

## **UK VAT**

### **UK granted derogation on charges made by motor dealers to staff for the use of cars**

The UK has been granted a derogation allowing it to apply the open market value to charges made by motor dealers to staff for the use of cars in respect of which the dealer has obtained full input tax recovery (i.e. cars which are stock in trade of the dealer). This is the derogation which authorises the changes introduced in this year's Finance Act to block the planning arrangement whereby, if a nominal charge for the stock in trade car was made to the employee, output tax was only due on the actual amount. Customs now have the power to issue an open market value direction. The derogation was applied for in February 2004, agreed on 21 Oct 2004 and expires on 31 December 2009. The text of the derogation is in the Official Journal of the European Union.

## **Customs**

### **Withholding repayment of input tax**

UK Tradecorp bought goods in the UK and exported them (some supplies were to other EU countries, but most supplies were exports to countries outside of the European Union). The company was therefore usually in a repayment position at the end of every VAT period. There was a suspicion of missing trader fraud: Customs were concerned that some of the traders who had imported the goods subsequently exported by Tradecorp had failed to account for output tax. Customs were not suggesting that Tradecorp shared any improper motive with the missing traders, but they withheld payment of Tradecorp's input tax claims pending investigations. These investigations sometimes took in excess of eight months, and Tradecorp was therefore denied access to the funds held by Customs as its input tax. The company was obliged to borrow money in order to pay its trade creditors and had no remedy against Customs other than judicial review.

Initially on its application Tradecorp sought declarations that the period taken by Customs to reach decisions on its claims to recover input tax and the manner in which Customs conducted the investigation breached the principles of the Sixth VAT Directive. No claim was made for any relief other than such a declaration, i.e., no claim was made for interest, or any damages or compensation. However, in the course of the hearing Tradecorp "sensibly and properly" (the judge's words) dropped its claim that Customs had breached any of the principles of the Sixth Directive.

Instead, Tradecorp sought declarations to the effect that in verifying Tradecorp's claims for input tax Customs were under a duty to act proportionately and in failing to pay interest at London Inter Bank Offered Rate in respect of the period between the accrual of the claimant's right to input tax and actual payment of that input tax they were not acting proportionately.

Perhaps the most interesting and concerning part of the decision is one which may be a point of discussion for some time – the last two paragraphs. First of all, however, Mr. Justice Lightman set out some factors which need to be taken into account when investigating a claim to input tax and the relevant interests which need to be balanced, e.g., the need to protect the Revenue, the likely outcome of the investigation, the effect (if any) of withholding funds on the trader and his business and the representations made in this regard, the nature and complexity of enquiries necessary to verify the claim, whether either Customs or the taxpayer have contributed to any delay in the verification process, whether an interim / part / full repayment should be made ahead of the conclusion of the investigations (bearing in mind the taxable person's track record), whether there is any scope for judicial review of Customs' conduct, and whether there is any recompense for delay in repayment. However, as mentioned it is the last two paragraphs which are worthy of attention.

In the final two paragraphs, Mr. Justice Lightman held that the absolute obligation to pay interest from the date of a repayment claim to the actual repayment does not arise from the doctrine of proportionality (which he accepts...). In fact, he goes so far as to state that it is scarcely consistent with the principle of proportionality, given that national VAT authorities are bound to investigate and defer payments of claims to refunds and irrespective of the reasons for any delay in the conclusion of the investigation and

accordingly payment, even if the reason is the deliberate obstruction of investigations by Customs. Further, he states: "The principle of fiscal neutrality of VAT does not, as it seems to me require (if it extends to payment of interest at all) payment of interest in respect of the period prior to the acceptance or establishment of the right to deduct and repayment." Mr. Justice Lightman did accept that Community law may require payment of interest if repayment is wrongly deferred from the date that the claim has been accepted or established, but it does not oblige Member States to pay interest on repayments of input tax from the date of the making of the claim to repayment.

This is in line with the UK statutory position under s.78(1)(d). Therefore it would appear the taxpayer's only recourse is either to repayment supplement under s.79 if Customs' investigation is unreasonable on a subjective analysis, or, potentially, a common law claim for damages. It is understood that this issue is currently the subject of a reference to the ECJ in *Teleos* (in which the claimants argued that their right to property under Article 1 of the First Protocol to the European Convention on Human Rights was breached (the claimants argued that their right to recover input VAT constituted a possession within the meaning of Article 1 and Customs' infringement upon this right was based on provisions which lacked legal certainty). No doubt a ruling from the ECJ will provide more clarity.

