

> "An assessment under subsection (1), (2) or (3) above of an amount of VAT due for any prescribed accounting period must be made within the time limits provided for in section 77 and shall not be made after the later of the following:
> …
>
> (b) one year after evidence of facts, sufficient in the opinion of the Commissioners to justify the making of the assessment, comes to their knowledge…"

78. It was common ground that section 73(6) should be construed in accordance with the observations of the Court of Appeal in *Pegasus Birds Ltd v C&E Commrs* [2000] STC 91. Aldous LJ stated (paragraph 15):

> "An opinion as to what evidence justifies an assessment requires judgment and in that sense is subjective; but the existence of the opinion is a fact. From that it is possible to ascertain what was the evidence of facts which was thought to justify the making of the assessment. Once that evidence has been ascertained, then the date when the last piece of the puzzle fell into place can be ascertained."

HMRC referred also to the statement by Sir Douglas Frank QC (sitting as a deputy judge) in *Cumbrae Properties (1963) Ltd v C&E Commrs* [1981] STC 799 at 805 that "the tribunal cannot substitute its own view of what facts justify the making of an assessment but can only decide when the last of those facts was communicated or came to the knowledge of the officer". Senior counsel for DCM sought to persuade us, under reference to more recent authorities, that the Upper Tribunal was entitled to apply a degree of value judgment as to what facts should or should not be regarded as critical; we are not, however, convinced that such a course is open to us.

79. Against that background, we address firstly the general question of whether facts coming to the knowledge of the commissioners in relation to a particular period regarding input tax permits them to make an assessment to recover under-declared output tax in the same period where, if the output tax issue stood alone, the assessment would be time barred. In our opinion it does not. The argument for HMRC was founded upon the proposition that an assessment is a unitary demand for tax, so that the reference in section 73(6) to "the assessment" is to the particular total or net amount brought out at the end of the calculation as due by the taxpayer. In our opinion this proposition is unsound. It is inconsistent with the terms of section 73(4) which states as follows:

> "Where a person is assessed under subsections (1) and (2) above in respect of the same prescribed accounting period the assessments may be combined and notified to him as one assessment."

It is apparent from this provision that the word "assessment" can be used, according to context, to mean either a component part of an overall assessment or, alternatively, the aggregation which produces the total or net amount due for a particular period. In any event, it could not, in our view, be said as a matter of ordinary language that evidence of facts coming to the knowledge of the commissioners in relation to one matter can be utilised to justify the whole of an assessment that also seeks to recover VAT due as a consequence of another or other matters to which those facts have no relevance. Indeed, we would regard it as a somewhat startling proposition.

80. Senior counsel for HMRC sought to derive support from the analysis by Arden LJ in *BUPA Purchasing Ltd v C&E Commrs* (above) of the meaning of the term "assessment". That judgment is, however, concerned with different matters, including in particular whether an assessment must be for an amount of VAT due, and whether an assessment includes the underlying reasoning. It does not provide relevant guidance in relation to the point arising in the present proceedings.

81. We therefore conclude that the FTT erred in law in treating facts coming to HMRC's knowledge in relation to input tax as relevant to the question whether the assessment in so far as relating to underdeclared output tax was out of time. We turn therefore to consider whether the FTT's findings relating to output tax entitled it to conclude that the assessment was in time. Again it is helpful to draw together the findings in fact made by the tribunal:

- No voluntary disclosures were ever made in relation to output tax (70).
- HMRC considered that SDC was not in operation as at 27 October 2003 (75)
- At the meeting on 31 August 2005, Officers Boyle and O'Pray were given copies of the VAT account which disclosed the output tax percentages used for all periods from 7/02 onwards. For the four periods subject to the assessments under appeal, the percentages were 38, 30, 30 and 30 respectively (82).

- DCM was immediately told that as approval for SDC had not been in place, periods 7/03 to 1/04 would have to be recalculated (83).
- The following day the officers noted that the 2003 settlement had not been honoured (84).
- It was the information uncovered at the August visit that enabled and caused Officer Boyle to calculate the figures underpinning the assessment (191).
- After 2003 DCM was repeatedly told that in the absence of an agreed SDC, FCA would have to be in place. It was not, but HMRC could not have known what DCM was doing without seeing their records (192).

82. The fact that DCM was not operating a FCA method did not come as news to the officers at the August 2005 meeting. DCM had never represented that it was in use and HMRC had never proceeded on the basis that it was. As at January 2004, Officer O'Pray had been aware that DCM was not operating a FCA method. He was further aware that DCM was not yet operating a SDC method that was acceptable to HMRC, and that the method that DCM was operating went back prior to period 07/03. The only new information obtained in August 2005 was the percentage splits used by DCM to calculate taxable outputs for the periods from 10/02 onwards.

83. What, then, was the last piece of the puzzle that rendered the evidence sufficient, in the opinion of the commissioners, to justify the making of the assessment? The FTT found in fact that it was the information uncovered at the August 2005 visit that enabled, and caused, Officer Boyle to calculate the figures underpinning the assessment. That, however, is not a conclusive answer to the statutory question. We have already noted that, in our view, the FTT erred in regarding information obtained in relation to input tax as relevant to whether the assessment was in time as regards output tax. The FTT's finding in fact does not distinguish between the two. It is clear, moreover, that calculation of the output tax underdeclaration did *not* depend upon figures obtained at the August 2005 meeting. This calculation consisted of the difference between (a) the amounts which had been declared by DCM in its VAT returns, and (b) the amount of output tax due on the basis of the 64/36 percentage split which Officer Boyle applied, in exercise of best judgment, because that had been the split agreed for earlier periods. The fact that different percentages had in fact been used by DCM was not therefore material to the calculation of the amount of output tax due.

84. The contemporaneous correspondence (Officer Boyle's letter of 7 September 2005 and the reconsideration letter of 25 January 2006) indicates unequivocally that what prompted the assessment so far as output tax was concerned was the fact that HMRC had never accepted that SDC was being correctly operated prior to 1 February 2004. That fact was known to HMRC by at least January 2004. The assessment made by Officer Boyle in October 2005 could have been made at any time thereafter; on the basis of the correspondence and the FTT's findings, no further evidence of relevant facts came to the

commissioners' knowledge. It follows, in our opinion, that the last piece of the puzzle which was thought to justify the assessment as regards output tax was in place more than one year before October 2005. The assessment was therefore out of time in relation to the periods in issue.

Summary

85. We summarise our conclusions as follows:

(i) In relation to Ground of Appeal 1 (the amendment issue), the appeal is refused.

(ii) In relation to Ground of Appeal 2 (the SDC issue), the appeal is allowed.

(iii) In relation to Ground of Appeal 3 (the discounts issue), the appeal is refused.

(iv) In relation to Ground of Appeal 4 (the time bar issue), the appeal is allowed.

Parties were agreed at the conclusion of the appeal that our decision in principle on each of these four issues should enable them to work out the practical consequences as regards the assessments and decisions appealed against. It is however open to parties to seek further directions from this Tribunal should that prove to be necessary.

86. We are grateful to all counsel for their very full and helpful written and oral arguments.

LORD TYRE
JUDGE DEAN

Release Date: 5 December 2018