[2021] UKFTT 0307 (TC)

TC08249

VALUE ADDED TAX – decision on one issue in the appeals (interest) – amounts paid by HMRC to appellants as bad debt relief under section 36 Value Added Tax Act 1994 – whether interest should be paid on such amounts by HMRC from date of entitlement (rather than date of claim) – section 78 Value Added Tax Act 1994 – error on the part of HMRC – invalid statutory condition was not an error by HMRC – statements in HMRC Notices were errors by HMRC – Found: statements in Notices were not the cause of outcomes required in s78(1) – s78 not satisfied – EU law principles considered – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal numbers: TC/2016/03110
TC/2010/09116

BETWEEN

HBOS PLC
LLOYDS BANKING GROUP PLC **Appellants**

-and-

THE COMMISSIONERS FOR
HER MAJESTY'S REVENUE AND CUSTOMS **Respondents**

TRIBUNAL: JUDGE ZACHARY CITRON

The hearing took place on 24-27 May 2021. The form of the hearing was V (video) on the Teams platform. A face to face hearing was not held due to the pandemic. The documents to which I was referred were an electronic hearing bundle of 184 pdf pages and an electronic authorities bundle of 2,056 pdf pages. The parties' statement of agreed facts and issues and position on Brexit was sent to the Tribunal on 15 June 2021.

Prior notice of the hearing had been published on the gov.uk website, with information about how representatives of the media or members of the public could apply to join the hearing remotely in order to observe the proceedings. As such, the hearing was held in public.

Ms A Brown QC, instructed by KPMG Law, for the Appellants

Ms E Mitrophanous QC, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION ON THE "INTEREST" ISSUE IN THE APPEALS

INTRODUCTION

1. The brief background to this hearing was that

   (1) until 1997, the UK legislation providing VAT refunds for bad debts contained a condition of entitlement that, in a Court of Appeal decision in 2016, was found to be invalid under EU law principles;

   (2) in 2007 and 2009, the appellants made claims for bad debt refunds on supplies made in the period 1989-1997 – the condition in question was not satisfied and for that reason HMRC initially rejected the claims;

   (3) HMRC eventually paid those bad debt refunds to the appellants, in 2019;

   (4) HMRC also paid interest on those refunds from the dates the refunds were claimed, on the basis that there had been an error on HMRC's part in not paying the refunds upon the making of the claims;

   (5) the issue in the hearing was whether HMRC should also have paid interest from earlier dates, being the dates when all conditions for the refunds, apart from the invalid condition, had been satisfied.

2. References in this decision

   (1) to sections (or "s") are to sections of Value Added Tax Act 1994 (unless otherwise indicated);

   (2) to regulations are to Value Added Tax Regulations 1995 SI 1995/2518 (unless otherwise indicated);

   (3) to Articles are to articles of Council Directive 2006/112/EC; and

   (4) include the statutory predecessor of the provision referred to (as explained in the summary of legislation in the appendix to this decision).

THE APPEALS

3. The appeals were brought in respect of HMRC's decisions to refuse to pay refunds considered due to the appellants relating to bad debts on supplies made in the period 2 October 1978 to 19 March 1997 in the case of the second appellant and for the period 1 April 1989 to 19 March 1997 in the case of the first appellant.

4. Claims for the period 2 October 1978 to 31 March 1989 related to the 'old regime' for bad debt refunds enacted, first, under s12 Finance Act 1978 and, subsequently, from 26 October 1983, under s22 Value Added Tax Act 1983. The 'old regime' was repealed by s39(5) Finance Act 1997. These periods were not in issue in this hearing.

5. Claims for supplies made in the period 1 April 1989 to 19 March 1997 were covered by the 'new regime' for bad debt refunds enacted under s11 Finance Act 1990 and re-enacted with amendments under s36.

6. I was told that other issues in the appeals, apart from the interest issue summarised above, had either been agreed or were stayed behind other cases.

RELEVANT LEGISLATION

7. Relevant legislation is set out or summarised in the appendix to this decision.

ISSUES BEFORE THE TRIBUNAL AND TRIBUNAL'S JURISDICTION

8. The "agreed" issue was whether interest was due from

(1) (as HMRC contended) the respective dates of claim (such interest having already been paid); or

(2) (as the appellants contended) earlier dates (the "**earlier dates**"), being the dates on which the relevant returns (the "**earlier returns**") were made for the first prescribed accounting period following the date on which, in relation to a given supply (i) the "statutory waiting period" (this term is explained in the appendix) expired or, if later (ii) the consideration is likely to have been written off in the accounts (which the parties, if necessary, would seek to agree in the first instance on the basis of extrapolated data).

9. Expressed in terms of statutory provisions, this issue was:

(1) were s78(1)(c) or (d) satisfied on the facts of this case (it was common ground that s78(1)(a) and (b) were not satisfied)?

(2) if so, when did the "applicable period" begin?

(3) did s85A(2) apply?

(4) if so, what was the starting date for interest to run?

10. The parties were agreed that if I were to determine that interest ran from the earlier dates, I should not determine the quantum of that interest, but rather ask the parties to agree quantum (failing which, they could apply to the Tribunal for determination).

11. HMRC's further "issue for determination" was: whether the fact that, after the removal of the property transfer condition from 1997, an issue arose with HMRC about the attribution of consideration received as between the supply of the vehicle and the supply of finance, means that, even if HMRC do not succeed on their primary contention, interest was due from later dates than the earlier dates.

12. The Tribunal had jurisdiction as regards the liability of HMRC to pay interest under s78 and the amount of interest so payable (s83(1)(s)).

EVIDENCE

13. The hearing bundle contained Tribunal documents and correspondence between the parties; the authorities bundle contained a number of HMRC publications, as well as legislation and case law.

14. I had a witness statement, and heard oral evidence, from Andrew Plant, who, since 2008, had been a senior VAT manager in the second appellant's VAT team. He was responsible for the second appellant's bad debt refund claim in 2009. He had 30 years of VAT experience in the advisory profession and industry (Bass Plc, Woolwich plc, and BMW – which had a substantial finance business). He had regularly attended meetings (normally quarterly) of (and was for two periods the chair of) the VAT working group of the Finance Leasing Association (a leading trade body involving, amongst others, hire purchase businesses) since 2000. I considered Mr Plant to be a reliable witness as to facts of which he had direct knowledge; in addition, given his expertise and experience, I put weight, in making my findings of fact, on his general knowledge of in-house VAT departments at large businesses and banks in the periods of time relevant to the issues before the Tribunal.

15. I also had a witness statement from Mark Treacher, an indirect tax specialist at KPMG. Mr Treacher had been involved in preparation of the second appellant's bad debt refund claim in 2009; his statement concerned how that claim was prepared. Mr Treacher was not required by HMRC to attend the hearing for cross examination.

FINDINGS OF FACT

16. I make the following findings based on the evidence before the Tribunal and the ordinary civil standard of proof (balance of probabilities). Where the finding is based on contested or inconsistent evidence, I have given more detailed reasons for the finding.

The appellants & the bad debt refunds claims

17. At all relevant times the appellants' groups' businesses included provision of motor vehicles to customers by means of hire purchase ("**HP**"). In the ordinary course of that business, some customers defaulted on their obligations under the HP agreements to make payments; this gave rise to a right of the appellant (or relevant member of its group) under those agreements to terminate, repossess the vehicle and sell it; where the net sales proceeds were less than the sums due under the original agreement, the appellant (or member of its group) suffered "bad debts".

18. The appellants claimed refunds (the "**bad debt refunds**"), pursuant to s36, of amounts of VAT chargeable in relation to supplies made by them (or members of their groups) between 1 April 1989 and 19 March 1997 (the "**relevant years**") on 14 February 2007 (for the first appellant) and 31 March 2009 (for the second appellant) (the "**dates of claim**").

19. The bad debt refunds claims were initially refused by HMRC and the appellants appealed to the Tribunal (on 18 October 2007 (for the first appellant) and 1 December 2010 (for the second appellant)).

20. In February 2019 HMRC paid the bad debt refunds in the sum of £12,298,561.

21. Later in 2019, HMRC paid the appellants interest on the bad debt refunds from the dates of claim.

22. The appellants were representative members of large publicly-listed UK banking groups, with tax departments staffed with qualified tax professionals, including VAT specialists.

23. The first appellant's bad debt refund claim related to supplies by a group member, Capital Bank, that had been acquired in 1998. Capital Bank was an asset financing bank that financed the purchase of assets like cars. The VAT team at Capital Bank comprised two people who had specialist VAT knowledge and had previously worked at HM Customs and Excise.

The property transfer condition – supplies made in the relevant years

24. The UK statutes in force in respect of supplies made in the relevant years contained a condition (the "**property transfer condition")** of entitlement to bad debt refunds that in a case of a supply of goods, the property in the goods must have passed to the person to whom they were supplied. In supplies of vehicles under HP arrangements, the property transfer condition was not satisfied (due to retention of title).

25. In 2006, GMAC UK plc (which, like the appellants' groups, was in the business of providing motor vehicles to customers on HP terms) made a claim for bad debt refunds in relation to its supplies of motor vehicles in the relevant years. The claim was based on the direct effect of Article 90 and contended that the property transfer condition (inter alia) was incompatible with EU law. In *GMAC UK plc v HMRC* [2016] EWCA Civ 1015 the Court of Appeal held that the property transfer condition was not in accordance with the EU law requirements of appropriateness and necessity and fell to be disapplied.

26. Until the *GMAC* Court of Appeal decision, HMRC considered that the property transfer condition was legally valid in respect of supplies made in the relevant years; due to this mistaken understanding of the law, HMRC made the following errors:

(1) HMRC's Notice 700/18 *Relief from VAT on Bad Debts* (1991, 1996 and 1997 editions) included the property transfer condition in its bullet-point list of conditions for refund (as did News Release B5/96, released in 1996). Notice 700/18 also stated, under the sub-heading "What must I have before I can claim for a refund?":

> "If you supplied goods under a contract with a clause reserving title until they have been paid for (a Romalpa clause), and the goods have not been passed on with good title to a third party, you must send your customer a statement formally giving up your rights under the clause"

(2) HMRC rejected, and declined to pay, the bad debt refunds claims, until 2019.

27. *Revenue and Customs Brief 1 (2017): VAT – historical bad debt relief claims* announced HMRC's changed position on the legal validity of the property transfer condition following the *GMAC* Court of Appeal decision. It said that claims relating to supplies of goods in the relevant years would be paid subject to satisfactory evidence that the bad debts had occurred and that the VAT hadn't previously been reclaimed.

28. The reason the appellants (or members of their groups) did not claim the bad debt refunds at the earlier dates (or at any time prior to the dates of claim) was that, at those times, they considered the property transfer condition to be legally valid in respect of supplies in the relevant years, as it was set out in the UK statute. They thought it would be "non-compliant" to make bad debt refund claims on supplies in the relevant years when they did not satisfy the property transfer condition. They did not consider that EU law principles rendered the condition legally invalid, as they assumed the UK enacted the relevant EU directives correctly. The appellants changed their mind on these matters shortly before the dates of claim in part due to learning of the claims being made by GMAC and, following GMAC's claim, other taxpayers in similar positions to the appellants.

29. The foregoing is based on Mr Plant's evidence, in particular (and with more significant phrases in bold type)

(1) paragraph 24 of his witness statement, where he said it was unlikely

> "that a business would have challenged **the law where there was no obvious ambiguity**. The [bad debt refunds] **rules at the time were clear and unambiguous** as to the fact that a claim was prohibited where the supplier of goods had a retention of title clause. In particular, the **UK VAT law made it clear** that you could not claim [bad debt refunds] where the contract contained a retention of title clause."

(2) paragraph 25, where he said that "few taxpayers, regardless of their respective tax team's level of sophistication, would have challenged **the UK legislation** using EU Law rights. I am of the view that given the error in relation to [bad debt refunds] was an error of implementation of EU Law in the relevant period"

(3) paragraph 26, which stated:

> "In my view, it is not the role of the tax team, or the taxpayer, to challenge every inconstancy or possible error **in the UK VAT legislation**. As stated, the primary obligation of a taxpayer / tax team is making sure that the VAT return is accurate and complies with the **UK law at the time**. Indeed HMRC's ethos is, rightly, to ensure compliance: "right tax, right time" **by reference to the provisions of the domestic legislation**. In my view a taxpayer is entitled to take the position that the UK government assessed its obligations under the Directive and **enacted compliant legislation** such that meeting the requirements **imposed on us by that law** was what was required of us with

> HMRC bearing the responsibility (and cost vis a vis interest) where incorrect implementation led to circumstances in which VAT was over paid."

(4) in answer to a cross examination question about paragraph 25 of his witness statement and the extent of his knowledge of EU law, Mr Plant said:

> "I don't recall having that knowledge [of EU law]. **I recall having a knowledge of the UK law as it stood** with regards to retention of title and the prohibition of making bad debt relief claims, and that's why during that period I didn't make bad debt relief claims.

(5) the following exchange in re-examination:

> *Ms Brown QC*: "What impact did GMAC commencing its litigation have on the sentiment of taxpayers generally, in relation to this issue or other issues that GMAC litigated on?"
>
> *Mr Plant*: "Primarily, it would have raised awareness of the issues involved. So whereas on bad debt relief, for example, taxpayers, certainly those I had discussions with at the FLA, **had accepted the validity of UK law on the pre-97 claim, and hadn't thought to challenge the validity of that**. So it raised awareness. Also, given that GMAC were taking that forward as a lead case, it offered taxpayers a degree of protection from the cost, the reputational risk of taking litigation themselves, and so would have led to them submitting claims behind that."

30. One piece of Mr Plant's evidence, the following exchange during examination in chief, indicated a different reason for the appellants' omission to claim at the earlier dates, namely, HMRC's guidance:

> *Ms Brown QC*: "By reference to your experience at BMW and your knowledge of Lloyds since joining, do you know what caused Lloyds not to make the BDR claim earlier?"
>
> *Mr Plant*: "It was clearly stated in HMRC's guidance that we were precluded from making a claim where we had a retention of title clause. Given the nature of an HP agreement, where title is retained by the finance company until all the payments are paid, then we were not able to do that, nor from a risk perspective were we able to waive that retention of title, because we would always seek to repossess the asset where possible. You know, we had security over the amount loaned to the customer."

31. In my view, this last piece of evidence should be discounted because:

(1) it is a one-off that goes against the grain of his witness statement and other statements in oral evidence; and

(2) more fundamentally, it makes little intuitive sense, given that the appellants came to make claims at times when HMRC's publications continued to indicate that the property transfer condition was legally valid in respect of supplies in the relevant years; this fact, combined with the fact that the appellants were large banks with suitably staffed tax departments (see [22-23] above), indicates that the true reason for not claiming earlier was the appellants' belief that the property transfer condition was valid, rather than reliance on the contents of HMRC's Notice 700/18; such that, when, prompted by the actions of GMAC and other taxpayers, their views changed on the property transfer condition, they disregarded HMRC's publications in that regard.

Supplies made after 19 March 1997 & attribution of payments

32. Pursuant to s39(1) Finance Act 1997, the property transfer condition did not apply to supplies made after the end of the relevant years i.e. from 19 March 1997.

33. After this change in law, there was a period where HP-providing businesses discussed with HMRC the basis on which the quantum of bad debt refunds was to be determined, given the need to identify and attribute payments received between the taxable and exempt supplies arising under the HP contract. I make this finding based on Mr Plant's evidence.

34. Up to 1 January 2003, attribution of payments received under all agreements, including HP agreements, was governed by regulation 170, which imposed a "time" method of attribution.

35. Regulation 170A was introduced with effect from 1 January 2003. It provided for a "straight line" method of attribution for HP agreements.

36. On 6 December 2001 HMRC published *Business Brief 19/01 Bad Debt Relief on Goods Supplied by Hire Purchase or Conditional Sale*. It said this:

> ***"Attribution of payments in calculating entitlement to BDR***
>
> **Current policy**
>
> A purchase made by a customer of goods by hire purchase (HP) or conditional sale (CS) consists of two supplies for VAT purposes. There is a supply of goods (taxable) and a supply of financial services (exempt). The time of supply for goods is typically when they are made available to the customer (VATA 1994 s 6) and the time of supply of the finance (VAT Regulations 1995 reg 90) is when payment is made.
>
> Subject to meeting record keeping and timing conditions of the scheme, BDR arises when a customer defaults and the debt is unpaid. In determining how much BDR is recoverable, the supplier needs to allocate the payments received to the supply which occurred first (VAT Regulations 1995 reg 170(2)). In the case of HP and CS agreements, it will be the supply of goods that occurs first.
>
> The impact of these rules has meant that suppliers have been allocating all the payments received against the goods in the first instance and only to the finance after the goods have been paid in full .
>
> **Change in policy**
>
> While still believing the above analysis is correct in law, the Commissioners recognise that the outcome is not fair in relation to the commercial treatment of the transactions. Therefore with immediate effect, suppliers who make supplies under HP and CS agreements can apply the allocation rules set out in VAT Regulations 1995 reg 170(3). Now each payment can be allocated to interest and to goods in the same ratio as the total cost of the goods and total cost of the interest to the customer.
>
> For example, if a car cost 8,000 and the interest over the life of the agreement is £2,000, each payment can be allocated 80% goods and 20% interest.
>
> The Commissioners are currently considering whether a consequential amendment to the law is required to reinforce this new policy.
>
> …
>
> **Retrospective application of these new policies**

> Suppliers can re-calculate previous BDR claims by applying the new policies for the attribution of payments and of the treatment of repossessed goods and submit a voluntary disclosure. Any claim will be capped to three years starting six months from when the consideration was due and payable by the customer.
>
> Any suppliers who have not submitted any BDR claims can do so subject to being capped as above."

37. The second appellant started to make claims for bad debt refunds (in relation to supplies after the relevant years) on its VAT returns in around 2004. Prior to that, it made such claims otherwise than on its VAT returns, because of uncertainty about how the calculation should be made. I make this finding based on Mr Plant's evidence.

Methodology behind the bad debt refunds claims

38. The basis of the bad debt refunds claims was to extrapolate from known bad debt data for the period 2004 – 2007. The appellants identified the proportion of debts written off in the 2004 – 2007 period to determine a figure for the bad debt refunds on an annualised basis; that figure was then attributed to the relevant years. The reason for this approach was that, during the relevant years, the appellants' groups did not keep separate data for HP contracts (as opposed to other forms of asset finance) (the reason for this being that they had no reason to identify this data separately, as they thought, due to the property transfer condition, that they were not entitled to claim bad debt refunds for supplies during the relevant years).

Settlement agreement?

39. The parties did not come to an agreement in writing under the terms of which the decisions under appeal are to be treated as upheld without variation, varied in a particular manner, or discharged or cancelled.

40. Notice in writing was not given by HMRC to the appellants confirming that the parties had come to such an agreement otherwise than in writing.

41. These findings are based on the documents in the bundle; in particular, HMRC's letter to the second appellant dated 23 November 2018 which states HMRC's understanding that they would only enter into a s85 agreement if all matters were agreed (including as to claims prior to the relevant years, and interest); the second appellant's response dated 9 January 2019 suggesting that the principal issue be agreed by way of directions; and HMRC's response dated 30 January 2019 hoping that directions could be agreed; the trail then goes cold as regards a settlement agreement.

SUMMARY OF THE PARTIES' CASES

42. In terms of s78, the appellants' position was

(1) there had been an error on HMRC's part (in enacting and/or enforcing and/or providing guidance upholding the property transfer condition);

(2) that error had caused the appellants both

(a) to pay VAT which was not due (because they paid more VAT than they would have done had they claimed the bad debt refunds at the earlier dates (because if they had so claimed, the bad debt refund amount would have been set off against the VAT due)); and

(b) to suffer delay in receiving payment of the bad debt refunds (which became "due" to them at the time when the valid conditions of entitlement to claim were satisfied).

(3) hence, under s78 interest on the bad debt refunds should run from

(a) the date on which they paid the VAT that was not due; or

(b) the date on which HMRC would reasonably have authorised payment of the bad debt refunds, were it not for their erroneous position as regards the property transfer condition

43. HMRC's position on s78 was:

(1) whilst HMRC made an error in respect of their position on the property transfer condition,

(a) that error did not cause the appellants to pay amounts by way of VAT that were not VAT due

(b) the bad debt refunds only became due to the appellants upon their making claims; prior to that point, the bad debt refunds were not "due" the appellants;

(c) the appellants did suffer delay in receiving the bad debt refunds once they became due;

(d) the delay suffered by the appellants by reason of that error was the delay in accepting their claims for the bad debt refunds once they were made;

(e) hence s78 interest became payable from the dates of claim.

44. It was common ground that s78(1)(a) and (b) did not apply.

45. The appellants' alternative argument was that s85A applied.

46. HMRC's alternative argument was that, even if s78(1)(d) applied, the applicable period would not begin at the earlier dates, as it is likely that the claims for the bad debt refunds would not have been made for five to seven years because it is likely that the appellants would have delayed claiming whilst discussing attribution issues with HMRC (see finding at [33] above as regards discussions that took place following the change of law that removed the property transfer condition from 19 March 1997). The appellants said that the root cause of these attribution discussions was the property transfer condition. Had the property transfer condition never been enacted, the attribution issues would have 'played out' over the period 1978 to 1988.

Burden of proof

47. The burden was on appellants to show that s78 or s85A applied such that interest was payable on the bad debt refunds from the earlier dates.

PARTIES' AGREED POSITION ON LEGAL EFFECT OF "BREXIT"

48. The parties were agreed that:

(1) the appellants were permitted to invite the Tribunal to interpret the provisions of relevant UK legislation by reference to the general principles of EU law and by reference to retained EU case law on the basis that they began their appeals and pleaded their EU law rights prior to 31 December 2020;

(2) the Tribunal is bound by EU case law decided prior to that date;

(3) the Tribunal may have regard to relevant Court of Justice of the EU ("**CJEU**") case law after that date but is not bound by it.

SOME CASES REFERRED TO BY THE PARTIES

CJEU cases

Enel (Case-C-107/10) 12 May 2011

49. Refunds of overpaid VAT must be made within a reasonable period of time by a payment in liquid funds or equivalent means; the method of refund adopted must not entail any financial risk for the taxable person

50. Calculation of the interest payable which does not take as its starting point the date on which the excess VAT would have had to be repaid in the normal course of events in accordance with the VAT Directive would be contrary, in principle, to the requirements of Article 183 (concerning right of deduction of input tax).

Littlewoods (Case C-591/10) 19 July 2012

51. This case was in part about s78. The court referred to the principle of the obligation of member states to repay with interest amounts of tax levied in breach of EU law; it was for the domestic legal order of each member state to lay down the conditions in which such interest had to be paid, particularly the rate of that interest and its method of calculation (simple or compound interest). Those conditions had to comply with the principles of equivalence and effectiveness; i.e. they could not be less favourable than those concerning similar claims based on provisions of national law or arranged in such a way as to make the exercise of rights conferred by the EU legal order practically impossible.

Irimie (Case C-565/11) 18 April 2013

52. The court held that:

(1) as regards the principle of effectiveness, EU law principles requires, in a situation of repayment of a tax levied by a member state in breach of EU law, that the national rules referring to the calculation of interest which may be due should not lead to depriving the taxpayer of adequate compensation for the loss sustained through the undue payment of the tax.

(2) a system which limits interest to that accruing from the day following the date of the claim for repayment of the tax unduly levied, does not meet that requirement.

(3) that loss depends, inter alia, on the duration of the unavailability of the sum unduly levied in breach of EU law and thus occurs, in principle, during the period between the date of the undue payment of the tax at issue and the date of repayment thereof.

Compass (Case C-38/16) (14 June 2017)

53. There were differences in the nature of the rights at issue and the objectives pursued as between (i) the right to repayment of overpaid VAT - intended to remedy a situation which stemmed from an infringement of EU law by permitting the beneficiary of that right to neutralise an economic burden which was wrongly imposed, and (ii) the right to deduct input VAT – this stemmed from the actual application of the common system of VAT, so that the VAT payable or paid was not borne by the taxable person in his economic activities that were subject to VAT, thus ensuring neutrality of taxation of those activities. These differences justified the existence of legal rules specific to each of those two rights, inter alia, with regard to their content and the conditions for their exercise, such as the limitation period for actions to enforce those rights and, specifically, the date from which such a period applied. Having regard to those differences, the principles of fiscal neutrality, equal treatment and effectiveness did not require that national tax authorities treat the holders of those rights in the same way in respect of the limitation periods for claims concerning those rights

Nidera (Case C-387/16) 28 February 2018

54. This case found that a reduction in the amount of interest normally payable under national law on overpaid VAT, which was not refunded in due time for reasons connected to circumstances not attributable to the taxable person, was precluded. The court said:

> (1) whilst member states have a certain freedom in determining the conditions for the refund of overpaid VAT, those conditions cannot undermine the principle of fiscal neutrality by making the taxable person bear the burden of the VAT in whole or in part. In particular, such conditions must enable the taxable person, in appropriate circumstances, to recover the entirety of the credit arising from that overpaid VAT. This implies that the refund is made within a reasonable period of time and that, in any event, the method of refund adopted does not entail any financial risk for the taxable person.
>
> (2) when the refund to the taxable person of the overpaid VAT is not made within a reasonable period, the principle of fiscal neutrality of the VAT system requires that the financial loss incurred by the taxable person on account of the unavailability of the sums of money at issue be compensated through the payment of default interest. In the absence of EU legislation on VAT, it is for the internal legal order of each Member State to lay down the conditions under which default interest must be paid, particularly the rate of that interest and its method of calculation, whilst nevertheless observing the principle of fiscal neutrality

E.sp. (Case C-335/19) 26 November 2020

55. The case concerned Article 90. It decided:

> (1) the formalities to be complied with by taxable persons in order to exercise, vis-à-vis the tax authorities, the right to reduce the taxable amount for VAT, must be limited to those which make it possible to provide proof that, after the transaction has been concluded, part or all of the consideration will definitely not be received. It is for the national courts to ascertain whether that is true of the formalities required by the member state concerned.
>
> (2) to accept that it is possible for member states to exclude any reduction of the VAT taxable amount would run counter to the principle of the neutrality of VAT, which means, inter alia, that the trader, as tax collector on behalf of the State, is entirely to be relieved of the burden of tax due or paid in the course of his economic activities which are themselves subject to VAT.

FGSZ (3 March 2021)

56. The court held that Article 90, read in conjunction with the principles of fiscal neutrality and effectiveness, must be interpreted as meaning that, where a member state lays down a limitation period after which a taxable person, who has a debt which has become definitively irrecoverable, can no longer assert his right to obtain a reduction in the taxable amount, that limitation period must begin to run not from the date of performance of the payment obligation initially provided for, but from the date on which the debt became definitively irrecoverable.

57. The court noted that:

> (1) Article 90 embodies one of the fundamental principles of the VAT Directive, the principle of fiscal neutrality, according to which the taxable amount is the consideration actually received and the corollary of which is that the tax authorities may not collect an amount of VAT exceeding the tax which the taxable person received.

(2) the derogation power in Article 90(2) is only intended to enable member states to counteract the uncertainty as to the non-payment of an invoice or the definitive nature of that non-payment.

CS, technoRent (Case C-844/19) (12 May 2021)

58. In this case, technoRent was seeking interest from the time of its return claiming VAT credit resulting from a price reduction. The court stated the principles thus:

> "35 As regards the refund of excess VAT under Article 183 of the VAT directive, it should be recalled that, as the Court has repeatedly held, the right to deduct provided for in Article 167 et seq. of that directive is an integral part of the VAT scheme and in principle may not be limited. In particular, the right to deduct is exercisable immediately in respect of all the taxes charged on transactions relating to inputs (see, inter alia, judgments of 21 June 2012, *Mahagében and Dávid*, C-80/11 and C-142/11, EU:C:2012:373, paragraph 38, and of 26 April 2018, *Zabrus Siret*, C-81/17, EU:C:2018:283, paragraph 33).
>
> 36 The deduction system, and accordingly the refund system, is intended to relieve the operator entirely of the burden of the VAT due or paid in the course of all his or her economic activities. The common system of VAT therefore ensures neutrality of taxation of all economic activities, whatever their purpose or results, provided that they are themselves, in principle, subject to VAT (judgment of 21 March 2018, *Volkswagen*, C-533/16, EU:C:2018:204, paragraph 38).
>
> 37 It is also apparent from the Court's case-law that, while the Member States have a certain freedom in determining the conditions referred to in Article 183 of the VAT directive, those conditions cannot undermine the principle of fiscal neutrality by making the taxable person bear the burden of the VAT in whole or in part (judgments of 12 May 2011, Enel Maritsa Iztok 3, C-107/10, EU:C:2011:298, paragraph 33, and of 14 May 2020, Agrobet CZ, C-446/18, EU:C:2020:369, paragraph 35).
>
> 38 In particular, such conditions must enable the taxable person, in appropriate circumstances, to recover the entirety of the credit arising from that excess VAT. This implies that the refund is made within a reasonable period of time by a payment in liquid funds or equivalent means, and that, in any event, the method of refund adopted must not entail any financial risk for the taxable person (judgment of 12 May 2011, Enel Maritsa Iztok 3, C-107/10, EU:C:2011:298, paragraph 33).
>
> 39 If, in the event that the refund of excess VAT is not made within a reasonable period of time, the taxable person were not entitled to default interest, the taxable person's situation would be negatively affected, in breach of the principle of fiscal neutrality.
>
> 40 It follows that, even though Article 183 of the VAT directive does not lay down an obligation to pay interest on the excess VAT to be refunded or specify the date from which such interest is payable, the principle of fiscal neutrality of the VAT system requires that the financial loss incurred on account of a refund of excess VAT not made within a reasonable period of time be compensated through the payment of default interest (judgments of 28 February 2018, *Nidera*, C-387/16, EU:C:2018:121, paragraph 25, and of 14 May 2020, *Agrobet CZ*, C-446/18, EU:C:2020:369, paragraph 40).
>
> 41 The same is true, as the Advocate General observed in point 31 of her Opinion, in connection with the refund of VAT following from a reduction of the taxable amount for VAT pursuant to Article 90(1) of the VAT directive.

> 42 In such a situation, the taxable person is also charged excess VAT which must be refunded to him or her, incurring financial loss to his or her detriment, on account of the unavailability of the sums of money at issue. If, in the event that the tax authorities do not reimburse that excess within a reasonable period of time, the taxable person were not entitled to default interest, the taxable person's situation would be negatively affected, thereby undermining the principle of fiscal neutrality."

Court of Appeal cases

British Telecommunications v HMRC [2014] EWCA Civ 433

59. As to whether s39(5) Finance Act 1997, which barred the making of any 'old regime' bad debt refund claims after 19 March 1997, infringed the taxpayer's directly enforceable rights under Article 90 (which were the subject of a later claim): the bad debts in question arose from supplies made 20 years earlier; it had been open to BT from 1978 down to 1990 to make bad debt refund claims under the "old regime" in respect of each bad debt as it arose, and it continued to be open to it to make such belated claims until 1997. In making good such claims the taxpayer would have had to show that some statutory conditions were incompatible with its EU law rights; however, the case had to be approached on the basis that the taxpayer could and would have done so. The only reason the taxpayer did not make such claims was seemingly because it was unaware that it was open to it to do so. A lack of awareness could not be a relevant consideration. The taxpayer had every opportunity to obtain expert advice as to its rights. The taxpayer had had almost two decades in which to enforce its rights, but had done nothing towards doing so.

60. Section 80 applied to cases where the taxpayer had brought into account as output tax an amount that was not output tax due. When the taxpayer had made its supplies, it had accounted for tax which was then due. The subsequent failure of the customer to pay for the supply gave rise to a bad debt, and a possible claim for a bad debt refund, which would be for the repayment of all or part of the output tax originally paid by the taxpayer. The arising of such bad debt did not, however, mean that the output tax earlier paid was not output tax due within the meaning of s80. It was, and remained so, and the arising of the bad debt did not retrospectively change that.

GMAC

61. As well as finding the property transfer condition to be invalid, the Court of Appeal found that the exercise of GMAC's EU law rights was not rendered excessively difficult or virtually impossible by s39(5) Finance Act 1997: GMAC had more than adequate time to exercise its EU law rights and was given adequate notice of the withdrawal of the old scheme.

Tribunal decision: Ford

62. *Ford Motor Company Ltd v HMRC* [2017] UKFTT 0407 (TC) considered whether one of the outcomes set out at s78(1) was "due to" an error on HMRC's part. In its review of relevant case law at [8], the Tribunal cited the 1998 VAT and Duties Tribunal decision in *Chartered Institute of Bankers*, which said

> (1) "there is a need for us to look realistically at the true cause" (of the s78(1) outcome said to be "due to" HMRC's error); and
>
> (2) "plainly" a case where the taxpayer has got the tax wrong "due to" an error by HMRC can be where HMRC "gave him a clear but wrong ruling whether or not the taxpayer had asked for one. As part of their responsibility for the care and management of VAT, and using the powers given to them in that behalf, the Commissioners can and do give such advice."

63. At [9] the Tribunal set out six points, derived from *Chartered Institute of Bankers*, and endorsed by the VAT and Duties Tribunal in another 1998 decision, *CGI Pension Trustees v Customs & Excise Commissioners*, agreed by the parties as correctly representing the law:

> (1) "that "error" in s78 was to be widely interpreted, and included a positive mistake or misdirection;
>
> (2) that although VAT was a self-assessed tax, Customs enjoyed statutory powers of care and management under which they could, and frequently did, give rulings on VAT liability and the practical implications of the liability and accounting rules for individual taxpayers: and, when they did so, they risked triggering s78;
>
> (3) that it was no answer to CGI's case to say that Customs acted in good faith, or that CGI accepted the error at face value;
>
> (4) nor was it an answer to CGI's case to say that a particular area of law was complex and that Customs (or CGI) were confused. In such cases the tribunal should ask: from what did the taxpayer's confusion directly flow?;
>
> (5) that if an error was established there must be a causal link between the error and the taxpayer acting in one of the ways contemplated by s78(1). The section was satisfied if the taxpayer "relied on" Customs in taking the course it had taken, or, alternatively, if the error was the "true cause" of the taxpayer's action or inaction; and
>
> (6) that Customs' error need not be the sole cause of the taxpayer's course of action. However, if there was no causal link it would be "repugnant to common sense" to describe the taxpayer's course of action as "due to" Customs' error."

64. The decision considered wording in a VAT Notice published by HMRC. The Tribunal said:

> (1) "if an error occurs in an official HMRC VAT Notice and a taxpayer can establish that it has overpaid VAT as a result of that error then the causal connection between the overpayment ("due to") and the error is established; that is all that section 78(1) requires" (at [75]); and
>
> (2) "HMRC must have intended that taxpayers would read and rely upon that advice in relation to the common occurrence of a subsequent change in the consideration paid for a supply subject to VAT. If such an error existed and that error caused Ford to overpay output tax then the requirements of section 78(1) would be satisfied and Ford would be entitled to a payment of interest" (at [77]).

APPELLANTS' ARGUMENTS - MORE DETAIL

Section 78 and EU law rights

65. The appellants submitted that "entitlement" to a bad debt refund is "exercised" by making a claim, following which there is a refund of the VAT chargeable.

66. The appellants submitted that wherever a taxpayer establishes, by reference to the proportionately imposed statutory criteria, which may be limited only to those establishing the definitive nature of non-payment, total or partial non-payment, it has a directly effective, Article 90, entitlement to reduce the taxable amount.

67. The appellants argued that s36(2) recognises a distinction between the Article 90 "entitlement" and requirements arising from "obligations … deemed necessary to ensure the correct collection of VAT" under Article 273 by reference to which that entitlement is exercised "on making a claim".

68. The appellants said this distinction can be seen in the language of regulation 166, which says that a claimant who is no longer registered for VAT when they "become entitled to a refund" shall make a claim in such form and manner as HMRC may direct.

69. The appellants argued that they were entitled to refunds at the earlier dates. At that point they had a directly effective right of reimbursement under Article 90. However, the exercise of that right was precluded by HMRC's errors: (i) the terms of the property transfer condition, and (ii) HMRC's public guidance on the property transfer condition.

70. The appellants argued that there was a "statutory bar" on their making bad debt refunds claims, being the property transfer condition.

71. The appellants' position was that interest runs from the point at which they became entitled to refunds. The appellants accepted that entitlement arose only once the three conditions listed in s36(1) were met.

72. The appellants argued that the direct and inevitable consequence of their not claiming the bad debt refunds to which they were entitled at the earlier dates was that the VAT due on their returns was overstated and, as a consequence, over paid, such that the appellants bore the burden of VAT for which they had a directly effective EU right to reimbursement.

73. The appellants argued that, under CJEU case law, they had a right to adequate indemnity/reasonable redress for the loss suffered as a consequence of having been precluded from exercising their entitlement to the bad debt refunds and thereby having overpaid VAT, period by period and return by return, to HMRC in respect of supplies in the relevant years. The payment of interest in such circumstances is an inherent component of receiving adequate indemnity/reasonable redress.

74. They said that the case law is clear that whilst member states have autonomy as to the rate and method of calculation of interest there is no discretion as to the period for which it is payable.

75. The appellants contended that HMRC's position in restricting interest to only part of the period for which the appellants were out of pocket must be regarded as contrary to the principle of effectiveness since it means that the exercise of the right arising under EU law, and consisting of the right to compensation for a loss incurred as a result of the late refunding of tax, is impossible or at least excessively difficult.

76. HMRC's position also breached the principle of equivalence, the appellants contended, because in comparable situations regarding either input tax or where excess VAT is shown on a VAT return, interest is paid from the date on which entitlement to repayment arises.

HMRC'S ARGUMENTS - MORE DETAIL

Section 78

77. HMRC submitted that s78(1)(c) applies only in cases where a person has paid an amount of VAT that 'was not VAT due'. At all material times, VAT paid by the appellants was VAT due.

78. HMRC argued that, under s36, prior to claims being made, no refund is due. HMRC did not accept that the bad debt refunds were paid pursuant to any liability to repay VAT received from the appellants that was not due; they were payments of refunds claimed by the appellants.

79. HMRC said that the appellants did not overpay or over-account for VAT, or pay VAT that was not due. The Court of Appeal decided, in *BT* and *GMAC*, that s36 claims for bad debt refunds do not fall within s80, which concerns situations where there has been an over-accounting or overpayment of VAT or payment of VAT not due.

80. HMRC submitted that it was made clear in *GMAC* that it would not be appropriate in any moulding of the scheme for bad debt refunds to conform to Article 90, to set it aside in its entirety (see at [126]). That is, the requirement to make a claim for a bad debt refund would remain. A supplier is in the best position to know when a debt is bad (further to attempts to recover the relevant consideration, which in the HP context can be extensive) and to determine if and when a bad debt refund claim is to be made. CJEU case law permits implementation of Article 90 to take account of the uncertainty as to non-payment and a system of claiming relief is a permissible condition in this respect.

81. HMRC submitted that s78(1)(c) is intended to relate to s80(1B), and requires a payment to have been made to HMRC. In relation to 'repayment traders' who have not claimed bad debt refunds, no such payment would have been made.

82. The relevant start date for the payment of interest under s78(1)(d) is the date on which "apart from the error, the Commissioners might reasonably have been expected to authorise payment of the amount on which interest is payable." HMRC said they could not have authorised payment of the bad debt refunds prior to claims being made.

83. HMRC submitted that the appellants were wrong to assert that claims could not have been made prior to the dates of claim. Where, under the 'old scheme', BT and GMAC did not bring their claims in time (because they were brought after the old scheme came to an end), it was no answer to say that the relevant conditions were unlawful. The Court of Appeal's position was that the scheme for bad debt refunds nonetheless applied, would be shorn of only the offending provisions, and that there had been every opportunity to pursue such claims prior to repeal of the old scheme (see *BT* at [122], *GMAC* at [126, 133]). As the Court of Appeal noted at [133] in *GMAC*, that a claim would have been rejected by HMRC did not render GMAC's EU law rights excessively difficult or virtually impossible (and so offend against the principle of effectiveness) (see also *Repertoire Culinaire Ltd v HMRC* [2017] EWCA Civ 1845 [2018] STC 958 at [77-80], where inevitable refusal of a claim by HMRC did not mean that a statutory route was practically impossible or excessively difficult; and the CJEU similarly concluded that a refund system for claiming directly effective EU law rights should be given effect, with three unjustifiable conditions disapplied). A taxpayer had claimed bad debt refunds in 1994 on the basis that a condition that such refunds did not apply to barter transactions was unlawful and the CJEU ruling in that case was released in 1997: Case C-330/95 *Goldsmiths (Jewellers) Ltd v Commissioners of Customs and Excise*. GMAC brought its own claim in 2006; it is hard to see why there was anything preventing such a challenge being made sooner.

EU law rights

84. HMRC submitted that the case law relating to a "refund of charges levied in a Member State in breach of rules of EU law" (*Littlewoods, Irimie*) was of little relevance: as determined by the Court of Appeal in *BT* and *GMAC*, the VAT paid by the appellants was always properly due; these appeals do not involve claims for statutory restitution for over-accounted, overpaid or overcharged VAT.

85. HMRC submitted that in *CS, technoRent* the CJEU gave no indication that the domestic provisions from which interest starts to run within a reasonable time from when a claim to a refund is made, would be objectionable.

86. In HMRC's submission, in particular in a context in which the UK has not enacted any limitation period for a claim to bad debt refunds, it is entirely reasonable that interest be paid from the date a claim for the refund is made, such that there is no infringement of the principles of fiscal neutrality, effectiveness or equivalence.

87. HMRC emphasised the following:

(1) EU law does not require a member state to provide any refund or repayment or deduction where a taxpayer has not made a claim within the relevant limitation period *even where* domestic implementation has been unlawful or contrary to EU law. Inherent in this position is an acceptance that, it is entirely reasonable to require those who wish to rely on EU law to make a claim in time. The fact that their claims would have been rejected under domestic law does not mean that exercise of their EU law rights was rendered excessively difficult or virtually impossible.

(2) the domestic implementation of Article 90 in the form of claimed refunds is unobjectionable. That the UK bad debt rules contained an unlawful condition (such as the property transfer condition), is not a bar to HMRC's seeking to rely on those rules shorn of such an unlawful condition. The reason why the appellants have no earlier entitlement to interest is not because of the unlawful property transfer condition; it is because (as with those who miss limitation periods altogether) they simply did not make an earlier claim.

(3) were the appellants right that, even absent a claim, there is an entitlement to interest from some period soon after the debt becomes bad, then there would in principle be nothing preventing taxpayers from making a claim at some future point, possibly decades into the future (in light of the absence of a limitation period), and seeking interest from that earlier point.

DISCUSSION

Was s78(1)(c) or (d) satisfied?

88. To invoke s78, the taxpayer needs to show:

(1) an error on the part of HMRC;

(2) one of the outcomes in s78(1)(a) to (d); and

(3) a causal connection between (1) and (2) above (the "due to" requirement).

89. I have found two errors on HMRC's part (see [26] above), both caused by HMRC's (incorrect) belief that the property transfer condition was legally valid in respect of supplies made in the relevant years. In my view, the enactment of the property transfer condition, and its continued presence on the statute book up to 19 March 1997, was not "an error on HMRC's part", being an act of Parliament rather than of HMRC.

90. It was common ground that one of the errors by HMRC – that at [26(2)] above – did cause one of the prescribed outcomes, namely s78(1)(d) – it caused the appellants to suffer delay in receiving payment of the bad debt refunds that were due to them; the delay began at the dates of claim; it was common ground that the applicable period began (per s78(7)(a)) on the same dates.

91. The primary question at issue here is whether HMRC's other error – that at [26(1)] above, regarding the contents of Notice 700/18 – caused an outcome described in s78(1)(c) or (d).

92. The outcome that the appellants say answers to the description in s78(1)(c) is the fact that the appellants (or members of their groups) accounted for and paid more VAT in the earlier returns than they would have done had the bad debt refunds been credited to them in those earlier returns.

93. The outcome that the appellants say answers to the description in s78(1)(d) is that they did not receive the bad debt refunds in the period between their satisfying all the (valid) conditions in s36 for entitlement (i.e. the earlier dates) and the dates of claim – this was the

delay they said they suffered, in addition to the (agreed) delay suffered between the dates of claim and payment.

94. The factual outcomes, as summarised in the previous two paragraphs, are not themselves contested by HMRC – what is contested is whether they answer to the descriptions in s78(1)(c) and (d).

95. So the primary question at issue here can be expressed thus – whether the outcomes described at [92-93] above were due to HMRC's error as set out at [26(1)] above; in other words, even assuming that those outcomes answer to the descriptions in s78(1)(c) or (d), were they "due to" HMRC's errors in their publications as regards the validity of the property transfer condition?

96. The proximate cause of the outcomes described at [92-93] above, was the fact that the appellants (or members of their groups) did not claim the bad debt refunds in the earlier returns, or indeed at any time prior to the dates of claim: this omission to claim was the proximate cause both of

> (1) more VAT being payable by the appellants (or members of their groups) in the periods for which those earlier returns were made (because the refunds were not credited against the VAT otherwise due); and
>
> (2) the appellants' (or members of their groups) not receiving refunds in the period prior to the dates of claim (refunds could not be paid when no claim had been made).

97. Given the above, the primary question at issue here can be further refined as: did HMRC's error as set out at [26(1)] above cause the appellants (or members of their groups) not to claim the refunds at the earlier dates or at any time prior to the dates of claim?

98. This is answered, in the negative, by my finding at [28] above – the reason the appellants (or members of their groups) did not claim the bad debt refunds until the dates of claim was that they believed the property transfer condition was legally valid. This, in the language of *Ford* and the 1998 tribunal decisions on s78 which that decision followed, was, realistically, the true cause of the omission to claim prior to the dates of claim. It follows that statements in HMRC's public notices – the error on their part per the finding at [26(1)] above - were, realistically, not the true cause; it was the property transfer condition, rather than the statements in the Notice, that were "relied upon" when the appellants (or members of their groups) omitted to make claims.

99. Nor, for the avoidance of doubt, was the cause of the omission to claim, the impossibility of making a claim - it was clearly possible for the appellants (or members of their groups) to have claimed at the earlier dates, by including figures in the relevant returns in the manner mandated by regulation 166, or by claiming in another manner under that regulation (which would have had to be allowed by HMRC). The fact that HMRC would have rejected any such claim does not alter the fact that the appellants could have made claims.

100. This means that, even assuming one of the outcomes in s78(1)(c) and (d) for which the appellant contend, s78 is not engaged on the facts of this case for an "applicable period" beginning before the dates of claim, as the "due to" requirement is not satisfied.

101. I will, however, go on to consider other aspects of s78 that were argued on the hearing, on the hypothetical basis that the "due to" requirement was satisfied.

102. In my view the outcome described at [92] above does not answer to that required by s78(1)(c), because, in the absence of their making claims for bad debt refunds in the earlier returns, the VAT "due" pursuant to those returns was as shown on them.

103. However, the outcome described at [93] above does answer to that required by s78(1)(d):

(1) the statutory scheme of s78, based on the construction of s78(1)(b), is that where a taxpayer has failed (due to HMRC's error) to claim a credit it is entitled to claim, HMRC are as a consequence (of such entitlement to claim) "liable" to pay that amount to the taxpayer; in other words, entitlement to claim on the taxpayer's part is sufficient to create liability on HMRC's part. Applying this construct to s78(1)(d), this means that the bad debt refunds became "due" (because HMRC became liable) at the point at which the appellants (or members of their groups) satisfied the (valid) conditions for entitlement to claim.

(2) this construction of the statute is supported by the general law, which distinguishes between amounts "due" and amounts "payable": see the Tribunal's analysis in *Albany Fish Bar Limited; Waseem Akhtar v HMRC* [2021] UKFTT 100 (TC) at [142-143] in the context of a statutory reference to amounts due *or* payable:

> "142 … The issue is therefore whether there was an amount "due". In *Re Airedale Garage Co Ltd, Anglo-South American Bank Ltd v Airedale Garage Co* [1933] 1 Ch 64 at 78–79, Lord Hanworth MR said, albeit in a different statutory context:
>
> > "I think the words 'due and payable' in s 264 of the Companies Act [1929] are meant to refer to a liability in respect of which there had to be a payment..."
>
> 143. In other words, "due" means that there is a liability and "payable" that "there had to be a payment"…"

(3) I therefore conclude that the bad debt refunds were due to the appellants (or members of their groups) from the earlier dates; they therefore suffered delay in receiving amounts due to them.

EU law principles

104. The gist of my interpretation and application of s78 in this case is:

(1) interest on "delayed" bad debt refunds (i.e. refunds paid later than the time when (valid) conditions for entitlement were satisfied) is payable to the taxpayer only where an error by HMRC has caused the delay;

(2) the property transfer condition was not itself an error by HMRC;

(3) there were errors by HMRC here, but, per my findings of fact, they were not the true cause of the delay (up to the time of the dates of claim);

(4) the true cause of the delay was the taxpayer's belief that the property transfer condition was legally valid;

(5) hence, interest is not payable to the appellants on "delayed" bad debt refunds here in respect of the period prior to the dates of claim, even though the UK statute included a condition for bad debt refunds that was invalid as a matter of EU law.

105. The key question is whether the statutory scheme as laid out immediately above – in particular, points (1) and (5) above – runs contrary to EU law principles.

106. In a hypothetical scenario where the delay in payment of bad debt refunds was clearly due to fault on the part of the taxpayer – say, because the taxpayer delayed claiming as it did not know it had a right to claim, either through ignorance, or receiving bad advice – it seems to me that denial of payment of interest until the date of claim would not run contrary to EU principles:

(1) the governing principle is that the refund must be paid "within a reasonable period time" and, if it is not, interest becomes payable. This in turn is derived from the principle that conditions for claiming refunds must enable the taxable person, in appropriate circumstances, to recover the entirety of the refund. It seems reasonable that, if the taxpayer was fully able to claim but, for reasons unconnected with the tax authorities, delayed in claiming, the refund is paid upon receipt of the claim. It would be unreasonable to expect payment of the refund before it was claimed.

(2) this seems entirely in keeping with the principle of effectiveness – exercise of the taxpayer's right to the refund is not, on these facts, "practically impossible" – 'fault' for the delay between entitlement and payment lies at the door of the taxpayer.

(3) it is also seems in keeping with the principle of fiscal neutrality: the taxpayer has not been made to bear the burden of excess VAT; its right to deduct was exercisable as soon as the valid conditions were satisfied.

107. The situation here is essentially similar to the hypothetical one above, in the sense that that the appellants (or members of their groups) could have claimed but omitted to do so because they did not appreciate that they had a right to do so. There is an obvious difference, in that Parliament's enactment of the property transfer condition considerably muddied the waters as regards the potential claimants' appreciating what their true rights were. However, as the Court of Appeal's decision in *GMAC* demonstrated, that muddying of the waters did not impinge on the potential claimants' Article 90 rights; and it is clear, both from the wording of regulation 166 and from the appellants' eventual claims in 2007 and 2009, that the appellants (or members of their groups) could have claimed the refunds at the earlier dates. These latter points mean that, as in the hypothetical scenario above, and for essentially the same reasons, it is reasonable to extend the period for payment of the refund to the time of claim: there was no real constraint on the appellants' claiming earlier; the principles of effectiveness and fiscal neutrality are therefore respected; in such circumstances, to expect payment of the refund prior to claim is not reasonable.

108. As regards the principle of equivalence, I note that the requirement that the "due to" requirement applies to all the s78(1) outcomes, including those relating to overpaid VAT and failure to claim input tax credit. I do not therefore think that my construction of s78 as set out at [104] above offends against the principle of equivalence.

109. The EU law principle that the method of refund adopted must not entail any financial risk for the taxable person is also respected on the facts here: the refunds were paid, straightforwardly, in cash.

110. I conclude that my interpretation and application of s78 is in keeping with the relevant EU law principles.

Did s85A(2) apply?

111. Section 85A does not apply because the Tribunal has not determined the appeals under s83, nor is it deemed to have done so under s85, as there is neither an agreement in writing nor a notice of agreement in writing – see my findings at [39-40] above.

112. Even if s85A had applied by virtue of s85, the operative provision (s85A(2)) would not have had effect on the facts of this case, as "VAT credit" (defined at s25(3)) does not include a s36 refund.

CONCLUSION

113. Given my conclusions at [100], [110] and [111] above, the "agreed" issue (as set out at [9] above) is determined in favour of HMRC. This means that the "further" issue (as set out at

[11] above) does not arise. The appeal against HMRC's decision to pay interest from the dates of claim (and not earlier) is accordingly dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

114. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

ZACHARY CITRON
TRIBUNAL JUDGE

RELEASE DATE: 04 SEPTEMBER 2021

Article 11C(1) of the Sixth Council Directive 77/388/EEC (now Article 90 Directive 2006/112/EC)

1. In the case of cancellation, refusal or total or partial non-payment, or where the price is reduced after the supply takes place, the taxable amount shall be reduced accordingly under conditions which shall be determined by the Member States.

2. However, in the case of total or partial non-payment, Member States may derogate from this rule.

Summary of s11 Finance Act 1990 and (from 1994) s36 and relevant regulations as they applied to supplies in the relevant years

(1) A person must have supplied goods or services for consideration (on or after 1 April 1989) and accounted for and paid VAT on the supply (s11(1)(a) Finance Act 1990, s36(1)(a));

(2) the whole or any part of the consideration for the supply must have been written off in that person's accounts as a bad debt (s11(1)(b)) Finance Act 1990, s36(1)(b));

(3) two years must have elapsed from the date of the supply (s11(1)(c) Finance Act 1990) reduced, from 1991, to one year (s15 Finance Act 1991) and, from 1994, to six months (s36(1)(c)) (this period is referred to in this decision as the "**statutory waiting period**");

(4) in the case of the supply of goods, the property in the goods must have passed to the person to whom they were supplied or to a person deriving title from, through or under that person (section 11(4)(b) Finance Act 1990, s36(4)(b)). This was the property transfer condition. It was removed by s39(1) Finance Act 1997 for supplies made after 19 March 1997;

(5) regulations under s11 Finance Act 1990 and later s36, could require a claim to be made in a particular form and manner; for it to be evidenced and quantified by reference to records; require such records to be retained; and require repayment of refunds in specified cases (section 11(2) and (5) Finance Act 1990, s36(2) and (5));

(6) a person meeting these conditions was entitled, on making a claim to HMRC, to a refund of the amount of VAT chargeable by reference to the 'outstanding amount' (i.e. the unpaid consideration written off) (s11(2) and (3) Finance Act 1990, s36(2) and (3));

(7) claims were made by including the correct amount of the refund in the box opposite the legend 'VAT reclaimed in this period on purchases and other inputs' on the person's VAT return (save as HMRC may otherwise allow or direct) (regulation 166 and reg 3 VAT (Refunds for Bad Debts) Regulations 1991)

Section 78

Interest in certain cases of official error

(1) Where, due to an error on the part of the Commissioners, a person has—

(a) accounted to them for an amount by way of output tax which was not output tax due from him [and, as a result, they are liable under section 80(2A) to pay (or repay) an amount to him,] or

(b) failed to claim credit under section 25 for an amount for which he was entitled so to claim credit and which they are in consequence liable to pay to him, or

(c) (otherwise than in a case falling within paragraph (a) or (b) above) paid to them by way of VAT an amount that was not VAT due and which they are in consequence liable to repay to him, or

(d) suffered delay in receiving payment of an amount due to him from them in connection with VAT,

then, if and to the extent that they would not be liable to do so apart from this section, they shall pay interest to him on that amount for the applicable period, but subject to the following provisions of this section.

[(1A) In subsection (1) above—

(a) references to an amount which the Commissioners are liable in consequence of any matter to pay or repay to any person are references, where a claim for the payment or repayment has to be made, to only so much of that amount as is the subject of a claim that the Commissioners are required to satisfy or have satisfied; and

(b) the amounts referred to in paragraph (d) do not include any amount payable under this section.]

(2) Nothing in subsection (1) above requires the Commissioners to pay interest—

(a) on any amount which falls to be increased by a supplement under section 79; or

(b) where an amount is increased under that section, on so much of the increased amount as represents the supplement.

(3) Interest under this section shall be payable at [the rate applicable under section 197 of the Finance Act 1996].

(4) The "applicable period" in a case falling within subsection (1)(a) or (b) above is the period—

(a) beginning with the appropriate commencement date, and

(b) ending with the date on which the Commissioners authorise payment of the amount on which the interest is payable.

(5) In subsection (4) above, the "appropriate commencement date"—

(a) in a case where an amount would have been due from the person by way of VAT in connection with the relevant return, had his input tax and output tax been as stated in that return, means the date on which the Commissioners received payment of that amount; and

(b) in a case where no such payment would have been due from him in connection with that return, means the date on which the Commissioners would, apart from the error, have authorised payment of the amount on which the interest is payable;

and in this subsection "the relevant return" means the return in which the person accounted for, or (as the case may be) ought to have claimed credit for, the amount on which the interest is payable.

(6) The "applicable period" in a case falling within subsection (1)(c) above is the period—

(a) beginning with the date on which the payment is received by the Commissioners, and

(b) ending with the date on which they authorise payment of the amount on which the interest is payable.

(7) The "applicable period" in a case falling within subsection (1)(d) above is the period—

(a) beginning with the date on which, apart from the error, the Commissioners might reasonably have been expected to authorise payment of the amount on which the interest is payable, and

(b) ending with the date on which they in fact authorise payment of that amount.

[(8) In determining in accordance with subsection (4), (6) or (7) above the applicable period for the purposes of subsection (1) above, there shall be left out of account any period by which the Commissioners' authorisation of the payment of interest is delayed by the conduct of the person who claims the interest.

(8A) The reference in subsection (8) above to a period by which the Commissioners' authorisation of the payment of interest is delayed by the conduct of the person who claims it includes, in particular, any period which is referable to—

(a) any unreasonable delay in the making of the claim for interest or in the making of any claim for the payment or repayment of the amount on which interest is claimed;

(b) any failure by that person or a person acting on his behalf or under his influence to provide the Commissioners—

(i) at or before the time of making of a claim, or

(ii) subsequently in response to a request for information by the Commissioners,

with all the information required by them to enable the existence and amount of the claimant's entitlement to a payment or repayment, and to interest on that payment or repayment, to be determined; and

(c) the making, as part of or in association with either—

(i) the claim for interest, or

(ii) any claim for the payment or repayment of the amount on which interest is claimed,

of a claim to anything to which the claimant was not entitled.

(9) In determining for the purposes of subsection (8A) above whether any period of delay is referable to a failure by any person to provide information in response to a request by the Commissioners, there shall be taken to be so referable, except so far as may be prescribed, any period which—

(a) begins with the date on which the Commissioners require that person to provide information which they reasonably consider relevant to the matter to be determined; and

(b) ends with the earliest date on which it would be reasonable for the Commissioners to conclude—

(i) that they have received a complete answer to their request for information;

(ii) that they have received all that they need in answer to that request; or

(iii) that it is unnecessary for them to be provided with any information in answer to that request.]

(10) The Commissioners shall only be liable to pay interest under this section on a claim made in writing for that purpose.

[(11) A claim under this section shall not be made more than [4 years] after the end of the applicable period to which it relates.]

(12) In this section—

[(a) references to the authorisation by the Commissioners of the payment of any amount include references to the discharge by way of set-off (whether under section 81(3) or otherwise) of the Commissioners' liability to pay that amount; and]

(b) any reference to a return is a reference to a return required to be made in accordance with paragraph 2 of Schedule 11.

Amendment

Sub-s (1): in para (a) words "and, as a result, they are liable under section 80(2A) to pay (or repay) an amount to him," in square brackets substituted by Finance (No 2) Act 2005, s 4(1), (2).

> Date in force: this amendment has effect in any case where a claim under s 80(2) hereof is made on or after 26 May 2005, whenever the event occurred in respect of which the claim is made: see Finance (No 2) Act 2005, s 4(6).

Sub-s (1A): inserted with retrospective effect by Finance Act 1997, s 44(1).

Sub-s (3): words in square brackets substituted by Finance Act 1996, s 197(6)(d)(ii), (7), this amendment applies in relation to interest running from before, as well as interest running from, or from after, 1 April 1997.

Sub-ss (8), (8A), (9): substituted, for sub-ss (8), (9) as originally enacted, in relation to determining whether any period beginning on or after 19 March 1997 can be left out of account, by Finance Act 1997, s 44(4), (5).

Sub-s (11): substituted, with retrospective effect in relation to any claim made on or after 18 July 1996, by Finance Act 1997, s 44(2).

Sub-s (11): words "4 years" in square brackets substituted by Finance Act 2008, s 118(1), Sch 39, paras 32, 35.

Date in force: 1 April 2009: see SI 2009/403, art 2(1); for transitional provisions and savings see art 5 thereof.

Sub-s (12): para (a) substituted with retrospective effect by Finance Act 1997, s 44(3).

Section 85A

Payment of tax on determination of appeal

(1) This section applies where the tribunal has determined an appeal under section 83.

(2) Where on the appeal the tribunal has determined that—

(a) the whole or part of any disputed amount paid or deposited is not due, or
(b) the whole or part of any VAT credit due to the appellant has not been paid,

so much of that amount, or of that credit, as the tribunal determines not to be due or not to have been paid shall be paid or repaid with interest at the rate applicable under section 197 of the Finance Act 1996.

(3) Where on the appeal the tribunal has determined that—

(a) the whole or part of any disputed amount not paid or deposited is due, or
(b) the whole or part of any VAT credit paid was not payable,

so much of that amount, or of that credit, as the tribunal determines to be due or not payable shall be paid or repaid to HMRC with interest at the rate applicable under section 197 of the Finance Act 1996.

(4) Interest under subsection (3) shall be paid without any deduction of income tax.

(5) Nothing in this section requires HMRC to pay interest—

(a) on any amount which falls to be increased by a supplement under section 79 (repayment supplement in respect of certain delayed payments or refunds); or
(b) where an amount is increased under that section, on so much of the increased amount as represents the supplement.

Section 85

Settling appeals by agreement

(1) Subject to the provisions of this section, where a person gives notice of appeal under section 83 and, before the appeal is determined by a tribunal, [HMRC] and the appellant come to an agreement (whether in writing or otherwise) under the terms of which the decision under appeal is to be treated—

(a) as upheld without variation, or
(b) as varied in a particular manner, or
(c) as discharged or cancelled,

the like consequences shall ensue for all purposes as would have ensued if, at the time when the agreement was come to, a tribunal had determined the appeal in accordance with the terms of the agreement . . ..

(2) Subsection (1) above shall not apply where, within 30 days from the date when the agreement was come to, the appellant gives notice in writing to [HMRC] that he desires to repudiate or resile for the agreement.

(3) Where an agreement is not in writing—

(a) the preceding provisions of this section shall not apply unless the fact that an agreement was come to, and the terms agreed, are confirmed by notice in writing given by [HMRC] to the appellant or by the appellant to [HMRC], and

(b) references in those provisions to the time when the agreement was come to shall be construed as references to the time of the giving of that notice of confirmation.

(4) Where—

(a) a person who has given a notice of appeal notifies [HMRC], whether orally or in writing, that he desires not to proceed with the appeal; and

(b) 30 days have elapsed since the giving of the notification without [HMRC] giving to the appellant notice in writing indicating that they are unwilling that the appeal should be treated as withdrawn,

the preceding provisions of this section shall have effect as if, at the date of the appellant's notification, the appellant and [HMRC] had come to an agreement, orally or in writing, as the case may be, that the decision under appeal should be upheld without variation.

(5) References in this section to an agreement being come to with an appellant and the giving of notice or notification to or by an appellant include references to an agreement being come to with, and the giving of notice or notification to or by, a person acting on behalf of the appellant in relation to the appeal.