



# KPMG's Indirect Tax Update

TAX

## Highlights

The top story this week is of course the long awaited *My Travel* Tribunal case, which examined whether My Travel was able to deduct input tax it had claimed on fees paid by it to a professional firm. HMRC argued that My Travel had merely paid the fees, but that the supplies in question, were made to the banks and other institutions involved in the financial rescue package designed to save My Travel's business from closure. HMRC argued My Travel could not therefore claim this VAT, and that the lenders could not claim the VAT either as they had no invoice made out to them, and in any case the VAT would only have been attributable to exempt loans.

In finding for My Travel the Tribunal applied propositions previously set out in *Redrow*, *WHA* and *Loyalty Management UK*. My Travel was a party to the relevant (tri partite) engagement with the adviser. It requested the viability/refinancing review, authorised the adviser to do the work, and promised to pay for it. It needed the work to be done if the business was to continue so the work was used for the purpose of the business. It had involvement in deciding who was appointed. It received a copy of the report. All this confirmed that My Travel received the services. As it used them for its taxable business, VAT deduction was permissible.

Both sides proceeded on the basis that *LMUK* was good law, despite the ECJ referral by the House of Lords, which may call the *Redrow* principle into question.

In this Tribunal case there was only one supply of services, which meant it was different from *Redrow*, where the estate agents supplied normal marketing services to the householder who was going to buy a Redrow home. The Tribunal agreed with Redrow that it would provide those services without charging the householder, which benefitted Redrow's business as it would then sell new houses. However in both *WHA* and *LMUK* it was accepted that the same supply of services could be made to two recipients, (or supplied to one and provided to another) and it was the one who paid that obtained the input tax deduction, if he received a benefit in the course of business from the work.

My Travel was only able to secure this deduction because it did receive the supply – it did not argue that just paying for it was enough. However the primary right of the payer to secure input tax deduction where there are two recipients of the supply, and the suggestion that input tax deduction is in some way dependent on having paid the VAT in question do perhaps lead us inexorably to other scenarios where these fact patterns are not on the face of it replicated, and to wonder what impact these cases might have on these. Are these cases only relevant where there are in fact joint recipients? How do you determine if there are joint recipients? Surely it must still be possible to receive a supply, and to claim input tax under the normal rules, even if you do not pay for that supply.

Contents:	Page
From the Tax Authorities	2
EU News	3
UK News	4
News	4
In the Courts	4
ECJ Diary	6

Otherwise where is the fiscal neutrality, if the payer is also denied recovery as non recipient? Where is the line drawn between genuine third party consideration and jointly received services, as generally things a business pays for which might have previously been viewed as third party consideration will nonetheless secure some benefit for that business (such as a tenant paying the landlord's costs of amending a lease). Is the lack of any contractual ties between payer and supplier the fact that determines what is third party consideration as opposed to one party paying for supplies made to two? Certainly arrangements should be structured where possible so that, as in *My Travel*, the person who pays for a jointly received supply is always the one in the best position to claim the VAT on it, i.e. the one who uses the service for a business purpose and can relate it to taxable and not exempt supplies. It remains to be seen whether HMRC appeal, but if they do not, much of their guidance on viability studies would seem in need of review.

In the *DFS* decision we again saw the Tribunal considering whether an exempt supply was being made, when looking at input tax attribution on advertising costs and deciding if there was a sufficient link between the input tax and exempt insurance intermediation income to make the VAT residual rather than wholly attributable to the taxable sales of the advertised sofas. The adverts made no mention of insurance (you may remember the content of the adverts was a key factor in the similar *Skipton* decision decided some weeks ago – if the adverts did not mention exempt activities the Tribunal could not see how the advertising costs could be linked to those exempt activities). The Tribunal was content that not everyone who bought a sofa from *DFS* would even be offered insurance let alone buy it. One type was only relevant to fabric sofas and the other was only relevant if the sofa was bought on credit terms. This meant the link between the VAT and exempt income was not sufficiently direct and immediate to make the advertising costs residual as various contingencies could interrupt the progression from advert costs to exempt income, and *DFS* won its case. This whole concept of input tax attribution, identifying if input tax is a cost component of one or more supplies and whether there is a direct and immediate link from the VAT to one or more supplies is a really hot topic at the moment and the recent *Garsington* Brief shows that HMRC are taking quite a hard line.

The Brief on postal services post *TNT* suggests that, as expected, there will be no immediate change to the UK's rules on Royal Mail's postal services exemption. The difficulty will undoubtedly be in deciding what contracts have been individually negotiated by Royal Mail and hence are not provided under universal service terms and thus are not exempt.

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

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

## From the Tax Authorities

### Revenue & Customs Brief 64/09 – VAT treatment of postal services: decision of the European Court of Justice in the case of TNT Post UK Ltd

HMRC have released a Brief on the VAT treatment of postal services following the ECJ decision in the *TNT Post UK* case. This case, referred from the High Court examined the scope of the UK's exemption for public postal services. In the UK the conveyance of postal packets and any services in connection with that supply is exempt when supplied by the 'Post Office company' (Royal Mail). Whilst the exemption is not limited to the universal service provider, it is only Royal Mail who can currently benefit from the exemption. TNT argued this gave Royal Mail a competitive advantage when it came to pricing commercial contracts. In delivering its Judgment back in April, the ECJ concluded Royal Mail's exemption is too widely drawn as the public postal services exemption does not include supplies made by Royal Mail under individually negotiated commercial contracts.

The Brief confirms that in the UK, the application of the exemption provided under European law is limited to Royal Mail and other postal operators are required to charge VAT at the standard rate on their services. The Brief goes on to say that whilst the ECJ confirmed that Royal Mail is the only postal body eligible to exempt postal services the exemption does not apply to supplies made by Royal Mail for which the terms have been individually negotiated. The Brief therefore confirms that some postal services which are individually negotiated or not subject to any price and regulatory control will become liable to VAT.

The Brief finishes by merely confirming that HMRC are currently in discussions with Royal Mail to establish precisely which of their services will be affected and that any changes will be implemented from a future date.

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

### **Notice 732 Annual Accounting**

This Notice, which cancels and replaces Notice 732 (April 2006), explains the annual accounting scheme, who can use it and how to apply to join. It has been revised to improve clarity, including: new paragraphs to explain how to make balancing payments; information about leaving the scheme; what happens if you deregister; and where to send your application form.

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

### **Tariff Notice 19/2009**

This notice alerts importers to the fact that some EC member states are classifying certain glass television stands in different ways. Click [here](#) to read the notice.

### **Tariff Notice 20/2009**

This notice concerns the customs classification of a certain type of 'thong' sandal. Click [here](#) to read the notice.

### **Tariff Notice 21/2009**

This HMRC Tariff Notice concerns the classification of certain footwear. Click [here](#) to read the notice.

### **Recent JCCC (09) Paper**

HMRC has released the following JCCC Customs Information Paper:

[70](#) Withdrawal of inward processing (drawback) using a simplified authorisation.

## **EU News**

### **Commission conference on taxation for the low carbon economy**

The European Commission has organised a one day conference entitled 'What taxation for a low carbon economy?' The event will be held on 30 November 2009 in Brussels. The conference says it will concentrate on the role of taxation when it comes to cost-effective ways of reducing emissions outside the EU Emission Trading System. For further details of the conference please click [here](#).

### **UK and Sweden apply for extension of 'cash accounting' – UK requesting increase to £1.5 million**

Currently Sweden and the UK both allow businesses to account for VAT under cash accounting where turnover is below a certain threshold (SEK 3 million and £1.35 million respectively). The cash accounting scheme is an optional simplification for small businesses. It allows them to use date of payment to determine when output tax is due and input tax can be reclaimed. The previous derogation from Article 167 which was granted under Council decision 2007/133/EC expires at the end of the year. Sweden is requesting an extension to their derogation and the UK are also requesting an increase to £1.5 million. To read the proposal for the derogation click [here](#).

## UK News

### VAT Online Services events

HMRC have announced a number of events regarding the electronic submission and payment of VAT returns. During the events HMRC will show businesses how to enrol for VAT Online and other online services and where to get help and support. HMRC are planning to phase out paper VAT Returns from 1 April 2010 when businesses with an annual turnover of £100,000 and all newly registered VAT businesses, will be required to file returns online and make payments electronically. The news release confirms paper returns will remain for other businesses but will be reviewed in the run up to 2012. To read the news release in full click [here](#).

## 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

### UKFTT 256 My Travel Group Plc - who received advisory services provided – taxpayer win

The Tribunal has upheld My Travel's appeal. The main issue under dispute concerned the nature of the recipient of some advisory services provided by another Big four firm. My Travel was having financial difficulties and needed to restructure its borrowings. Naturally any prospective lender requires information before deciding whether to lend and on what terms. The adviser in My Travel set up a tri partite arrangement whereby My Travel was a party to the engagement and the fee note was made out to it rather than to the bank(s) for settlement by My Travel. Using the *Redrow* concept the argument was that My Travel was a party to a contract whereby it paid for a viability service to be supplied to it and the banks, and that service was received by My Travel and incurred primarily for My Travel's business purpose so it could continue to trade and make taxable supplies, so My Travel, as payer, could claim the VAT. HMRC argued that the supply was made to the bank(s) using the normal tests of supply and was a cost of making exempt supplies of loans hence irrecoverable. Any benefit to My Travel was ancillary and it merely paid the fee for a supply to another, so could not claim the VAT.

MyTravel is one of a number of cases relating to input tax recovery in the context of restructuring and deal fees and the long awaited BAA case is also expected shortly.

Click [here](#) for the case in full.

## UKFTT 204 DFS - advertising costs are a cost component of sales – tax payer win

The hearing took place from 11 to 19 May 2009 before Judge Charles Hellier and John Robinson in the London Tribunal Centre.

### Background

DFS is a well known supplier of sofas (the term sofas encompasses the variety of types of upholstered sitting furniture which DFS supplies). If a customer goes to a store and decides to buy a sofa then he may be offered, and he may agree to take one of two types of insurance. The first type is anti-stain insurance which is only offered to customers after they have made the decision to buy a fabric covered sofa. The second type of insurance is Payment Protection Insurance and is only offered to customers who bought a sofa on interest free credit terms. The issue concerned whether advertising costs were residual or fully recoverable.

None of the advertisements made any reference to any form of insurance. All advertisements contained DFS's logo and generally the catch phrase "think sofas, think DFS". All advertisements displayed pictures of sofas. The Tribunal accepted that the success of the marketing campaigns was measured by comparing relative values of sales by type of sofa in periods before, during and after the campaign. If during a campaign the sales of a featured model did not go up, then that model would be dropped.

### The Tribunal's findings

The Tribunal found that the advertising costs had a direct and immediate link to the taxable sales of furniture but that no direct and immediate link was present in relation to the exempt insurance intermediation income.

In reaching its conclusions, the Tribunal gave a lot of consideration to whether the cost of advertising is a cost component of the sales of sofas or the provision of intermediation. If it is not a cost component of either of the two, then it will fall into the overheads pot. The Tribunal considered that the correct test for determining the cost component question is, by reference to the activity of making the sales rather than to what is sold. On this basis the Tribunal concluded that the costs of advertising are a cost component of the activity of supplying sofas. The following reasons were given for this conclusion:

- The adverts are directed at the sale of sofas. There is nothing in the nature of the business of the Appellant which suggests that this is not an object of the advertising.
- The very fact that the Appellant, a commercial enterprise selling sofas incurs very considerable expense in placing adverts which are directed at the sale of sofas indicates objectively that the adverts are directly linked to the selling, and the costs of the adverts are directly and immediately linked to the sales activity: no enterprise would incur such costs if they were not for the sales activity.
- The link between advertising and the sales activity is free from any intermediate steps and is directly rather than indirectly connected to and bound up with that activity.

The Tribunal having reached a conclusion on the cost component issue proceeded to consider separately the issue of direct and immediate link. The Tribunal's view was that there is a link between the advertising and the intermediation. The issue however, is whether that is a direct and immediate link. The existence of a direct and immediate link to the selling of the sofas does not in itself prevent there also being a direct and immediate link to the intermediation making the VAT residual.

The Tribunal distinguished the case of *Dial-a-phone* (DAP) and held that the intermediation provided by DFS took place after, and was less commercially important than, the primary sales activity. In *DAP* the advertisements mentioned free insurance. Thus the adverts could be seen to be clearly linked to the subsequent 'paid for' insurance and indeed DAP acted as insurance intermediary throughout in respect of both the free and paid for contracts. The Tribunal held that the approach that they have taken is not inconsistent with the approach of the courts in *DAP* in particular the fact that it regarded the effect of the advertisement as relevant to the objective determination of how the advertising costs are utilised. However, the Tribunal concluded that though there is a link between adverts and intermediation in DFS's case it is not as clear and as close as it was in *DAP* and "not sufficiently close to be a direct link". The sales process in *DAP*, led seemingly unavoidably in each customer's case to the question of insurance. In DFS's case there are contingencies in the process which interrupted the link: PPI is only relevant if credit is taken and anti stain insurance is only relevant to fabric covered sofas. Those contingencies result in a large proportion of sofa sales being made without any intermediation activity.

Importantly, the Tribunal rejected the Commissioners' argument that the effect of the adverts was to get people in the stores to buy insurance. (That is because the stores were plainly places where people were to be sold sofas). Going to a store was necessary to buy a sofa from DFS: it was merely a step in the process of buying a sofa. And going to a store enabled insurance to be sold only if a sofa was bought first.

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

## ECJ Diary

Next weeks cases are below. Please note the eagerly awaited *AB SKF* (C-29/08) Judgment is the following week and will be delivered on 29 October.

### Thursday 22 October

#### **Judgment - Swiss Re Germany Holding (C-242/08) – Whether transfer of re insurance contracts was exempt or taxable**

In the Opinion the AG concluded that the transfer of 195 re insurance contracts from an insurance company in Germany to an associate insurance company in Switzerland, some for a negative consideration, is not an exempt supply of insurance, but is a taxable supply of services, supplied where the supplier belongs (current default rule for services). The referring German court had already concluded this could not be a transfer of a business as a going concern (TOGC) as there was no "transfer of an independent part of an undertaking, including tangible elements and, as the case may be, intangible elements which together, constitute a part of an undertaking capable of carrying on an independent economic activity". So the AG was simply considering whether the supply was goods or services and whether it was exempt or taxable and where it was supplied. To read the opinion click [here](#).

#### **Opinion - Commission v Ireland (C-221/08), Commission v Austria (C-198/08) and Commission v France (C-197/08) – Minimum price on cigarettes infringes community law – Excise Duty should be used to reduce consumption**

This case concerns Infringement proceedings against Ireland, Austria and France for the practice of fixing minimum prices on cigarettes. The Commission believe that such fixing of minimum prices infringe Community law, distort competition and benefit only manufacturers, by safeguarding their profit margins. To achieve the objective of reducing tobacco consumption, the Commission advocates increasing the excise duty on cigarettes. To read the Commissions earlier press release on the Infringement proceedings click [here](#) and [here](#). To read the applications in full click [here](#), [here](#) and [here](#).

#### **Hearing - Alstom Power Hydro (C-472/08) – Whether a time limit can be applied to carried forward VAT repayments**

This case asks whether it is contrary to Article 18(4) of the Sixth directive for domestic legislation to lay down a limitation period of three years for the exercise of the right to recover sums of VAT overpaid. Article 18(4) provides that where input tax exceeds output tax Member States may set down conditions to carry forward or repay the amounts. To read the question referred in full click [here](#). It does seem bizarre that we are still seeing cases about limitation periods and presumably the ECJ will say as it has always done, that where they relate to the time allowed to exercise the right to deduct they are fine as long as they are implemented properly. However if the case is about limiting the life of the right to deduct, once it has been exercised, it would seem difficult for the ECJ to support any time limit as this is a completely different point. Clearly indefinite carry forward of a VAT excess is not practical, but if the VAT can not be offset after a certain time, it should surely be refunded to the taxable person, not lost.

Your name and contact details have been recorded on a database by KPMG LLP (UK) in order to provide you with this newsletter. This database is accessible to KPMG LLP (UK) partners and staff in order to check appropriate clients are receiving the newsletter and to update/amend entries. If you do not wish to receive the newsletter and would like your name and contact details removed from this particular database, please send an e-mail to [jonny.morton@kpmg.co.uk](mailto:jonny.morton@kpmg.co.uk). If you wish to correct any details, please e-mail [jonny.morton@kpmg.co.uk](mailto:jonny.morton@kpmg.co.uk). The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.

The electronic version of KPMG's Indirect Tax Update contains hyperlinks to Web sites which are independent of KPMG LLP (UK) and over which KPMG LLP (UK) has no control. To the fullest extent permitted by British law, KPMG LLP (UK) will not accept any responsibility or liability for the content of any such other Web sites or for any consequences.