

**VAT credit notes**  
***Brunel Motor Company Limited***

The Court of Appeal (CoA) has unanimously directed the case be remitted back to the Tribunal and reheard. The issue under dispute concerned the validity of credit notes, issued by Ford to Brunel Motor Company (a Ford car dealer) in respect of certain vehicles supplied on a 'dealer sold' basis that Brunel had not paid Ford for. Ford and HMRC submitted they were, Brunel argued they were not. Brunel was in receivership and wished to retain the input tax credit it had claimed on the vehicles, (insolvent bodies are by concession not required to repay to HMRC the input tax incurred pre insolvency, on unpaid purchases over six months old) but if the credit notes were valid it lost that entitlement as the supply of the vehicles would be deemed never to have happened. The Tribunal and High Court found for Ford and HMRC that the credit notes were valid. Brunel appealed.

'Dealer sold' meant that Ford would issue VAT invoices for the cars but retain title to them until full payment was made: payment was not due until the first of certain events occurred. Here the event that triggered payment falling due was Brunel becoming formally insolvent.

Essentially as soon as Brunel went into receivership it became liable to pay for these cars immediately and the supply agreement also terminated. As Brunel could not pay, it should have returned the cars to Ford, and if Ford had been unable to sell them to someone else for the same price then Ford had the right under the agreement to pursue Brunel for any shortfall. However the receivers needed stock to trade with and to generate income and wanted to avoid creation of any potential shortfall claims by Ford.

Ford repossessed the unpaid cars. The credit notes were to reflect that repossession, as a retention of title clause does not mean the goods were not supplied for VAT purposes. However Ford then re-issued new tax invoices to sell the cars back to Brunel again, at the same price, so the cars never moved location. This later sale took place after the date the receivership period began. This was effectively an unwritten variation to the terms of the supply agreement. Brunel argued that the cars had been supplied to it by Ford and that original supply had not been cancelled nor had the price changed, so the credit notes were invalid. Ford and HMRC argued that the credit notes had to be given effect.

The lead judge in the CoA said the taxable consequences of the original supplies of vehicles by Ford to Brunel can only be discharged by some subsequent contractual rescission or novation which is evidenced by the credit notes. He then went on to query whether the comment by the High Court judge that "the parties have, in effect, agreed that the Supply Agreement should come to an end on the basis that it was rescinded" was justified. The Tribunal's primary findings of fact did not justify that conclusion – the CoA judge concluded that they are equally consistent with

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findings of unilateral conduct of Ford in repossessing the vehicles and issuing credit notes to which Brunel submitted because it had neither the power nor the commercial incentive to do anything else. On that basis the judge concluded the appeal should be reheard as the Tribunal had asked itself the wrong question and the High Court could only look at points of law. However he did not specifically conclude that the credit notes were invalid or ineffective, as Brunel were contending. The case would need to be heard again on the correct basis to decide that. The other judges concurred.

The CoA judge's analysis of 11 C 1 of the Sixth Directive (below – emphasis added) about when the VAT amount can be varied is interesting.

“Article 11 C 1 is applicable to 'cancellation' or cases where 'the price is reduced after the supply takes place'. It seems to me to be axiomatic that such cancellation or reduction be pursuant to some legal entitlement whether arising from or conferred by the original contract of supply or subsequently; otherwise VAT would be a voluntary tax in every sense of the word. The legal entitlement might take the form of a remedy, such as rescission for mistake or misrepresentation, a right under the original contract to return the goods in certain specified events or a subsequent agreement discharging the original contract. To the like effect is the definition contained in Regulation 24. That requires that there shall be 'a decrease in the consideration due'. The word 'due' clearly connotes some legal entitlement to the decrease. Such entitlement may arise either from a term of the original contract of supply, see *Commissioners of Customs & Excise v General Motors Acceptance Corporation (UK) plc* [2004] STC 577, or under some subsequent rescission or novation. Regulation 24 makes it clear that the credit note is not of itself sufficient to justify a decrease, it is only evidence of an entitlement to the decrease”.

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