VAT update - 14 August 2015

In this month's edition of the VAT update we look at:

1. consultation on Tribunal reform and proposal to charge fees
2. VAT reduced rate for installation of energy saving materials
3. Golf club tax planning scheme
4. boundaries of the exemption for medical care and dentistry
5. partial exemption rules for hire purchase finance company groups.

1. Consultation on Tribunal reform and proposal to charge fees

I was a supporter of the old system of the General Commissioners because it gave taxpayers an accessible and independent route to settle disputes with HMRC on a no cost basis. Therefore I was opposed to the proposals which did away with the General and Special Commissioners and created the new tribunals. However, I was reassured that taxpayers' safeguards were preserved because there was an election for taxpayers to choose that there would not be any costs awarded to the losing party.

In 2012 I presented a paper in which I recommended that the HMRC review teams needed to improve their performance because far too many cases arrived at tribunal when it was clear that the case should have been, and could have been settled by negotiation and a clear explanation of the law. There were also many appeals against late filing penalties that year and this demonstrated how important it was to safeguard taxpayers. There were many examples of HMRC seeking a penalty which was inappropriate and quite disproportionate

The Ministry of Justice is responsible for administering the tribunals. It is now consulting on proposals to introduce fees for taxpayers who take their cases to the First-tier or Upper Tribunal. Consultation closes on 15th September and there is a huge public interest element to this consultation.

The consultation is part of a wider set of proposals to introduce and /or increase charges for accessing Courts and Tribunals. For the First-tier Tribunal for paper and basic cases an issue fee of £50 is proposed, and for standard and complex cases an issue fee of £200. Where cases go to a full hearing, fees are proposed as follows: basic £200; standard £500; complex £1,000.

I am concerned that the introduction of fees might deny many taxpayers access to justice and will deter many taxpayers from pursuing legitimate arguments which involve small amounts of money. I think that it is important to preserve free access to the First Tier Tribunal.

The consultation also proposes to charge fees to access the Upper Tribunal. For the Upper Tribunal there would be a fee of £100 to seek permission to appeal; £200 for a permission hearing (where permission has been refused on the papers); and £2,000 for a substantive appeal hearing.

2. VAT reduced rate for installation of energy saving materials

On 31 July 2015, **R&C brief 13(2015)** was published. The European Court has decided that the UK's application of the reduced rate of VAT for the installation of energy saving materials was wider than permitted by EU law.

If legislative change is necessary, it will not be before 2016.

The R&C brief 13(2015 states that:

The government is currently considering the implications of the decision. If there are to be any legislative changes, they won't be implemented before Finance Act 2016. Until then, supplies of the installation of energy savings materials will continue to be reduced rated and any changes won't apply to future supplies and will not apply to supplies already made.

Our interpretation of this statement is that, subject to transitional provisions, any legislative change will only affect supplies made on or after the date those changes take effect.

3. Golf club tax planning scheme fails to get exemption

In **Massey & Anor (t/a Hilden Park Partnership) v Revenue and Customs [2015] UKUT 405**, a tax planning scheme to gain the benefit of the sports exemption failed.

The Upper tribunal's (UT) decision is interesting because it upheld the decision of the First-tier Tribunal (FTT) and considered whether the arrangement was an abuse of law, deciding that it was. The UT agreed with the FTT's conclusion that a planning scheme that failed technically was 'abusive' and could be re-characterised. The re-characterisation ignored the involvement of two companies which had been set up to implement the tax planning attempt to make the supplies to golfers exempt rather than standard rated.

A Partnership owned and operated a golf club at Hilden Park golf course ('Hilden Park') in Kent. Supplies of services closely linked to golf by golf clubs that are privately owned and run as a business for profit ('proprietary golf clubs') to persons taking part in the sport are chargeable to VAT at the standard rate. The partnership charged and accounted for VAT on supplies of the right to play golf at Hilden Park.

In 2001, the Partnership entered into arrangements with the aim of converting Hilden Park from a proprietary club to one owned by a 'not-for-profit' organisation. Supplies by non-profit making bodies of services closely linked to sport are exempt under Group 10 of Schedule 9 to the Value Added Tax Act 1994 ('VATA94').

The Partnership transferred the golf club business to two companies ('the companies') limited by guarantee and prohibited by their articles from distributing profits. The Partnership retained the golf course and club premises, which it let to the Companies.

The Companies paid rent to the Partnership as landlord. The Appellants considered that they made exempt supplies of land so that no VAT was charged or accounted for on the rent, and the Companies considered that they made exempt supplies of sports services so that no VAT was accounted for on the supplies of golf services to members and guests at the club.

This 'scheme' attempted to turn a proprietary, profit making, golf club into a 'not for profit' club that made exempt, rather than VATable, supplies. If the scheme had worked the Partnership could have increased their profit. Unfortunately, the scheme failed and even worse was held to be an abuse of law and so the partnerships were treated as making the VATable supplies to players, and the assessments against the Partnership were confirmed. The insertion of the alleged not for profit companies, which were now insolvent, was ignored for tax purposes and the protective assessments on those companies - (insolvent) - fell away.

I think that the findings of fact made by the FTT meant that the scheme was doomed to fail. They found that at all times the companies were controlled by Mr Massey and that the rent paid to the partnership was excessive. The judgement is worth a read because of its review and discussion of the Halifax and Weald Leasing decisions on abuse of law.

4. Examining the boundaries of the exemption for medical care and dentistry

With VAT standard rate at 20%, controlling costs and irrecoverable input tax for any exempt business activity is very important. In **City Fresh Services Ltd –v- R&C 2015UKFTT0364**, the dispute was whether the supply was one of exempt medical care or a standard rated supply of staff service, the latter being HMRC's contention. The Appellant argues that the supplies made by City Fresh Services Limited to a dental partnership, the City Dental Practice are exempt supplies of medical care under Schedule 9, Group 7, Item 2 (and note 2) VATA 1994.

From March 2010 City Fresh invoiced Wolverhampton City Dental Practice (CDP) for the supply of "dental services" for a fixed monthly fee of £30,000. An important difference from the case mentioned above is that there was no suggestion that either CDP or City Fresh had been set up other than for commercial reasons and could be treated as making the supplies in question.

Ms Parmajit Kaur Athwal's witness statement explained that having set up CDP in 2005 and entered into a contract with the NHS Trust, she became aware in 2006 of a change in the rules which allowed companies to carry out dentistry services and that a corporate structure would provide asset protection and tax deferrals.

In practice all the dentistry work of CDP was carried out by Ms Athwal and her partner in their roles as directors of City Fresh through the informal sub-contracting arrangement. Ms Athwal said that in her view dentistry work was not carried out by CDP, but by herself and her partner through City Fresh.

Although it may seem something of a tangent, this case is of interest to direct tax practitioners because it is looking at the underlying issue of employment status and, in particular, the test of control. The essence of the supply of staff is that they are under the control and supervision of the recipient who determines what they are used to do. This is consistent with HMRC's Notice 700/34. This was not the case here since the "staff" were directors of City Fresh and partners in the recipient CDP partnership and so could not be controlling themselves.

In circumstances where there is no suggestion that a chain of entities has been set up for abusive purposes and where there is a complete coincidence between the services provided by each entity in the chain to the end user NHS trust, the FTT do not think that nature of the service should be treated any differently between the parties in the chain; all are making exempt supplies of medical care.

5. Clarification of partial exemption recovery for hire purchase finance groups

Volkswagen Financial Services (UK) Ltd v HM Revenue & Customs [2015] EWCA Civ 832 is a complex case and not one that I could summarise effectively in a few words.

Volkswagen Financial Services (UK) Limited ("VWFS") is the representative member of the VWFS VAT group. It is a wholly owned subsidiary of Volkswagen Financial Services AG which is itself ultimately owned by Volkswagen AG. The Volkswagen Group owns and manufactures cars and commercial vehicles under the well-known VW, Audi, SEAT and Skoda marques. Many of the sales are financed through captive finance houses of which VWFS is one.

For the purposes of VAT, the business of VWFS is divided into a number of different sectors which are summarised in the agreed statement of facts prepared for the purpose of these proceedings. They are:

1. Retail – (i) entering into hire purchase ("HP") agreements with customers in respect of Group Brand vehicles; (ii) entering into leasing agreements with customers in respect of Group Brand vehicles; and (iii) fixed price service and maintenance contracts on Group Brand vehicles;
2. Wholesale – providing funding to dealers of Group Brand vehicles for the purchase of demonstrator vehicles and stock (new and used cars);
3. Volkswagen Insurance Services ("VIS") – the arrangement of insurance for owners of Group Brand vehicles and dealers of Group Brand vehicles;
4. Asset Backed Securitisation ("ABS") – servicing (and reporting on) securitised hire purchase contracts;
5. Contract Disposals – the disposal of previously leased and/or repossessed Group Brand vehicles; and
6. Catch All – miscellaneous items, such as the provisions of training programmes or the rental of signage to dealers of Group Brand vehicles.

For VAT purposes VWFS is treated as making two separate supplies to a customer who purchases a car on finance. The first is a taxable supply of the car or other vehicle on which VWFS must account

for output tax on the full price of the vehicle at the date of the contract. The second is an exempt supply of finance. In economic terms this has the effect that VWFS is required to account to HMRC for output tax on the price of the vehicle when sold, but can only recover the VAT from the customer as part of the monthly payments made under the HP contract. The vehicles are sold on to the customer at the same price as they are purchased from the dealer. Nor is any finance provided by VWFS except in respect of VW Group brands.

The issue on this appeal is whether any of the residual input tax paid by VWFS in respect of the general overheads of the business is deductible against the output tax paid on the taxable supply of vehicles to customers. In short, HMRC contend that the correct tax treatment of the residual input tax on overheads in this case is that the overheads are all attributable to the exempt supplies of finance and the input tax is therefore irrecoverable.

In a unanimous decision delivered on 28 July the Court of Appeal has found in favour of the taxpayer. The part of the residual tax recovery should be based on a proportion that the overheads are allocated on the basis of some taxable supplies. If you have a client involved in finance and hire purchase, this is an essential read but it is a lengthy and complex decision.

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The views expressed in these podcasts are Derek Allen's personal views and do not necessarily represent AAT policy or strategy.

This podcast concentrated on VAT. There will be a general tax podcast updating AAT members on recent developments and decisions available on the website on 31 August 2015.