



# KPMG's Indirect Tax Update

TAX

## Highlights

We hope you enjoy reading our further thoughts on the *Lookers* Tribunal case. The more we looked at the bits of legislation that were covered by this appeal, the more circular the issues appeared to be. There is certainly a tension between the EU provisions that deem business assets put to private use to be a supply, which make no mention of consideration (logical as, since consideration creates a supply, there is no need to deem a supply if consideration is given), but the equivalent in UK law does not appear to view consideration as a bar to the deeming provisions applying. If it did view consideration as a bar, the conditions for the open market value (OMV) direction, that was the issue under appeal, could not be met, as the direction requires there to be both consideration at undervalue and a supply under the Schedule 4 para 5 (4) deeming provisions. It did seem to us that there were a great many questions around the difference between the UK and EU provisions, the meaning of consideration and the nature of supplies and when they in fact take place, that were not examined in this very short case and which may, for instance, come to be of great importance around the time of the rate change.

The Tribunal accepted the UK law at face value and also accepted that the £10 payment for ten years private use of the demo cars by each employee constituted consideration for private use. It may have been consideration under contract law, but as we have said in the longer article it does not seem to meet the conditions to be consideration under VAT principles, being too remote from the underlying supplies. As the Tribunal was able to reach a conclusion based on the wording of Schedule 4 para 5 (4), and regulation 81, this meant the advance payment did not create a time of supply for the private use appropriation, even if it was consideration. Therefore the OMV anti avoidance provisions had been implemented by the time the supplies actually took place, and so the Tribunal could find for HMRC and strike down the planning without probing the underlying issues. We have to ask ourselves, how far should the Tribunals go in cases like these that seem on the face of it to only raise a simple time of supply question under UK regulations, but could actually lend themselves to a much wider debate?

Speaking of rate change issues, one point which comes up on a regular basis is correction of invoices which show the higher rate when in fact the supplier could make a s88 election, ignore the invoice tax point, and charge the lower rate. When the rate went down HMRC allowed 45 days for credit notes correcting VAT invoices in this way to be raised. The normal time limit is 14 days and a special statutory instrument (SI) had to be laid to change this. Now that SI had no expiry date, and is still extant, but as it also includes the reduced flat rate scheme percentages arising from the rate cut, can we be certain that it won't be repealed come 1 January? When a rate goes up, s88 is only beneficial if the invoice is being issued after the basic time of supply, (or the payment is received then, but as credit

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notes are not needed to adjust the VAT accounted for on uninvoiced supplies the main issue here concerns invoice tax points) but the invoice/payment is the tax point under normal rules. Many businesses will have set their systems to issue all invoices at 17.5 percent automatically from 1 January and would only look at this if customers specifically asked about s88 on receipt of the invoice. If the credit note time limit does revert to 14 days, it is highly unlikely there would then be time to issue valid credit notes. So although s88 is usually at the supplier's discretion, customer goodwill could be earned by considering and offering s88 automatically at the time the invoice is issued if s88 is beneficial and VAT is a cost to the customer.

Given the anti forestalling provisions (which impose s88 on suppliers in certain circumstances where s88 is not beneficial and leads to 17.5 percent VAT being due) most businesses (unless the customer base is 100 percent fully taxable businesses or no supplies will span the rate change date) will at least have to think about s88. Why not take the opportunity to create some goodwill at the same time. In these credit crunch times that small gesture may save losing or annoying a customer, or having to foot a 2.5 percent discount because the decision is taken to accommodate the customer and issue a credit note, albeit that it is out of time and hence not valid for VAT purposes. It is easier to keep a customer than find a new one.

The *Halifax* two stage abuse test is in the back of any business's mind if they are thinking about implementing any VAT planning arrangements. In particular the need to show that a VAT advantage is not the essential aim of the transactions, or that the intention of the Directive is not thwarted by the arrangements. Although planning challenged as abusive by HMRC in the *Pendragon* case has been blocked by a change to the law, and the case concerns transactions that took place years ago, the decision is still worth a read for the in depth analysis of the meaning of abuse. There was no dispute that a significant VAT advantage was obtained by recovering input tax on cars but only accounting for output tax on the profit, under the second hand goods rules of the time. However the transactions that secured that advantage and which meant the goods met the UK definition of being second hand, were driven by a need to secure finance and to provide the offshore lender with the security it required. Also EU law did not require there to be blocked VAT within the price of a second hand item, so the purpose of the Directive was not blocked by the planning. The abuse provisions should not be a back door way for HMRC to achieve a retrospective effect for a change in law to block a planning scheme that works technically under the law before it was changed, and does not contravene the *Halifax* principles.

Will the Member States ever reach agreement about the scope of exempt financial and insurance services, particularly outsourced support services? We see successive countries attempt to progress the matter in their Presidency period and suggest compromise words, (the latest developments are set out below), but still fail to secure the unanimous agreement of all. Is there still enthusiasm amongst enough Member States to carry on the debate?

Finally, there were no surprises in the *SPO* ECJ decision. The activities of a publicly funded political party were not economic activities - it was not in competition with commercial advertising agencies when passing on PR costs to district and local party organisations. There was no supply of services for consideration.

To access the highlights podcast, please click [here](#).

To access the full podcast, please click [here](#).

## From the Tax Authorities

### Revenue & Customs Brief 58/2009 VAT: Relocation of Telecoms and Internet Service Providers and Broadcasters

The purpose of this Brief is to explain HMRC's concerns and intended response to all businesses within the telecommunications, Internet service and broadcasting sectors who claim to have moved or may consider moving the place of supply of their services from the UK to another Member State. The Brief adds HMRC are aware that a number of businesses have entered into such arrangements to take advantage of more favourable VAT rates. HMRC say they will carefully examine all such arrangements. Where they consider that there are sufficient human and technical resources in the UK or where the entity purporting to make the supplies does not have a sufficient presence in the other Member State, HMRC will mount a robust challenge.

Click [here](#) to read the brief in full.

### HMRC Manual Update: Partial Exemption - October 2009

This HMRC Manual has been updated to include: additional text stating the requirement to notify local TAPE teams on receipt of a special method application; and an amendment to the special method example paragraph, regarding longer period adjustments, to reflect Budget 2009 changes.

Click [here](#) for the manual.

### E24 (2009) Tips, Gratuities, Service Charges and Troncs

HMRC has reintroduced its Booklet E24 on tax treatment of tips. This follows the publication of a new Code of Practice stipulating that tips can no longer be made to count towards the National Minimum Wage, with effect from 1 October 2009. Tips are outside the scope of VAT when genuinely freely given and therefore the changes to the rules on tips should have no VAT effect.

Click [here](#) to read the booklet.

### Rates of Exchange for Customs and VAT purposes - October 2009

For customs entries accepted by customs during the period Thursday 1 October 2009 to Saturday 31 October 2009, the following rates of exchange are to be used when any foreign currency amount has to be converted to sterling in the determination of the value for customs and VAT purposes.

Click [here](#) to view the rates.

### Notice 162 Cider Production

This notice cancels and replaces the March 2009 version. Changes include the method of duty calculation and a new section on review and appeal procedures effective from 1 April 2009.

Click [here](#) to read the notice.

### Recent JCCC papers

HMRC has released the following JCCC (09) Papers:

[62](#) New registration numbering series

[63](#) Tariff Preference: Cumulation provisions within Pan Euro-Med countries

## EU News

### Treatment of Insurance Financial services – Presidency paper on services specific to and essential for exempt insurance and financial services

We reported in September that the Presidency had sent three new documents to the Indirect Tax working party. One of these documents, a paper on 'services specific to and essential for exempt insurance and financial services', is now available. The remaining Directive and Regulation are still not publicly available.

The note reported back on discussions at the meeting of the Tax Questions Group on 16 July 2009. At this meeting the previous Presidency note on outsourcing (click [here](#)) was discussed which highlighted the split in opinion between those who want to introduce criteria which says that the services provided must entail 'changes in the legal and financial situation' from the *Sparekassernes Datacenter* (SDC) (C-2/95) ECJ ruling and those who want exemption to cover outsourced back office services in the insurance sector which were deemed taxable by the ECJ in the *Arthur Andersen* (C-472/03) ruling. The Presidency's compromise text containing reference to 'specific and essential to' was as follows:

"The exemption provided for in points (a) to (gf) of paragraph 1 shall apply to the supply of any constituent element of an insurance or financial service which itself constitutes a distinct whole and is specific to and essential for the exempt service. To be exempt under this point, the supply provided [by the sub-contractor must be intended to form part of the contractual obligations of the main supplier and] must entail a change in the legal and financial situation."

This note confirmed that a majority of Member States (fifteen) were supportive of the Presidency proposal but that some delegates wanted further clarity on what transactions should be considered to change the legal and financial situation. The note also reports that some delegations suggested the text should not cover the management of investment funds nor intermediary services and states the text has 'adjusted accordingly'. The note then goes on to look at the interpretation of the proposed Article 135(1a) concerning outsourcing and exempt services in general.

To read the paper in full click [here](#).

### The Lisbon Treaty takes a step closer to agreement.

The Lisbon Treaty has taken another step closer to agreement following Ireland's referendum last week with about 67 percent of voters in favour of the Treaty. The Treaty needs to be ratified by all 27 Member States and now only Poland and the Czech Republic have yet to do so. The Treaty is an attempt to streamline EU institutions and making the EU more democratic and efficient. Changes include a smaller European Commission, with fewer commissioners and a redistribution of voting weights between the member states. The Treaty introduces a new system for voting by member states, in cases where unanimity is not required. This says that a vote is passed if (a) 55 percent of member states are in favour - that's 15 out of 27 - and (b) these countries represent 65 percent of the EU's population. It is also passed if fewer than four countries oppose it. Currently the system is even more complicated. One of the conditions for a vote to pass is that 255 of the 345 votes distributed among the member states should be cast in favour - that is about 74 percent of the total.

The Treaty contains new powers for the European Commission, European Parliament and European Court of Justice (ECJ). However the ECJ changes primarily concern cases dealing with justice and home affairs legislation such as laws on asylum and visas, illegal immigration, or judicial co-operation etc. The UK has negotiated the right to pick and choose which of these policies it can sign up to. Under the Treaty where the UK has signed up, the UK would be affected by rulings made by the ECJ, essentially similar to Indirect Tax currently.

One change which will hopefully impact Indirect Tax concerns the leadership of the European Council. Under the Treaty a politician will be chosen to be president of the European Council for two-and-a-half years, replacing the existing system where countries take turns at being president for six months. This should hopefully give greater consistency in terms of prioritisation and approach when negotiating complex new legislation and remove the constant changing ownership every six months. Currently three successive presidents form a 'triple-shared presidency' with the aim of working together over a year and a half period to try and accomplish a common agenda by continuing the work of the previous 'lead-president' after the end of his/her term.

When the Lisbon Treaty will be ratified by the remaining Member States is currently the centre of much speculation. Whilst Poland were expected to ratify the Treaty if Ireland voted yes, in the Czech Republic there is a legal challenge by a group of senators in the constitutional court.

## UK News

### Change of Rate - Will HMRC extend time limit for issuing credit notes following s88 election

From 1 January many businesses systems will revert to 17.5 percent. Customers may challenge invoices issued at the beginning of January which relate to supplies made prior to the rate change and may ask suppliers to make a s88 adjustment. However if businesses wait until customers complain will they be in time to make an election?

#### Background

Historically regulation 15 of the VAT regulations 1995/2518 provided that where there is a change in rate and an invoice is issued before a s88 election, the supplier had 14 days after the change of rate to issue a valid credit note to give effect to the change of rate on the invoiced supply. As part of the VAT rate decrease HMRC increased this period to 45 days (see SI [2008/3021](#)). Suppliers who had pre invoiced or been pre paid, and therefore created a tax point at 17.5 percent, needed both the ability and time to correct invoices to reflect the performance of services and the actual supply of goods after the rate change at 15 percent, and in allowing 45 days for credit notes, HMRC recognised both the short notice period given of the rate decrease, and the fact that the rate change came into effect just before Christmas, when accounts sections would be closed for up to two weeks and thus unable to respond to requests from customers for a s88 election to be made and for a credit note to be issued.

The VAT increase will again result in some circumstances where a s88 election is beneficial. However on a rate increase a s88 election will only be beneficial where the performance / an element of the performance or the actual supply of goods (basic tax point) was prior to the change in rate and the actual tax point is afterwards. Therefore the s88 election can be taken when the invoice is raised after the rate change, and the result of that election would be a 15 percent rate applied to that supply. This is of course the opposite situation to that which applies when the rate goes down, when s88 is beneficial in cases where the invoice/payment creates a tax point before the rate change and the basic tax point is afterwards.

Therefore 'in theory' on a rate increase credit notes will not actually be required if the supplier makes a s88 election when raising the invoices and thus issues the invoice showing 15 percent in the first place, as the supplier will know when he issues the invoice whether the basic tax point occurred before the rate change and thus whether he can make the election. This may be one reason for the short time period allowed for credit notes in the regulation, since most rate changes are in an upward direction.

In reality businesses may be unaware of the correct application of s88 or simply unwilling to invest time and resource to ensure all beneficial elections are made on post 1 January 2010 invoices given that the primary benefit of the s88 election is not the supplier's but the customer's. This will mean that invoices will be issued to customers at 17.5 percent on which suppliers could make an election. So what happens if a customer returns the invoice requesting the supplier makes an election because the basic tax point of the supply was pre 1 January?

With the existing 45 day time limit this should allow time for most reasonable s88 requests. The SI introducing the 45 day limit had no expiry date and is currently still extant. However the SI also included the reduced flat rate scheme percentages arising from the rate cut. The key question is, when a new SI with the revised flat rate scheme percentages is released, will HMRC maintain the 45 day time limit? If HMRC revert to the 14 days time limit for credit notes under s88 by the time invoices are returned / queried it will be too late to raise a valid credit note and the VAT will be stuck at 17.5 percent. Whilst any s88 election is at the suppliers' discretion customers would certainly be unhappy at incurring extra costs needlessly, and could put pressure on the supplier to discount by the VAT differential amount, meaning the supplier then bears the cost or has a partial bad debt.

## Summary

Clearly this problem will be minimised by the retention of the 45 days limit. However it is possible that HMRC may simply reverse the 45 day extension at the same time as releasing revised flat rate percentages. It is therefore worth considering when issuing post 1 January VAT invoices, whether these are for supplies whose basic tax point was pre 1 January, made to partly exempt clients, where a s88 election made at the time the invoice is issued would both generate customer goodwill, and potentially save time and disputes (and possibly money) later.

## News

### **KPMG VAT Package website – sign up now**

As a result of the implementation of the VAT Package across the EU, from January 2010, most business to business supplies of services will be taxed where the customer is established. VAT registered customers receiving services from abroad must account for VAT by way of reverse charge as a basic rule. Businesses will also be required to submit a return to their local tax authorities in respect of cross border services supplied, the 'EC Sales List for Services'. In addition, a new electronic foreign Eighth Directive VAT refund procedure will be in place.

**We have developed a free website for our clients that sets out the key changes in every EU Member State, provides contacts across Europe in all sectors, and gives you access to our latest thinking on the key issues. Please speak to your usual KPMG advisor to request access to the site.**

## In the Courts

### ECJ

#### **Judgment C-267/08 - SPÖ Landesorganisation Kärnten – external advertising supplies of a political party are not an economic activity**

The Judgment has followed the AGO's opinion finding that the external advertising activities of a Member States political party is not an economic activity. SPÖ Landesorganisation Kärnten (SPO) is a section of the Austrian socialist party in the Land of Carinthia. SPO undertook activities on behalf of the district and local organisations of the party. Their activities were described as external advertising including public relations, advertising and information. As well buying in and selling on advertising material they were also responsible for organising a ball. Prior to 2004 only a small proportion of expenses were recharged with deficits being up from public funds, member contributions, subscriptions and donations. Then in 2004 to cover unattributable costs SPO started making a publicity charge to the various districts based on the number of members and members of parliament returned. The dispute concerned whether SPO was carrying out an economic activity. SPO argued it was and declared their external advertising as taxable turnover and claimed the related input tax.

The questions referred essentially asked whether the supplies made by SPO are economic activities under Articles 4(1) and (2) of the Sixth Directive. These provide:

#### **Article 4**

1. "Taxable person" shall mean any person who independently carries out in any place any economic activity specified in paragraph 2, whatever the purpose or results of that activity.
2. The economic activities referred to in paragraph 1 shall comprise all activities of producers, traders and persons supplying services including mining and agricultural activities and activities of the professions. The exploitation of tangible or intangible property for the purpose of obtaining income therefrom on a continuing basis shall also be considered an economic activity.

The Court confirmed from settled case law that an analysis of the definitions of taxable person and economic activities has shown the scope of economic activities is very wide. However for there to be a taxable supply there needs to be direct link between the service supplied and the consideration.

The Court added that for a supply of services to be effected 'for consideration' under Article 2(1) and therefore taxable, there needs to be a legal relationship between supplier and recipient under which remuneration constitutes the value of the service supplied. Secondly under 4(2) there needs to be income on a continuing basis. The Court noted that SPO is funded from public funds without which there would be no generation of income on a continuing basis. In fact the only continuing revenue was that from public funds. The court therefore concluded SPO's activities did not meet the criteria of an economic activity under the Sixth Directive.

Click [here](#) to read the Judgment in full.

## Tribunal

### **UKFTT 192 Pendragon Tribunal Case – were cars margin scheme cars – yes – were arrangements abusive – no – essential aim was to obtain finance – tax payer win**

The Tribunal has released the *Pendragon* Tribunal case on abuse. This is a long decision and a complex fact pattern but some of the comments by the Tribunal are critical in the context of interpreting the *Halifax* tests.

## Background

The key issue under dispute is whether demonstrator cars were second hand margin scheme cars or not and hence whether VAT was only due on the profit or on the full sale price. It was accepted these cars were used goods. HMRC's argument was that the structure which meant the cars qualified as margin scheme cars was abusive.

*Pendragon* had a commercial need for a greater range of potential financiers, better gearing and an improved range of finance repayment dates. These were all objective factors. The tax efficient demonstrator finance arrangements we devised for *Pendragon* met these objectives. In summary the transaction steps were:

- Step 1 – Captive Companies of *Pendragon* would acquire new cars from the Dealership companies
- Step 2 – On the same day the vehicles are leased back to the Dealership companies
- Step 3 – The following day the Captive Leasing companies would start to assign the benefit of the lease agreement with title to a Jersey bank
- Step 4 – About a month later the bank would transfer the leases to another *Pendragon* captive company as part of a transfer of a going concern
- Step 5 – This captive company would sell the cars as margin scheme cars to customers at arms length through the agency of the dealership companies

Essentially the arrangements used the provisions of SI 1995/1268 Art 5 (4) to make the cars margin scheme cars under Art 8 of the Cars Order, because there had been an assignment by an owner of goods comprised in an HP agreement (i.e. the demo cars) of his rights and interest to a financial institution (an off shore bank), which is a supply on which no VAT was charged as it is a desupplied transaction under that SI. The vehicles were then reacquired by a *Pendragon* subsidiary 45 days later by way of a TOGC of the car hire business from the bank and again no VAT was charged. The Art 8 conditions were thus met for these vehicles to become margin scheme cars. All this was done to secure short term loan finance for *Pendragon*, which was a commercial objective, but there was also a VAT benefit as input tax had been claimed on these cars but VAT was only accounted for on the profit when they were finally sold, if any.

It was accepted that on the face of it the transactions complied with UK law and the cars met the margin scheme conditions at the relevant time (the law was changed later to more tightly define the circumstances under which Art 8 applied) so the only issue was one of abuse and whether *Halifax* applied. Was the essential aim to obtain a VAT advantage that was contrary to the Directive? HMRC argued that the change of law meant the advantage obtained under the old law was unintended but *Pendragon* countered that the function of abuse was not to allow domestic law to be changed retrospectively.

The Tribunal concluded the essential aim was to obtain finance, and that the Directive provided that second hand goods should be sold under a margin scheme. The Tribunal used the four *WHA* questions – did the scheme result in a tax advantage, contrary to the purpose of the Directive? Was the tax advantage the essential aim? Were there any special features of the scheme or relevant law which would prevent abuse succeeding even if the answers to q1 and 2 was yes? If the answer to q3 was no, can and must the scheme or relevant part be redefined?

The Tribunal commented that EU law on second hand goods does not require there to be trapped VAT, or even that input tax should have been paid if the goods are to be treated as margin scheme goods. As *Pendragon* was selling second hand goods and complying with how the Directive envisaged these to be taxed it was difficult to see how this was contrary to the purpose of the Directive. Anyone could also see *Pendragon's* need for finance and external financiers would require the security over the vehicles that the scheme provided. This was all commercial. *Pendragon* chose to limit its VAT liability but this was not abusive. The difficulty of recharacterising the transactions also had a bearing on the decision. *Pendragon* also suggested that the UK provisions the arrangement relied on had no obvious EU vices so abuse could not be cited. However the UK Court of Appeal has rejected submissions that abuse can only be invoked in relation to EU law.

HMRC made much of the advisors involvement in 'authors, promoters and peddlers of an abusive tax avoidance scheme'. These arrangements were suggested in 1999 and implemented in 2000, in a climate that was very different from the post Halifax world of today. Even still the Tribunal did not view the arrangements as abusive and recognised that any taxpayer still has the right to organise his affairs tax efficiently within the basis of the law.

Click [here](#) to read the case.

### **UKFTT 215 Lookers Motor Group Limited – whether prepayment created time of supply before anti avoidance legislation came in – no caught by regulations under s 6(14) – appeal dismissed**

We promised to look at the questions raised by the *Lookers* Tribunal case in some more detail.

#### **Background**

This case concerned the putting of business assets (on which input tax had been claimed) to private use by the employees of the appellant. The assets were demonstrator cars owned by car dealers. EU law recognises that the putting of business assets to private use is a supply – it has to be otherwise it would be possible to acquire goods for private use without a VAT cost by routing them through a VAT registered business, and this would be distortive. However EU law supposes that no charge is made for the private use and so the appropriation of the goods becomes a deemed supply. That is to say something that would not normally be a supply under the usual rules, (which require some form of consideration (monetary or otherwise) to be paid in return for goods or services provided by a taxable person to bring them within the scope of VAT), becomes a supply by virtue of a specific provision deeming it so. This deemed supply has to be given a value so that VAT can be accounted on the private use – that value is the cost of making the asset available.

#### **Analysis**

##### The Relevant Law

Perhaps the best starting point for our analysis is Paragraph 1A(1) of Schedule 6 VATA 1994 (which is reproduced below for ease of reference):-

"1A – (1) Where –

"(a) the value of a supply made by a taxable person for **a consideration** (emphasis added) is (apart from this sub-paragraph) **less than its open market value** (emphasis added);

(b) the taxable person is a motor manufacturer or motor dealer;

(c) the person to whom the supply is made is –

I. an employee of the taxable person,

II. a person who, under the terms of his employment, provides services to the taxable person, or

III. a relative of a person falling within sub-paragraph (i) or (ii) above.

(d) the supply is a **supply of services by virtue of sub-paragraph (4) of paragraph 5 of Schedule 4** (emphasis added) (business goods put to private use etc)

Sub-paragraph (4), paragraph 5, Schedule 4, VATA1994 states the following:

*“Where by or under the directions of a person carrying on a business goods held or used for the purposes of the business are put to any private use or are used, or made available to any person for use, for any purpose other than a purpose of the business, **whether or not for a consideration** (emphasis added), that is a supply of services”*

## Commentary

Why did the draftsman use the phrase “whether or not for a consideration”? And what did he intend it to mean? Did he intend that there should be a supply of services under Sub-paragraph (4), paragraph 5, Schedule 4, VATA1994 (“The UK Deeming Provision”) in the circumstances where consideration was paid and also in the circumstances where no consideration was paid? Or did he want to ensure that transactions where no consideration was paid were brought within the scope of the tax by virtue of specific deeming provisions? At first glance the wording of The UK Deeming Provision could seemingly be interpreted either way. Thus arguably there is some ambiguity in The UK Deeming Provision. Clearly the draftsman had an obligation to enact the relevant EU law which is now contained in Article 26.1(a) Directive 2006/112/EC (previously Article 6.2(a) Directive 77/388/EEC.); we shall use the “old Sixth Directive” references in the remainder of this commentary because they were extant at the time the relevant UK provisions were enacted.

At first glance Article 6.2(a) does not shed any further light on the meaning and purpose of The UK Deeming Provision because it merely states that the application, by a taxable person, of his business assets to a non-business use is a supply for a consideration and makes no reference to a charge or consideration or the lack of either. However, by reference to the general principles of the tax (for these purposes established by the interaction of Article 5, Article 6 and Article 11) we know that “*any transaction which does not constitute a supply of goods*” is a supply of services the taxable value for which is “*everything which constitutes the consideration which has been or is to be obtained by the supplier*”. Article 2 emphasises this point further by stating that “*the following shall be subject to value added tax .... the supply of ... services effected for consideration*”. Thus against this background it is arguable that Article 6.2 merely sought to bring within the scope of the tax those transactions which would not otherwise have been taxed under the general principles of the tax. This interpretation is supported by the preamble to Article 6.2 which states “*The following shall be treated as supplies for a consideration*”. Put simply why did Article 6.2 need to specify something as a supply for consideration if it was already a supply for a consideration? It could, of course, be argued all the provision did was to state that the supply was one of services. However, this interpretation does not seem to hold much water because the use of an asset does not involve “*the transfer of the right to dispose of tangible property as owner*” and thus the said use was already a supply of services under the provisions of Article 6.1. The logical conclusion must be that Article 6.2(a) sought to tax things done for no consideration and by extension that logic should apply to The UK Deeming Provision.

Sadly the position is not beyond doubt because Article 6.2(a) makes no reference to consideration (or the lack of it). However, its “sister” provisions namely Article 5.6 and Article 6.2(b) help (a little) by stating that the relevant “deemed” supplies occur when the relevant transaction is undertaken “*free of charge*”. It is perhaps important at this juncture to draw a distinction between “a charge” and “consideration” as this may explain why the European draftsman used the different terms. Generally, of course, different terms suggest different meanings / purpose. In the opinion of the editor “consideration” will always constitute “a charge”. However, “a charge” may not always be “consideration” in a VAT context. Certainly a “nominal charge” seems to lack the nexus with the thing done to be considered consideration for VAT purposes. Put simply consideration must be directly, causally and quantifiably linked to the thing done (see *Tolsma*). However, consensual agreement between the supplier and the customer about the subjective value of the supply / consideration is generally sufficient to satisfy the criteria for VAT purposes.

With those general points made let's return to Paragraph 1A (1) of Schedule 6 VATA 1994 and the *Lookers* case. There are two critical parts to Paragraph 1A (1) of Schedule 6 VATA 1994. Put simply a direction to use Open Market Valuation is triggered, inter alia, by (a) supply under The UK Deeming Provision (i.e. condition 1A(1) (d)) and (b) where that supply is made for a consideration below its Open Market Value (i.e. condition 1A(1)(a)). The critical questions can therefore be summarised as follows and we shall address each of these in turn:-

1. Was the £1 annual charge for private use consideration?
2. If the £1 annual charge was not consideration then can all the conditions of Paragraphs 1A (1) of Schedule 6 VATA 1994 be met?

3. If on the other hand the £1 annual charge was consideration then can there be a supply under The UK Deeming Provision

Was the £1 annual charge for private use consideration?

There are competing arguments here. On the one hand the consensual agreement between the parties suggests there was consideration. However, on the other hand, Paragraph 1A (1) of Schedule 6 VATA 1994 is drafted on the basis that the "connection" between the supplier and his staff means that the relationship between them excludes the possibility of normal commercial relationships. By logical extension this suggests that the £1 charge was not / could not be established by consensual agreement. Outside such an agreement the nominal nature of the £1 looks to fail the nexus test for consideration.

The Tribunal's decision relating to the time of supply under Regulation 81 could arguably be supported by a lack of consideration, i.e. the payment (lacking the required nexus) was not made in respect of the supply and thus could not accelerate the tax point for the supply. However, in the editor's opinion s6(14) effectively carves out specific tax point rules for certain types of supply and thereby creates the VAT equivalent of "oil and water". Put simply once caught by the provisions of Part XI of the VAT Regulations the relevant supplies are unaffected by the provisions of s6 and vice versa.

On the balance of probabilities the editor considers that there was no consideration paid in respect of the private use. Whilst these arguments were made before the Tribunal they were made in isolation of the relevant EU law which as detailed above gives some further guidance to The UK Deeming Provision.

If the £1 annual charge was not consideration then can all the conditions of Paragraphs 1A (1) of Schedule 6 VATA 1994 be met?

On the basis of the above conclusion the answer has to be no because condition 1A (1)(a) is not met.

If on the other hand the £1 annual charge was consideration then can there be a supply under The UK Deeming Provision

For the reasons stated above the editor considers that The UK Deeming Provision's purpose is to tax supplies that would otherwise escape taxation for lack of consideration. Therefore, in circumstances where consideration is paid the resulting supply of services is made under s5(2)(b) VATA 1994 not The UK Deeming Provision. It should be stressed that this construction of the UK Law is based on the construction of the corresponding EU Law.

For the sake of completeness reference should be made to the wording of s5(1) VATA 1994 which states "*Schedule 4 shall apply for determining what is, or is to be treated as, a supply of goods or a supply of services*". Viewed in isolation that is to say as something which merely categorises supplies (assuming one exists in the first place) as one of goods or one of services and nothing more (i.e. not something that creates or deems a supply) there is support for the Tribunal's decision. However, for the reasons stated the editor considers that The UK Deeming Provision is a deeming provision designed to create a supply where one would not otherwise exist.

Finally did the last part of Article 6.2 which stated the following give the UK some powers to derogate from what the editor considers was the stated objective of that provision?

*"Member States may derogate from the provisions of this paragraph provided that such a derogation does not lead to distortion of competition"*

The editor considers that "all" these powers allowed the UK to do was to choose not to create a deemed supply in the circumstances specified in Article 6.2.

## Summary and Conclusions

For the reasons stated above it seems impossible to satisfy condition 1 A (1) (a) and condition 1 (A) 1 (b) at the same time. As this is a requirement of Paragraph 1A(1) of Schedule 6 VATA 1994 the conditions necessary for a direction cannot have been satisfied.

However, the payment of consideration in respect of supplies within Regulation 81 cannot accelerate the tax point.

## ECJ Diary

There are no Indirect Tax cases at the ECJ this week.

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