



VAT Voice[®]

The bi-monthly newsletter of VAT Advisers Limited

May/June 2010

Inside this issue...

1. Latest VAT news
2. In focus
3. VAT cases
4. VAT Tips

HMRC NOW REQUIRES DISPUTED VAT TO BE PAID WHERE IT WINS CASE AND TAXPAYER LODGES AN APPEAL

In March, the HMRC website announced a new policy to increase the consistency of tax collection in cases where a Tribunal or court has found **against** a taxpayer, but there is a further appeal.

Currently, in the event of a taxpayer win, HMRC repays overpaid taxes before the appeal is heard in the higher court. However, on decisions in HMRC's favour, it does not consistently collect the tax before the appeal. The new policy requires prepayment of tax in all cases, and applies to Tribunal or court decisions made from 1 April 2010.

Specifically for VAT and other indirect tax appeals, HMRC say taxpayers may apply for the tax to be set aside if they will suffer hardship by being forced to pay the tax before the appeal. Also, HMRC says it will not enforce payment where it would lead to the bankruptcy or liquidation of the taxpayer.

COA SAYS ONLINE INSURANCE INTRODUCTIONS ARE EXEMPT INTERMEDIARY SERVICES

On 22 April 2010, the Court of Appeal released its decision in the joined cases of *InsuranceWide.com Services Ltd* and *Trader Media Group Ltd*, which concerned the scope of the insurance intermediary exemption. The Court found unanimously for the taxpayers.

Both companies provided online introductory services between people seeking insurance and a panel of insurers. Customers were attracted to the companies' websites because of their reputation in the market as facilitators for the obtaining of insurance. The High Court had previously found for the taxpayers, confirming that both qualified as insurance brokers/agents for the purpose of the VAT exemption, and that the services they rendered were not merely advertising services.

At the CoA, HMRC argued that neither company was acting as an insurance broker or insurance agent, but merely providing a 'click through' facility. HMRC urged the CoA to make a referral to the ECJ, but it rejected this along with all of HMRC's other submissions. The Court held that:

- Exemption is not dependent on whether a business describes itself as an insurance agent or broker. The critical point is what they **do**
- Insurance regulatory definitions should only be used for VAT purposes to the extent that they reflect legal realities and practice
- The essential characteristics of an insurance broker or agent are that they put insurers in touch with potential clients, or act as intermediaries between insurers and clients/potential clients
- Exemption does not require a person to be carrying out all the functions of an insurance agent or broker
- The relevant UK law was clear, so an ECJ referral was not needed

As the Court outlined a number of principles on the issues, the case is likely to be referred to repeatedly in resolving liability in future. Upon applying those principles to the facts in the joined cases, the CoA had no trouble in finding that the supplies were exempt. In moving away from regulatory definitions, the Court's decision hopefully ensures that future interpretation of the exemption keeps pace with commercial developments in the modern insurance world. Notably, the Judges acknowledged that the application of the exemption is highly fact-dependent. Both companies were seen to provide much more than a mere 'click through' service, with specific note taken of their involvement in selecting the most appropriate insurer for potential clients (using pricing, products, and customer service).

HMRC has apparently sought permission to appeal to the Supreme Court. However, the confidence and unanimity of the Court's decision suggests it will be refused, and as an ECJ referral also looks blocked, the litigation may well end here. This would be great news for those cases which have been stood behind this appeal. If a business has charged VAT on similar services, but has not yet made a claim, it should consider doing one now.



Latest VAT News

REVENUE & CUSTOMS BRIEF 08/10

VAT – Land and Buildings - Changes to the operation of the option to tax and updated definitions of housing associations

Details of the three 1 April 2010 changes to Schedule 10 VATA 1994, which covers the liability of supplies of land and buildings, and one change to Group 5 Schedule 8 VATA 1994, which covers the zero-rate for construction services.

The Brief explains the reasons for the changes, advising that, following the introduction of the rewritten Schedule 10 on 1 June 2008, HMRC continued discussions with business on ways in which the legislation could be further improved and simplified. During these discussions, other concerns were identified on certain aspects of the option to tax rules which have led to a small number of minor amendments being made that are intended to both simplify the legislation and facilitate business needs. A further change is also necessary as a result of the Housing and Regeneration Act 2008, and the redefining of the term 'relevant housing association'. HMRC say the changes balance the business need for flexibility with the requirement that revenue should be protected.

Details of the three changes are as follows:

- occupation of minor parts of buildings (no more than 10% of the total area) by persons that 'provided finance' for developments is now disregarded for the purposes of the option to tax anti-avoidance provision. A new sub-para 15(3A) has been introduced in Sch 10 (see *Annex A of VAT Info Sheet 02/10*)
- the conditions for revoking an option to tax during the 'cooling-off' period have been amended. The requirement that the land must not have been used has been removed (Sch 10 para 23(1)(b)). (see *Annex B of VAT Info Sheet 02/10*)
- the legal definition of 'relevant housing association' has been amended in Sch 10 para 10(3). The term 'registered social landlord' will be replaced from 1 April in England only with 'private provider of social housing' as defined by the Housing and Regeneration Act 2008. This change ensures English housing associations continue to enjoy the same VAT reliefs as they do at present in common with housing associations in the rest of the UK. A similar change is also being made in Group 5 to Sch 8 VATA 1994 with an opportunity to update the reference for Scotland as well.

HMRC say a revised Public Notice 742A will be issued in due course.

REVENUE & CUSTOMS BRIEF 09/10

Announcement of revised HMRC policy on the supply of education by a university subsidiary trading company (VAT Info Sheet 03/10 provides further detail).

HMRC say that following recent developments in case law and methods by which universities deliver education, it has reviewed its policy on supplies of education by companies owned or controlled by a university. The review has identified a need for policy change, and as a result, the liability of supplies of education will change in certain circumstances. The new policy applies to supplies made from the date of the Brief subject to transitional provisions.

Following the review, HMRC concluded that where a university trading company provides education, it is usually acting as a 'college, institution, school or hall of a university.' As such, it is an 'eligible body' for the purposes of Group 6 Sch 9 VATA 1994, which means that any education or training provided by the university subsidiary trading company is an exempt supply of education.

Latest VAT News (continued 1)

HMRC say the policy change is limited to those companies that are:

- owned/controlled by a university
- provide university level education leading to a qualification awarded by a university or a nationally recognised body
- have close academic links with their parent university (e.g. where students on the company's courses are registered or enrolled with the parent university, subject to its rules and regulations, and awarded qualifications by it)

Although the new policy will make educational and vocational training supplies exempt, other supplies, particularly consultancy services, will remain standard-rated.

Affected companies may apply the new policy with retrospective effect, and make the relevant adjustments to its VAT accounting. However, as they will have budgeted on the basis that their supplies are taxable, affected companies may also continue to apply the old policy to supplies which are to be delivered before 1 August 2010.

Where a tax point is created for courses to be delivered both before and after 1 August 2010, only the element to be delivered before 1 August 2010 is subject to previous policy.

REVENUE & CUSTOMS BRIEF 10/10

VAT: Partial Exemption – changes to the de minimis rules

Details of two changes intended to simplify the partial exemption de minimis effective from 1 April 2010.

The changes are being made following a consultation on ideas to simplify the partial exemption rules. They are optional, and do not need HMRC's prior approval to be used. Under the changes, the de minimis limit remains the same but it is easier and less time-consuming for businesses to confirm de minimis status.

Simplified Tests

The first change is a simplified de minimis calculation comprising two tests as follows:

Test one: total input tax is no more than £625 per month on average, and the value of exempt supplies is no more than 50% of the value of all supplies

Test two: total input tax less input tax directly attributable to taxable supplies is no more than £625 per month on average, and the value of exempt supplies is no more than 50% of the value of all supplies

If, in a VAT period, a business passes either test, it may treat itself as de minimis and provisionally recover input tax relating to exempt supplies. There is no need to carry out a full partial exemption calculation in the period. However, the business must still carry out an annual adjustment at the tax year-end, and account for any under/over recovered input tax as normal.

HMRC say '*total input tax*' excludes blocked input tax (such as on business entertainment), and that '*value of all supplies*' includes taxable supplies made in the UK, supplies made outside the UK that have a right of input tax recovery (known as 'Reg 103 supplies') and exempt supplies. The term '*input tax directly attributable to taxable supplies*' is input tax on costs that are used or to be used exclusively in making taxable supplies.

Annual Test

The annual test gives the option of applying the de minimis test once a year, instead of four or five times a year (depending on when a business does its annual adjustment). It allows a business that was de minimis in its previous partial exemption year to treat itself as de minimis in its current partial exemption year. This means it can provisionally recover input tax relating to exempt supplies in each VAT period, saving the need for partial exemption calculations.

Latest VAT News (continued 2)

Businesses must still review their de minimis status at the year-end, and if the de minimis test for the year is failed, the input tax relating to exempt supplies that was provisionally recovered in-year must be repaid. However, there is no need carry out in-year partial exemption calculations.

The annual test has three conditions as follows:

- pass the de minimis test in the previous partial exemption year
- consistently apply the annual test throughout any given partial exemption year
- have reasonable grounds for not expecting to incur more than £1million input tax in its current partial exemption year

If any conditions are not met, the business is required to apply the de minimis test in each VAT period, which remains the default position.

The risk with the annual test is that a business provisionally recovers input tax relating to exempt supplies in-year, but then fails the test at year-end and has to repay the input tax to HMRC. If a business is likely to fail the test at year-end and then struggle to repay the input tax, the annual test should be avoided.

REVENUE & CUSTOMS BRIEF 11/10

VAT: The decision of the VAT Tribunal in respect of Rank (gaming machines) issued December 2009

An update on the current position in the gaming machine side of the Rank case.

The Brief begins by referring to the 2009 High Court decision, which found that there had been a breach of fiscal neutrality by HMRC on both mechanised bingo and gaming machines.

On the gaming machines, as the judgment related to an appeal against an interim ruling of the VAT Tribunal, HMRC advised that no claims for output tax wrongly paid over would

be considered until the Tribunal issued a final ruling in respect of Rank, which was issued in December 2009 and found that Fixed Odds Betting Terminals (FOBTs) were similar to, and in competition with, taxable gaming machines. HMRC are appealing against this decision to the Upper Tribunal, and additionally, the Court of Appeal is due to hear the appeal against the earlier findings of both the VAT Tribunal and the High Court.

HMRC say that, on the basis of the Tribunal and High Court findings (and subject to the appeals), they will consider paying those claims already received in respect of VAT paid on gaming machine takings.

As FOBTs came into UK commercial use in November 1998, as agreed by the Tribunal, HMRC will now accept existing claims submitted within required time limits for VAT paid on gaming machine takings between 1 November 1998 and 5 December 2005. Claims that have been previously rejected and are not under appeal will be rejected. HMRC state that no new claims for the period 1 November 1998 and 5 December 2005 can be made. Subject to providing satisfactory evidence, HMRC aim to repay these claims by 31 March 2011.

The Brief closes with a comment that HMRC will issue protective assessments to recover the repayments should its appeal succeed.

REVENUE & CUSTOMS BRIEF 12/10

VAT: provision of health professionals, nursing auxiliaries, care assistants and support workers by employment businesses – clarification of policy

A clarification of HMRC policy on the VAT treatment of supplies of health professionals, nursing auxiliaries, care assistants and support workers by employment businesses.

The Brief begins with a useful list of definitions which are worth reproducing, beginning with

the meaning of the term 'health professional' as follows:

- *Dentist or Dental Care Professional – an individual registered with the General Dental Council*
- *Doctor – an individual registered with the General Medical Council*
- *Nurse, midwife or community public health nurse – an individual registered with the Nursing & Midwifery Council*
- *Individuals registered by the Health Professions Council – including:*
 - *Arts Therapist*
 - *Biomedical Scientist*
 - *Chiropodist/Podiatrist*
 - *Clinical Scientist*
 - *Dietician*
 - *Occupational Therapist*
 - *Operating Department Practitioner*
 - *Orthoptist*
 - *Paramedic*
 - *Physiotherapist*
 - *Psychologist*
 - *Prosthetist/Orthotist*
 - *Radiographer*
 - *Speech & Language Therapist*

'Nursing auxiliary' – an individual who is not enrolled on any register of medical or health professionals but whose duties must include the provision of medical, as well as personal, care to patients.

'Care assistant' - an individual who is not enrolled on any register of medical or health professionals but who provides both medical and personal care to the recipient.

'Support worker' - an individual providing personal care and support services that may or may not be directly connected with the welfare of the recipient.

'Medical care' – in the context of what is provided by nursing auxiliaries and care assistants, includes monitoring the health of patients, for example, by taking blood pressure and temperatures, as well as administering drugs to patients under the direct supervision of a health professional.

'Personal care' – includes washing and dressing, feeding, helping people to mobilise, bed making, toileting etc., but does not include medical care.

The Basic VAT Position

The Brief outlines the basic VAT position that staff supplied by an employment business, where that person comes under the direction and control of the client, is a taxable supply of staff. This is regardless of whether the person is an employee of that business, or is self-employed and engaged under contract by the employment business. Consequently, the employment business must account for VAT on the full charge to the client.

Where an employment business maintains the direction and control of its staff to make a supply of welfare or medical services directly to the final consumer, HMRC would see this as providing health or welfare services rather than just a supply of staff. In these circumstances, subject to certain relevant criteria being met, HMRC would consider it an exempt supply.

The Brief then goes on to look at more specific types of supplies as follows:

- Supplies of registered health professionals (other than nurses, midwives and community public health nurses) where staff controlled by the third party – *taxable supply of staff*
- Supplies of locum GPs - *taxable supply of staff*
- Supplies of nurses, nursing auxiliaries and care assistants by state regulated agencies (i.e. the nursing agency concession) – *exempt supply of staff*
- Supplies of contracted out welfare services – *taxable supply of staff or exempt supply of welfare, depending on structure in place with the local authority*

The Brief ends with a section on the wording of terms and conditions of agreements, stating that they are "aware that some employment businesses state in their contract terms that

Latest VAT News (continued 4)

their staff are still working under their control and direction rather than the third party to which their staff are being supplied". HMRC say that such businesses are no longer acting as an 'employment business' within the definition of the Employment Act 1976, and that the VAT liability of a supply cannot be determined conclusively by the terms of any contract or other documentation alone.

REVENUE & CUSTOMS BRIEF 13/10

VAT: Place of Supply of freight transport and associated services - used and enjoyed outside the EU

This Brief details a temporary 'administrative easement' in relation to B2B supplies of freight transport (and also services closely associated with freight transport) which are physically performed outside the EU. HMRC say that the easement applies from 15 March 2010, and is not retrospective.

The Brief explains that, prior to 1 January 2010, supplies of freight transport and associated services were supplied 'where physically performed', so that where performed outside the EU, they were outside the scope of VAT. In addition to this, transportation within the EU which related to imports and exports was zero-rated.

From 1 January 2010, B2B supplies of freight transport and associated services became subject to the new B2B 'general rule' for place of supply of services (i.e. where the business customer belongs), regardless of the place of physical performance. As such, where the customer is in the UK, the place of supply is the UK even if the supply physically takes place outside the EU. As zero rating only applies to supplies in connection with EU imports and exports, the liability of supplies outside the EU is standard-rated. This means that either the UK-based customer must perform a reverse charge for the supply (if the supplier is outside the UK) or the supplier needs to account for UK VAT on the supply.

HMRC says it has become aware that this change has had an adverse impact, either in

terms of increasing administrative burdens or, in some cases, resulting in a real VAT cost (particularly for charities). HMRC can see that the law change has produced an unintended anomaly in the treatment of supplies enjoyed outside the EU, which may also be taxed locally in the place of performance. As such, with immediate effect, where a supply of freight transport (or closely associated services) would be treated as supplied in the UK, it will not be treated as supplied in the UK if the use and enjoyment of the services is outside the EU. The easement is being introduced as a temporary measure to allow time for consideration of a more permanent legislative solution.

REVENUE & CUSTOMS BRIEF 14/10

VAT payments by cheque – important changes with effect from 1 April 2010

As advised on the front page of the last VAT Voice, from 1 April 2010, all cheque payments sent by post to HMRC will be treated as being received on the date cleared funds reach HMRC's bank account, not the date that it is received. As such, businesses should allow enough time for their payment to reach HMRC and clear into its bank account by the due date shown on the VAT return.

Note that the change does not affect cheque payments made by Bank Giro, as they get up to an extra seven calendar days for the cleared payment to reach HMRC (unless the business uses Annual Accounting or is required to make Payments on Account).

Following the 1 April 2010 requirement for businesses with a turnover of £100,000 or more (and all newly registered businesses) to file VAT returns online and pay electronically, the purpose of the change in the cheque rules is to encourage compliance with electronic payment by removing the cashflow advantage enjoyed by businesses paying by cheque. It is also intended to make electronic methods of payment more attractive to those businesses not required to file their VAT returns online and pay electronically from 1 April 2010.

REVENUE & CUSTOMS BRIEF 15/10

VAT: Change in treatment of certain sports related services following the ECJ judgment in Canterbury Hockey Club (C-253/07)

Details of changes to the VAT exemption for sports-related services being introduced from 1 September 2010. They will primarily affect affiliation fees charged by sports governing bodies to member clubs, but the Brief says the treatment of other sports-related supplies may also be affected.

Certain services closely linked with and essential to sport or physical education are exempt when supplied by an 'eligible body' (i.e. non-profit making bodies) to an individual taking part in sport. On affiliation fees charged by sports governing bodies to member clubs, HMRC previously restricted exemption to fees calculated on a per person basis. Affiliation fees calculated by other methods, (e.g. on the basis of the club size or the number of teams fielded), were standard-rated.

However, in the case of *Canterbury Hockey Club and Canterbury Ladies' Hockey Club* the ECJ found that the VAT exemption applies more widely. It said the exemption included services supplied to corporate persons and to unincorporated associations, provided that the supplies are closely linked and essential to sport, are supplied by non-profit making organisations and the true beneficiaries are individuals taking part in sport.

From 1 September 2010, eligible bodies meeting the conditions for exemption outlined in Notice 701/45 'Sport' must exempt supplies where the true beneficiaries are persons taking part in sport, even if the supply is not made direct to an individual and irrespective of how the fee is calculated. Supplies made to commercial profit-making organisations do not meet the true beneficiary test, and will not fall within the exemption for supplies of services closely linked and essential to sport.

HMRC say that where the affiliation fee provides several benefits, which, individually, would have different VAT liabilities, the advice

in section 4 of Notice 701/5 can be followed to determine whether there is a single or multiple supply. Where the conditions of ESC 3.35 are met, governing bodies may continue to take advantage of the option to apportion their affiliation fees between the rates due on the individual elements. The ECJ gave examples of services not falling within the exemption, including advice about marketing and the obtaining of sponsors. HMRC say these will be liable to the standard rate when ESC 3.35 is applied, unless relief is available under another part of the VAT Act.

The policy change may affect other supplies closely linked and essential to sport by eligible bodies to unincorporated associations and corporate persons where the true beneficiary is a person taking part in sport. An example could be the letting of sports facilities to a club for use by members. In these circumstances, the supply is exempt if the club is non-profit making. Otherwise, it will be taxable.

Although the change is to be introduced from 1 September 2010, HMRC say organisations can apply exemption to their fees before that date if they so wish. Claims for VAT refunds will be subject to the usual time limits.

REVENUE & CUSTOMS BRIEF 16/10

New time limits for assessments and claims

A reminder about the new four-year time limit for assessments and claims of VAT effective from 1 April 2010 (per Sch 39 FA 2008).

From that date, the new time limits are:

- Normal time limit - four years
- Careless behaviour - four years
- Deliberate behaviour - 20 years

from the end of the relevant tax period.

HMRC no longer has 20 years where a tax loss was attributable to negligent conduct now equating to careless behaviour. However, the 20-year time will still apply to cases of 'failure to notify', and certain failures in respect of tax avoidance schemes.

REVENUE & CUSTOMS BRIEF 19/10

VAT: postal services - claims for Input Tax
Further to the issue of BN48 in the recent Budget, HMRC now confirms that certain postal services previously treated as exempt, will become standard-rated from 31 January 2011. The change in liability follows the ECJ's decision in *TNT Post UK (C-357/07)*, which was originally outlined in R&CB 64/09.

Broadly, the proposed changes will mean that any service which is individually negotiated or not subject to any price and regulatory control will become liable to VAT at the standard rate. This includes, but is not limited to:

- all individually negotiated services
- Parcelforce services
- door-to-door (unaddressed mail)
- mailroom services

Services which Royal Mail provides under the terms of its licence, and are therefore subject to price and regulatory control, will remain exempt from VAT (subject to there being no individual negotiation). This applies to:

- services covered by Royal Mail's Universal Service Obligation (including stamped mail)
- regulated services
- access to its network for private postal operators

HMRC say they will now process VAT claims submitted on the back of the TNT decision. They will consider following in doing so:

- the contractual arrangements between the claimant and Royal Mail over the period of the claim
- whether the supplies to which the claim relates would have been taxable at the standard rate under the new rules
- evidence that input tax was incurred
- (for 'Fleming' claims) developments in the postal market and related legislation over the period of the claim

Comment: *It is hard to see how claimants will be able show that input tax was incurred if it was never actually charged to them in the first place!*

VAT INFORMATION SHEET 02/10

VAT: Changes to the operation of the option to tax on supplies of land and build
A more in-depth look at the changes outlined in R&CB 08/10 on page 2 of this VAT Voice.

VAT INFORMATION SHEET 03/10

VAT status of university trading companies: new guidelines
A more in-depth look at the changes outlined in R&CB 09/10 on page 2 of this VAT Voice.

VAT INFORMATION SHEET 04/10

VAT: Partial Exemption - changes to the de minimis rules
A more in-depth look at the changes outlined in R&CB 10/10 on page 3 of this VAT Voice.

VAT INFORMATION SHEET 05/10

Electronically supplied services: Special scheme for non-EU businesses
From 15 March 2010, the standard rate of VAT in Greece will increase from 19% to 21%.

VAT INFORMATION SHEET 06/10

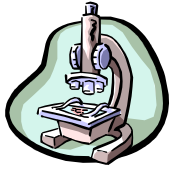
Electronically supplied services: Special scheme for non-EU businesses
On 1 January 2010, the standard rate in the Czech Republic increased from 19% to 20%.

VAT INFORMATION SHEET 08/10

VAT: Land & buildings - minor changes in relation to the option to tax
Details of tertiary law and wording changes for Notice 742A and some of the VAT1614 forms.

VAT INFORMATION SHEET 09/10

Electronically supplied services: Special scheme for non-EU businesses
Details of the currency exchange rates to be used for the March 2010 period in the Special Scheme for Non-EU Businesses relating to the supply of electronically supplied services.



In Focus

APRIL FOOL'S DAY PROVES TO BE NO JOKE FOR HMRC!

In the usually sedate world of VAT, it's fair to say that 1 April 2010 has turned out to be a maelstrom of HMRC changes. So much so, that we thought it might be useful to summarise them all for easy reference:

Increased VAT Registration and Deregistration Thresholds

The VAT registration increased from £68,000 to £70,000, and the deregistration threshold increased from £66,000 to £68,000.

Online VAT return filing

Compulsory electronic submission now applies to any existing VAT registered business with an annual VAT exclusive turnover of more than £100,000, and all new businesses VAT registered on or after 1 April 2010. The seven-day extension rules for electronic VAT return submission and payment continue unchanged.

New four-year time limit for assessments and claims

Following the completion of the transitional period introduced from 1 April 2009 (which prevented the twelve-month period prior to 31 March 2006 from coming back into time again), there is now a four-year time limit for HMRC to raise assessments of tax. In terms of making VAT claims, the effect is two-fold as follows:

1. Overpaid output tax (s80 claims)

The time limit for claiming overpaid output tax is now *four years from the end of a prescribed accounting period (i.e. VAT return period)*. The first output tax to fall out of time will be for periods ending 30 April 2006, which will fall out of time after 30 April 2010. For businesses with calendar quarters, the first output tax to fall out of time will be for the periods ending 30 June 2006, with the deadline for such claims being 30 June 2010.

2. Underclaimed input tax (reg 29 claims)

The time limit for under-claimed input tax is *now four years from the due date for the return period during which the entitlement to input tax arose*. This means the first input tax to drop off will be that incurred in March 2006, which will have been claimed on a return due post 31 March 2006). This VAT will go out of time on 30 April 2010.

New 'failure to notify' penalty

In VAT terms, the failure to notify penalty is essentially a new late registration penalty, but it also covers other failures to notify, such as the requirement to give notification of acquisition of goods from another Member State. This penalty was the subject of the 'In Focus' section of the previous edition of VAT Voice. It is calculated on the amount of tax due, and the bands of penalty percentages are very similar to those of the 'inaccuracy penalty' regime introduced last year for VAT returns.

VAT & Excise wrongdoing penalty

A new VAT & Excise 'wrongdoing penalty' has been introduced, and applies where a person:

- Issues an invoice with VAT he is not entitled to charge
- Handles goods on which Excise Duty has not been paid or deferred
- Uses a product in a way which means more Excise Duty should have been paid
- Supplies a product at a lower rate of Excise Duty knowing that it will be used in a way that means a higher rate of Excise Duty should be paid

As with the 'inaccuracy' and 'failure to notify' penalties, the penalty banding depends on the reason for the wrongdoing and the nature of disclosure.

VAT payments by cheque – cleared funds rule

From 1 April 2010, all cheque payments by post to HMRC will be treated as being received on the date when cleared funds reach HMRC's bank account. This needs to be considered when paying VAT returns by their due date.

Partial exemption simplification

Two simplifications to the partial exemption process were introduced from 1 April 2010. The first is the 'annual test', which allows a business to apply the de minimis test on an annual basis rather than quarterly. However, this will not be available to businesses that expect their total input tax to exceed £1m per year, or to newly VAT registered businesses.

The second simplification is the 'simplified test', which gives VAT registered taxpayers the opportunity to use a simple test to calculate whether they are de minimis, rather than performing a full partial exemption calculation. The test requires total input tax (minus input tax that relates exclusively to taxable supplies) to be no more than £7,500, and the value of exempt supplies to not exceed 50% of the value of all supplies.

Enforcement of Judgments in litigation

Currently, where a Tribunal or Court finding is appealed by HMRC following a taxpayer win, HMRC has to repay overpaid taxes before the appeal is heard. However, where the decision is in favour of HMRC, they do not consistently collect the tax from the taxpayer before the appeal. Going forward, a new policy will require payment of the tax in all cases, and will take effect on all decisions made by the Tribunals or Courts from 1 April 2010. In VAT appeals, the taxpayer may apply for the tax to be held over if they can demonstrate they would suffer financial hardship by being forced to pay the tax prior to appeal hearing.

Simplification of the Option to tax and changes to definition of a housing association

A number of changes have been made to the liability of supplies of land and buildings, as well updating the legislative definitions of a 'relevant housing association'. The first change is a simplification of the option to tax concerning disapplication. It excludes certain transactions from the anti-avoidance provisions, and allows developers to tax supplies of buildings where persons financing the construction are only in minor occupation of the building. There is also a simplification of the six month 'cooling-off' period to revoke an option to tax. HMRC have removed the condition that a taxpayer must not have used the land in order to be able to revoke the option. Changes were also made to the definition of a 'relevant housing association' to reflect the new Housing and Regeneration Act 2008, which replaces the existing system in England. Schedule 10 refers to the Housing Act 1996, which only now applies in Wales. A similar definition change was also made to Group 5 of Schedule 8, which covers construction.

In Focus (continued 2)**A REMINDER OF THE BUDGET 2010 VAT CHANGES****1. CHANGES WHOLLY FOR VAT****Increased turnover thresholds for VAT registration and deregistration**

From 1 April 2010, the registration threshold will increase from £68,000 to £70,000, and the deregistration will be increased from £66,000 to £68,000.

Changes in Fuel Scale Charges

The scale charges will be increased significantly to reflect the equivalent rise in fuel prices, with new rates being applicable to VAT return periods beginning on or after 1 May 2010.

Reverse Charge for Emissions Allowances

The reverse charge on goods to counter MTIC fraud is to be extended so that it can be also applied to services. From 1 November 2010, a reverse charge will be introduced for supplies of emissions allowances, and will mean that a VAT registered business purchasing allowances will have account for and pay the VAT chargeable instead of the supplier. The measure will replace the interim zero-rate introduced on 31 July 2009. The new legislation will also provide an option for the introduction of reporting requirements to deal with fraud in the services sector. There will no additional reporting requirements for emissions allowances, however so suppliers will not be required to provide Reverse Charge Sales Lists (RCSL) for those supplies.

Postal Services

Following the ECJ's decision in the TNT case, the VAT exemption for postal services has been narrowed to that of public postal services supplied by a universal service provider (USP). As such, it will only directly affect Royal Mail. The measure also updates zero rating for passenger transport services to reflect the status of the provider of a passenger transport service made in conjunction with its postal services. The change is effective from 31 January 2011, with the relevant legislation to be included in Finance Bill 2010.

Changes to zero-rating of qualifying aircraft

From 1 September 2010, the legal definition of zero-rated aircraft will change from being based on weight and usage to being based on the status of the customer. Aircraft will only be zero-rated where used by airlines operating for reward chiefly on international routes. State institutions will not be affected by the change.

Place of supply of gas, electricity, heat and cooling

From 1 January 2011, the place of supply rules for natural gas and electricity supplies will be amended to:

- cover supplies in all types of natural gas pipeline, but will no longer apply to natural gas in pipelines located outside the EU unless linked to EU pipelines;
- provide relief from import VAT for all natural gas imported via a network (including liquefied natural gas by tanker); and
- extend the scope to include heat and cooling supplied through networks.

In Focus (continued 3)

2. CROSS-TAX CHANGES WHICH INCLUDE VAT

Penalties for late filing and payment of returns

An announcement of new cross-tax penalties, which will be introduced over a number of years due to the changes required to current HMRC computer systems. Under the new penalty regime, to be set out in Finance Bill 2010, there will be separate penalties for late filing and late payment, split between quarterly and monthly return periods.

- For late filing of quarterly returns, there is an initial fixed £100 penalty and 1-year penalty period. Further defaults within the penalty period can increase the penalty by £100 to a maximum of £400, with the penalty period extended for each subsequent fault. Prolonged failure will incur an additional 5% penalty of the tax amount after 6 and 12 months, and there is scope for a 100% penalty where the taxpayer is found to be withholding information.
- For late filing of monthly returns, there is a fixed £100 penalty for on each of the first three defaults, and a fixed penalty of £200 for each the second three defaults, etc., up to a maximum of £400.
- For late payment of quarterly returns, an initial default will only trigger a 1-year penalty period, but further defaults will incur incremental 2%, 3%, and 4% penalties, with the penalty period being extended for each default. Prolonged defaults will incur an additional 5% penalty of the tax amount after 6 and 12 months.
- For late payment of monthly returns, there is also just a 1-year penalty period for the first default, but the next three defaults in the penalty period incur penalties at 1%, and the next three defaults at 2%, up to a maximum of 4%.

The new regime comes with the right of appeal for reasonable excuse. Late payment penalties can also be avoided where there is a Time To Pay Arrangement in place.

Cost-sharing exemption

HMRC recognises the efficiencies that can be achieved by organisations such as charities sharing services, and the potential direct tax and VAT barriers that exist. HMRC will work with charities and other affected sectors to consider options for implementing the EU cost sharing exemption.

Arrears of Tax - Business Payment Support Service

The Business Payment Support Service (BPSS) is set to continue. The service grants streamlined access to Time to pay, and is available for all HMRC taxes, including VAT

Arrears of Tax - Large Time To Pay applications

HMRC will require businesses seeking Time To Pay arrangements of £1million or more, to provide an Independent Business Review (IBR) in support of their request. However, IBRs will only apply to less than 0.25% of businesses seeking time to pay. The new requirement is expected to be introduced from April 2010.



VAT Cases

VAT Voice – May/June 2010

TRIBUNAL SAYS ONLINE SELLER OF OVERSEAS HOTEL ROOMS WAS ACTING AS A PRINCIPAL

The Appellant operates a website through which it markets hotel accommodation located in the Mediterranean and Caribbean. A traveller or travel agent would book accommodation through the website and pay the deposit and balance to the Appellant, who also kept the bank interest on this money. The relevant hotel would be paid a lesser amount by the Appellant, as agreed between the two, and would not know the price paid by the traveller. Equally, the holidaymaker would not know what the hotel received. The Appellant might pay the hotels in advance to secure the accommodation, and if cancellation charges became due from the customer under the booking conditions imposed by the Appellant, it would retain these. The Appellant also dealt with complaints, and would agree compensation without clearing the sum with the hotel. It said that where it had departed from the agency agreements and acted in a way more consistent with it being a principal, this was simply for commercial reasons.

It argued that for the period in dispute, it acted as disclosed agent for the hotels. It based this contention on its Terms and Conditions and agreements with the various parties involved. As an agent, its income comprised purely commission rather than the full amount charged for accommodation supplied to travellers/travel agents. As such, the place of supply of its services would be where the accommodation was located rather than the UK, so no UK VAT was due. However, as it was not VAT registered in any other country, VAT was not accounted for anywhere on the commission, meaning a proportion of the amounts paid by the travellers escaped VAT (i.e. a tax gap).

HMRC argued that when you looked at the entirety of the commercial arrangements and the accounting procedures, the Appellant was acting as a principal. On that basis, the supplies of accommodation would be covered by the Tour Operators Margin Scheme, meaning that its supplies took place in the UK, and that UK VAT would be due on the profit derived on the EU accommodation. On the back of that contention, HMRC had previously issued a £7m assessment to the Appellant.

The Tribunal found for HMRC after concluding that the Appellant was acting as a principal. The three main reasons for this were that it did not disclose the selling price to the hotels, the holidaymakers contracted with Med Hotels with no terms imposed by the hotel, and no hotel could go to the holidaymaker and demand payment for the accommodation provided. Other supporting factors were that it took forex and financial risks when it paid hotels in advance, it kept no client trust account, and that if a hotel made a mistake and under-invoiced the Appellant, it would retain the excess. Also, for a period when Appellant agreed it was a principal, it acted in broadly the same way as it had done when it said it was an agent.

The decision shows that it is not enough to cite contractual terms and the contents of other agreements as support of your status; what actually happens in practice is crucial. Additionally, the UK and EU courts seem increasingly to be giving decisions that plug any tax gaps where they are seen to exist. Clearly, any web-based operators that are using a similar business model to that of the Appellant should immediately review their position in light of this case.

*Secret Hotels2 Ltd (formerly Med Hotels Ltd)
(TC00431)*

VAT Cases (continued)**TRIBUNAL SAYS INJURY RISK MANAGEMENT SERVICES WERE NOT EXEMPT MEDICAL SUPPLIES**

The Appellant's services consisted of two main elements. The first was to arrange swift treatment for client companies when one of their employees sustained a musculoskeletal injury. The second was to understand clients' businesses, either on a site-by-site basis or by reference to the different activities performed by employees, so as to provide collated information about injuries sustained by all employees. This then enabled companies to locate risk areas in their businesses so that they could reduce the risks of injury, and thereby reduce the levels of sick absence.

HMRC argued that the Appellant was providing, via its health practitioner sub-contractors, exempt medical services, and that all the administrative services of compiling and delivering various reports to client companies were ancillary services. Alternatively, if the administrative services could not fairly be regarded as ancillary, HMRC argued that it was still appropriate to conclude that, from an economic point of view, the clients still receive one single composite service, and not several distinct services. As the medical aspect dominated the composite service, the whole service was exempt. The Appellant said that HMRC had misunderstood the unique nature of its business, which was to manage employee injury risk, identify risk areas, and develop suggestions to reduce the risk of injury. As such, its supplies were standard-rated.

In reaching a decision for the Appellant, the Tribunal said HMRC had been wrongly influenced by the way in which the clients were charged for each visit to a practitioner. It examined what was meant by Note 2 to items 1 and 2 of Group 7, Sch 9 VATA 1994,

finding that he Note extends exemption to "supplies of services made by a person who is not registered ... where the services are wholly performed or directly supervised by a person who is so registered or enrolled". HMRC argued that Note 2 need only apply to the dominant supply, but the Tribunal disagreed, finding that there is a single supply (i.e. Note 2 must be satisfied for all elements of the service). In this case, there was a single supply, with only one part being performed by registered practitioners. The other ancillary elements were not performed or overseen by a practitioner, so the service could not qualify as an exempt medical service. The single supply was taxable.

Health Response UK Ltd (TC00434)

ECJ SAYS DUTCH INPUT TAX BLOCK ON ENTERTAINMENT AND CARS COMPATIBLE WITH EU LAW

This case involves two joined Dutch appeals, with both cases concerning exclusions from the right to deduct input tax which the Netherlands had maintained upon adopting the Sixth VAT Directive.

The first case concerned input tax recovery on cars, where the Dutch authorities disallowed the VAT on the basis that they had not been used wholly for the needs of the company.

The second case concerned input VAT recovery on a wide range of goods and services, including the provision of food and drink to staff, business gifts, and the provision of accommodation and recreation to staff. The case also looked at the Dutch treatment where part-consideration is received, which allows input tax to be recovered up to the equivalent value of the consideration received, with the balance being blocked.

This case caused a flurry of activity earlier this year when the AG's Opinion was released, as it suggested that some of the Dutch input tax

VAT Cases (continued)

restrictions were incompatible with EU law because they were not properly defined. This led to speculation that the case could invalidate the UK's block on business entertainment, which was of a similar nature. However, the ECJ has subsequently disagreed with the AG, finding that all the Dutch input tax restrictions in place at the date of adoption of the Sixth VAT Directive were actually compatible with European law.

Having concluded that the exclusions from credit were compatible with EU law, the ECJ proceeded to look at a third question in the second case. This looked at subsequent amendments to the rules regarding the provision of food and drink which may, in certain specific situations, widen the scope of input tax credit exclusion. Here, the ECJ did agree with the AG that the essential changes reduced the scope of the exclusion from input tax credit which is compatible with derogations under Article 17(6). The existence of a theoretical scenario which might result in the widening of the exclusion did not preclude such amendments.

X Holding BV (C-538/08) and Oracle Nederland BV (C-33/09), European Court of Justice, 22 April 2010

Comment: *the fact that the ECJ has subsequently ignored the AG's Opinion presumably means that the UK law is no longer under threat.*

ECJ SAYS TAXPAYERS' CLAIM FOR COMPOUND INTEREST ON VAT REFUNDS WAS OUT OF TIME

On 25 March 2010, the Court of Appeal released its Judgment in a high-profile compound interest case, finding for HMRC. Although the taxpayers lost their appeal on whether compound interest is properly payable from HMRC on VAT refunds, it seems they only lost on the basis that they had brought their claims too late.

Whilst the decision appears to have ended this particular litigation, the CoA suggested that the underlying issue concerning an taxpayer's entitlement to seek compound interest should, in an appropriate case, be the subject of a reference to the ECJ. As the claimants lost on time limits, a reference was not possible, and whilst the arguments for compound interest are compelling on the basis of current case law, it now looks likely that a resolution of this issue will not be reached for some time yet.

In reaching its conclusion, the Court took account of its decision in *FII Group* in February 2010. The combined effect of these decisions is to create a degree of uncertainty in relation to the time limits applying to the bringing of such claims. The argument that the six-year time limit for the issue of High Court claims in VAT cases runs from the discovery of the liability mistake (or the date upon which a taxpayer reasonably have discovered the mistake), remains a forceful one. However, on the basis of *FII*, the Courts could ultimately decide that taxpayers will only be entitled to compound interest on tax overpaid in the period beginning six years before they issue their High Court claim.

If the latter scenario was accepted by the Courts, it could give rise to a rolling deadline operating in similar fashion to the four-year cap on reclaiming overpaid tax. However, as the decision in *FII* was solely concerned with direct tax, it is also possible that the Courts will restrict its application to direct tax cases.

Businesses should continue to apply a cautious approach to making claims of this nature, but where claims appear arguably valid, urgent consideration should be given to the issue of High Court proceedings.

FJ Chalke Ltd & Anor (a.k.a 'VIC GLO') Court of Appeal (EWCA Civ 313), 25 March 2010



VAT Tips

VAT Voice – May/June 2010

TEN BASIC VAT TIPS FOR BUSINESSES

1. Should you be VAT registered?

If your UK taxable supplies are above £70,000 p.a., you must register compulsorily, unless they are all zero-rated, in which case, you could apply for exemption from registration. If your taxable supplies are below £70,000, and your customers are mainly or wholly VAT registered, you can register voluntarily to recover UK input tax. If you have a UK business establishment (including a branch or agency), but your supplies (including certain exempt supplies) are all made outside the UK, voluntary registration to recover UK input tax is again an option, but does mean you might be compulsorily registerable in another country.

2. Make sure you recover all pre-registration VAT (including pre- incorporation VAT if applicable)

VAT incurred on capital assets and stock which is still on hand at the registration date can be recovered up to four years previously. VAT on services can usually be deducted up to six months before the registration date.

3. Unregistered businesses can also save VAT

The use of unregistered suppliers may help, as could the use of non-UK suppliers of services (but this may count towards your UK registration turnover). If you are looking to rent premises, consider looking for a property with a non-VAT rent, or else raise the issue of your inability to recover VAT in the rent negotiations. Charities should check they are getting VAT relief on their income under the charity zero-rating concessions and fundraising exemption. Similarly, for expenses, charities can check that suppliers are zero-rating or reduced-rating their supplies wherever possible.

4. Use an appropriate simplification scheme

The Flat Rate Scheme (with a 1% discount in first year of registration), cash accounting, or annual accounting can all create cash flow and/or administrative savings.

5. Be compliant!

Keeping up-to-date VAT records, submitting and paying VAT returns on time, and disclosing errors as soon as they are found will avoid interest, potential penalties, and endless hassle from HMRC.

6. Recover VAT incurred the EU

You may be able to claim EU VAT via HMRC's online portal under the EC 8th Directive.

7. Needing a car?

Unless there would be purely business use (e.g. a taxi, hire car, or pool car), which would allow full VAT recovery, the VAT on the purchase of a car is irrecoverable just by being 'available' for private use. Consider leasing rather than buying, as 50% of VAT on the lease charge is recoverable, as is 100% of roadside maintenance if it is split out on the invoice.

8. Do you recover VAT on road fuel?

You can keep detailed records of private and business journeys to support apportionment of the input VAT, or else pay the fuel scale charges and recover all the VAT.

9. VAT on entertainment costs

The VAT on entertaining clients, potential clients, and non-employees is not recoverable (unless a reasonable charge is made), but the cost of staff entertainment will be recoverable if incurred for the ultimate benefit of the business (e.g. a team away-day).

5. Are your VAT liabilities correct?

Many businesses have complex VAT liabilities (e.g. printers, financial services providers, charities, take away food outlets). If you are not sure, it would be wise to have them reviewed to make sure you are not storing up a future VAT bill or a challenge from HMRC.

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