VAT update – 14 March 2016

In this edition of the VAT update we look at:

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1. Wakefield College: building construction rules as standard rated

In Revenue & Customs v Wakefield College [2016] UKUT 19, the Upper Tribunal considered that even though the college was supplying accommodation at less than it cost, the building was denied zero rating because it was in use in the furtherance of a business. This seems to me to be another example of HMRC pursuing the strict interpretation of the law and ignoring the spirit of the legislation. It seemed to the tribunal that it was a failure of Parliament to draft legislation which achieved its purpose properly.

The appeal represents the latest stage of a lengthy dispute between HMRC and Wakefield College ("the College") about the supply to the College of construction services relating to a new building for the College, known as the SkillsXchange ("the Building"), at Glasshoughton. The College maintains that the supply should be zero-rated for VAT purposes, but by a ruling communicated by a letter dated as long ago as 23 May 2007 HMRC refused to authorise the issue by the College to the builders of a zero-rating certificate. It is that refusal which is the subject of this appeal.

Group 5 of Sch 8 to the Value Added Tax Act 1994 provides for the zero rating of various supplies made in the course of construction of certain buildings. The part of that Group relevant here is Item 2:

"The supply in the course of construction of—
(a) a building … intended for use solely for…a relevant charitable purpose…of any services related to the construction other than the services of an architect, surveyor or any person acting as a consultant or in a supervisory capacity."

That provision has to be read together with Note (6) to Group 5:
"Use for a relevant charitable purpose means use by a charity …
(a) otherwise than in the course or furtherance of a business …".

HMRC's position, however, and the reason why they consider that the construction cannot be treated as zero-rated, is that some of the College's relevant supplies of further and higher education have been made in the course or furtherance of a business.

The FTT found in the College's favour on that issue, holding that the provision of education to the relevant students was not a supply "in the course or furtherance of a business" because the link between the tuition fees paid by the students and the courses they received was insufficiently direct for the former to amount to consideration for the latter.

HMRC's appeal disclosed that there are nearly 50 cases (involving VAT of about £121 million) awaiting the Tribunal's decision in this appeal.

The majority of the College's further education students were wholly grant-funded and paid no tuition fees at all; the cost of their education was met from a block grant from the Life and Skills Council (LSC). The College was obliged by reason of the perceived difficulty in payment some of its potential students would encounter - Wakefield, we were told, is in a deprived area - to charge rather less than the assumed fees. The amount it charged to these students or their employers was set by the College alone, without consultation with other colleges in the area or the LSC, and it was possible that other colleges, even those nearby, might offer the same course for a different tuition fee. The fee payable for each course was set out in an annual prospectus published by the College. It was, no doubt, because of the constraints on what it could charge that the fees the College received made up no

more than 6 or 7% of its total income. However this exceeds the concessional de minimis limit which HMRC operates.

The UT decided that the supplies were in the course or furtherance of a business. Paragraph 52 of the decision states:

> "In our judgment the fact that the fees charged to the para [23] students represented less than the cost of the supply, because that cost was in part defrayed by grant funding, does not have the consequence that the fees did not amount to consideration for the supply. There was a direct link between the payment and the supply, and there was reciprocity of obligation: as Mr Prosser accepted, the fees were determined on a course-by-course basis by operation of the formula we have described, and a student accepted on a course who, or whose employer, paid the fee became entitled to receive the tuition. Thus both the Apple and Pear Development Council and Tolsma requirements were satisfied, with the consequence that the fee must be regarded as the consideration for the supply."

What I found very interesting is the observation at the end which recognises that the outcome is not within the spirit of the law.

> *"We cannot leave this appeal without expressing some disquiet that it should have reached us at all. It is common ground that the College is a charity, and that the bulk of its income is derived from public funds. Because that public funding does not cover all of its costs it is compelled to seek income from other sources; but its doing so does not alter the fact that it remains a charity providing education for young people. If, by careful management or good fortune, it can earn its further income in one way rather than another, or can keep the extent of the income earned in particular ways below an arbitrary threshold, it can escape a tax burden on the construction of a building intended for its charitable purpose, but if it is unable to do so, even to a trivial extent, it is compelled to suffer not some but all of that tax burden. We think it unlikely that Parliament intended such a capricious system. We consider it unlikely; too, that Parliament would consider it a sensible use of public money for the parties to litigate this dispute twice before the FTT and now twice before this tribunal. We do not blame the parties; the College is obliged to maximise the resources available to it for the pursuit of its charitable activities, just as HMRC are obliged to collect tax which is due. Rather, we think the legislation should be reconsidered. It cannot be impossible to relieve charities of an unintended tax burden while at the same time protecting commercial organisations from unfair competition and preventing abuse".*

2. Was possible maladministration by HMRC tolerable?

I have a feeling of (almost) incredulity as I read the Court of appeal decision in BPP Holdings v Revenue and Customs [2016] EWCA Civ 121. The procedural background is set out in full in the FTT and UT judgments. A summary of the facts necessary to illustrate the key issue:

a) HMRC delayed service of their Statement of Case and failed to plead the facts on which they relied to justify their contention that the supply should be treated as part of a standard rated supply of education services with the consequence that BPP served a detailed Request for Further Information;
b) HMRC agreed to provide replies to each of the requests but refused to commit themselves to a timetable for the replies. In consequence, Judge Hellier made an order in the FTT on 15 January 2014 directing HMRC to file their replies by 31 January 2014;
c) HMRC failed to comply with Judge Hellier's order and provided replies that were manifestly inadequate with the consequence that BPP applied to the FTT for a debarring order;
d) HMRC failed to remedy their breach for several months causing further delay.

The substance of the VAT dispute of the three cases before the FTT was the chargeability to VAT of the supply of books and other printed materials by the second appellant, BPP Learning Media Limited, in the circumstance that other BPP companies (BPP Professional Education Limited and BPP University College of Professional Studies Limited) made those supplies. It was argued by HMRC that the supply of printed matter and the supply of education were indissociable from each other and accordingly chargeable to VAT as part of a composite standard rated supply of education services. In an ordinary case the supply of books and printed materials would have been zero rated under section 30 and Group 3 of Schedule 8 of the VAT Act 1994 ['VATA 1994'].

Two of the three FtT cases were conceded by HMRC in April 2014 following the decision of the FtT in *Kumon Educational UK Co. Ltd v HMRC* [2014] UKFTT 109 (TC) but one remains to be determined. It is said that the novelty in that case arises from the fact that from 19 July 2011, section 75(1) of the Finance Act 2011 amended the notes to Group 3, Schedule 8 VATA 1994 to remove zero rating of printed matter in particular circumstances. The remaining case will be the first case to consider the meaning of notes 2 and 3 to Group 3.

The Court of Appeal hearing was not about the technicalities of the VAT legislation, it was about the administration of the appeal process and the conduct of HMRC in not complying with a compliance order to supply information and documents. At the FTT decision, Judge Mosedale observed that the failure of HMRC to state its case and arguments led to a delay of 8 months and the issue now under consideration was whether HMRC should be barred from pursuing the appeal because the delay prejudiced the appellant BPP.

At the UT Judge Bishopp also held that:

> [59] "There has been prejudice to BPP, in that it has been put to expense in securing the information it required, and has suffered a significant, unnecessary and unwarranted delay in the process. There has been little, and in most respects, no explanation of the failure by HMRC to do what was required of them. It follows that HMRC attract little sympathy."

This case is interesting because it is looking at the fundamental principles of justice and the administration of appeals. The Court of Appeal decided that the FTT was correct in law in according the efficient conduct of litigation at a proportionate cost and compliance with rules, practice directions and orders significant weight as part of the consideration of the overriding objective.

My incredulity is because the **"Overriding objective and the parties' obligation to co-operate with the Tribunal**

1. The overriding objective of these rules is to enable the Tribunal to deal with cases fairly and justly.
2. Dealing with a case fairly and justly includes-
    (a) Dealing with the case in ways which are proportionate to the importance of the case, the complexity of the issues, the anticipated costs and the resources of the parties;
    (b) Avoiding unnecessary formality and seeking flexibility in the proceedings;
    (c) Ensuring, so far as is practicable, that the parties are able to participate fully in the proceedings;
    (d) Using any special expertise of the Tribunal effectively, and
    (e) Avoiding delay, so far as compatible with proper consideration of the issues.

3. The Tribunal must seek to give effect to the overriding objective when it-
    (a) Exercises any power under these Rules; or
    (b) Interprets any rule or practice direction.

4. Parties must-
    a) Help the Tribunal to further the overriding objective; and
    b) Co-operate with the Tribunal generally."

I find it almost impossible to understand how HMRC could have created this situation. Unlike an individual litigant in person who may have serious constraints on their resources, HMRC should not have a problem with resources if it managed the case properly. If it has a potential problem with resources it should concede the issue or apply for extensions of time. So it seems to me right that the FTT should have sanctioned HMRC when HMRC failed to co-operate with a direction of the judge. The three judges in the Court of Appeal unanimously agreed that HMRC were barred from pursuing the appeal.

3. New fiscal framework agreed with Scottish Government

On 23 February 2016, a new fiscal framework was agreed.

Scotland appears to be one of the most over governed countries in the world. We have a small population (8.9% of the UK) yet we have many MEPs, MSPs, MPs and a very large number of Councillors in local authorities. For VAT receipts from the first 10p of the standard rate of VAT and the first 2.5p of the reduced rate of VAT in Scotland will be assigned to the Scottish Government. The two Governments have agreed that VAT assignment will be implemented in 2019-20.

The assignment of VAT will be based on a methodology that will estimate expenditure in Scotland on goods and services that are liable for VAT. To allow the development and testing of the methodology for calculating Scotland's aggregated share of VAT liabilities, there will be a transitional operational period during which VAT assignment will be forecast and calculated each year, but with no impact for the Scottish Government. The effectiveness of the methodology will be reviewed in the final year of the transition period.

4. Monthly VAT statistics in VAT bulletin

If you are interested in statistics, this document is worth a scan. It confirms that the number of registered traders is increasing and that, for example the yield in VAT in 2011 was £95.2bn but by 2015 it had increased to £113,836bn.

5. HMRC publish revised Notice 709/05 on Tour Operators Margin Scheme

The legal basis for the Tour Operators Margin Scheme (TOMS) is section 53 of the VAT Act 1994 and the VAT (Tour Operators) Order 1987 (SI 1987/1806). Sections 8 to 13 of this notice, contained in boxes, have the force of law under this Order.

This notice explains how you must account for VAT if you buy-in and re-sell travel facilities as a principal or undisclosed agent.

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14 March 2016

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 including the budget and decisions available on the website on 31March 2016.