[2015] UKFTT 474 (TC)

TC04641

Appeal number: TC/2010/07246

PROCEDURE -categorisation of appeals - application by Appellant for case to be re-allocated as a Complex case –rule 23(3) and (4) Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 considered - application refused

FIRST-TIER TRIBUNAL
TAX CHAMBER

JSM CONSTRUCTION LIMITED

Appellant

- and -

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

TRIBUNAL: JUDGE GREG SINFIELD

Sitting in public in London on 15 September 2015

Francis Fitzpatrick QC, instructed by Donald Pugh, solicitor, for the Appellant

Ewan West, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

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DECISION

Introduction

1. The Appellant ('JSM') appeals against the decision of the Respondents ('HMRC') to disallow the deduction of input tax o£226,845.88 claimed by JSM for VAT accounting periods 09/09, 12/09 and 03/10. On receipt of the notice of appeal, the tribunal allocated the case to the Standard category. JSM has applied under rule 23(3) of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ('FTT Rules') for a direction that this case be re-allocated as a Complex case. For the reasons given below, I have concluded that the application should be refused and, accordingly, that the case should not be reallocated as a Complex case but should proceed as a Standard case.

Background

2. I set out below a summary of the factual background to the appeal for the purposes of JSM's application only. The summary is based on the skeleton arguments and oral submissions presented to me for the purposes of the application. I make no findings of fact for the purposes of the appeals by JSM.

3. JSM is an engineering contractor working in the utilities sector. It was formed around July 1998. When it first started trading it worked principally as a subcontractor to a number of regional and national construction companies. From around 2008 onwards, JSM began to work as a main contractor offering a range of services, including the design, supply and installation of high-voltage cabling; undertaking ductwork and cable installation for telecommunications installations; and the design and installation of cabling for wind-farm projects. JSM's clients now include national power and telecommunications companies.

4. JSM enters into 'framework contracts' with its customers. These contracts set the terms of the work that JSM may be asked to undertake but do not guarantee any particular amount of work. As a result, although JSM employs some 110 staff, variations in the levels of work mean that JSM is often required to supplement its own workforce with subcontracted labour.

5. In 2009 and 2010, JSM engaged a provider of labour known as Goldflex Solutions Limited ('Goldflex') to supply labour to JSM for it to use to fulfil its contracts with its customers. Between September 2009 and May 2010, JSM paid Goldflex around £1.3 million for services supplied. On 22 June 2010, Goldflex became insolvent and a liquidator, Mr Katz, was appointed.

6. On 20 July 2010, HMRC decided to refuse JSM's claim for a repayment of input tax of £89,365.13 for the period 03/10. JSM appealed to this tribunal against HMRC's decision on 15 September 2010.

7. Mr Katz, acting as liquidator of Goldflex, initially pursued JSM for outstanding sums in respect of supplies of labour by Goldflex to JSM. The outstanding amounts remained unpaid and, on 6 May 2011, Mr Katz issued a credit note to JSM in respect of all the invoices that Goldflex had issued to JSM between 17 September 2009 and 3 June 2010 on the ground that Goldflex had not supplied any services to JSM. JSM has not challenged the lawfulness of the credit note issued by Mr Katz

8. On 17 May 2011, HMRC made a further decision to deny input tax deduction by JSM in respect of all Goldflex invoices during the periods 09/09, 12/09 and 03/10. JSM appealed to the tribunal against this decision on 5 January 2012. The Notice of Appeal filed on 5 January 2012 included submissions that the appeal should be allocated as a Complex case. Notwithstanding those submissions, but without any formal decision, the tribunal allocated the case to the Standard category.

9. On 21 May 2015, JSM applied under rule 23(3) of the FTT Rules for its appeal to be re-allocated as a Complex case on the grounds that it met all of the criteria set out in rule 23(4) for re-allocation as a Complex case. JSM made the application because it wished to bring the appeal within the costs regime in rule 10(1)(c) of the FTT Rules. HMRC opposes the application on the ground that the appeal does not fall within any of the criteria in rule 23(4).

10. The appeal is listed for a six day hearing between 18 and 25 January 2016. JSM has served witness statements from five witnesses. HMRC do not currently propose to call any witnesses. The document bundle for the hearing is still the subject of discussion between the parties but it seems likely that there will be at least four, perhaps five, lever arch files of documents.

Summary of issues in the appeal

11. It appears to me that the only question for the tribunal hearing the appeal is whether JSM is entitled to deduct the VAT shown on the Goldflex invoices although that question raises on a number of subsidiary issues. As I understand the parties' positions, JSM maintains that it received supplies of labour services from Goldflex and incurred input tax, which it is entitled to deduct, when it paid Goldflex for those services and HMRC contends that Goldflex did not supply any services to JSM or, alternatively, that the VAT on the supply by Goldflex is not input tax of JSM because the charge to VAT is not evidenced and quantified by documents or other information specified by HMRC.

12. HMRC makes no allegation of fraud against JSM and does not suggest that JSM was party to any fraud perpetrated by Goldflex or any other person. HMRC's primary case is based on the argument that the unchallenged issue by an insolvency practitioner of a credit note is sufficient to dispose of JSM's appeal. HMRC's position is that the issue by Mr Katz of a credit note in respect of all the supplies purportedly made by Goldflex, which has not been challenged by JSM, conclusively shows that no VAT was properly charged by Goldflex and, thus, that JSM has no right to deduct any input tax. HMRC contend that the tribunal is bound to have regard to the issue of the credit note by the liquidator and cannot reconsider whether it was properly issued or reach a contrary conclusion. HMRC's alternative case is based on the arguments that they have the power, by virtue of regulation 29 of the VAT Regulations 1995, to require JSM to hold or produce such evidence of entitlement to deduct input tax as HMRC may direct even after the time of supply and where JSM already holds invoices which, on their face, meet the requirements of regulations 13 and 14 of the VAT Regulations.

Law and practice on re-categorisation

13. The relevant parts of Rule 23 of the FTT Rules are as follows:

> "(3) The Tribunal may give a further direction re-allocating a case to a different category at any time, either on the application of a party or on its own initiative.

> (4) The Tribunal may allocate a case as a Complex case under paragraph (1) or (3) only if the Tribunal considers that the case -
>
> (a) will require lengthy or complex evidence or a lengthy hearing;
>
> (b) involves a complex or important principle or issue; or
>
> (c) involves a large financial sum.
>
> (5) If a case is allocated as a Complex case--
>
> (a) rule 10(1)(c) (costs in Complex cases) applies to the case; and
>
> (b) rule 28 (transfer of Complex cases to the Upper Tribunal) applies to the case."

It is clear from rule 23(4) of the FTT Rules that the tribunal may only allocate a case as a Complex case where, in the tribunal's view, the case comes within one or more of the three criteria.

14. Guidance on the correct approach to categorising an appeal as a Complex case was given by the Upper Tribunal in *Capital Air Services v HMRC* [2010] UKUT 373 (TCC) ('*Capital Air Services*'). The Upper Tribunal in *Capital Air Services* said at [25]:

> "In any case, it is clear beyond argument, we think, that the assessment of what is 'complex' evidence or a 'complex' issue within r 23(4)(a) and (b) is a matter of judgment. The task of making that judgment is assigned to the tribunal whose decision, if made applying the correct principles, can be overturned on an appeal to the Upper Tribunal only if it can be said that no reasonable tribunal could have reached that decision."

I refer further to what was said in *Capital Air Services* and also by the Judge Bishopp *Dreams v HMRC* [2012] UKFTT 614(TC) ('*Dreams*') below when discussing the rule 23(4) criteria.

15. The Practice Statement on Categorisation of Tax Cases in the Tax Chamber of the First-tier Tribunal issued by the Chamber President (Judge Bishopp) on 29 April 2013 states in relation to Complex cases as follows:

> "Rule 23 provides that the Tribunal may allocate a case as a Complex case only if the Tribunal considers that the case-
>
> (a) will require lengthy or complex evidence or a lengthy hearing;
>
> (b) involves a complex or important principle or issue; or
>
> (c) involves a large financial sum.
>
> The Tribunal will assess whether, having regard to the nature of a particular case, any one or more of these criteria are satisfied. In making this assessment the Tribunal will take into account all the circumstances, including the implications of the costs-shifting regime (subject to the right of the taxpayer to opt out) and the fact that cases allocated to the Complex category are eligible, subject to various consents, to be transferred to the Upper Tribunal.
>
> If on such an assessment the Tribunal considers that a case meets the stated criteria, it will, in the absence of special factors, allocate the case to the Complex category."

Discussion

16. In deciding whether or not to categorise an appeal as a Complex case, the tribunal must first decide whether or not it meets one or more of the criteria in rule 23(4) of the FTT Rules. Nothing in this decision should be taken as indicating any view about the issues that arise in this appeal other than whether the case meets one or more of the criteria in rule 23(4). Mr Francis Fitzpatrick QC, for JSM, submitted that JSM's appeal meets all of the conditions. Mr Ewan West, for HMRC, submitted that the appeal did not satisfy any of the criteria.

Will the case require lengthy or complex evidence or a lengthy hearing?

17. The first criterion in rule 23(4)(a) is whether the case will require lengthy or complex evidence or a lengthy hearing. The Upper Tribunal in *Capital Air Services* did not define 'lengthy' or 'complex' in rule 23(4)(a) but, at [24], indicated that there were certain limits to the tribunal's discretion to consider that a hearing is lengthy. In relation to the duration of the hearing, the Upper Tribunal stated that "[i]t would be perverse to say that a hearing of half a day could ever be lengthy or that a three month case was not lengthy." The Upper Tribunal then went on to say:

> "But in many cases there will a judgment to be made where different judges of the Tax Chamber might reasonably take different views. It cannot be said that there is a single 'right' answer that can be objectively ascertained as a matter of law. The Rules assign the task of making that judgment to the Tribunal by providing that a case can be allocated as Complex only if the Tribunal considers one or more of the criteria to be met. We do not consider that there is a single objective and correct answer to how long is 'lengthy' or how large is a 'large financial sum'."

18. The First-tier Tribunal in *Dreams* commented on this approach at [19]:

> "In other words, it is not possible to provide comprehensive guidance, and each case has to be considered on its own merits. In my view the gateway in rule 23(4)(a) can be sensibly applied only if one starts from the proposition that a case must have some feature out of the ordinary if it is to be categorised as Complex. By that I do not mean, for example, that only hearings requiring more than a pre-determined number of days are to be regarded as lengthy; I agree with the Upper Tribunal that setting criteria of that kind in advance is neither desirable nor practical. A three-day hearing, as is suggested will be needed for this case, is by no means unusual in this Chamber. But it might nevertheless be unusual for a particular case. I take the example of a late return penalty appeal. Normally such appeals are allocated to the Default Paper category, but the parties may ask for an oral hearing. In such a case the hearing will usually be listed for an hour. If, however, the parties were to say they require three days, it would be difficult to resist the conclusion that the hearing was lengthy for that type of case. What amounts to 'complex evidence', too, is not susceptible of advance definition. Again, as it seems to me, there must be something out of the ordinary - evidence of a technical nature, requiring for its understanding a judge or member with particular experience or training might be an example."

19. Mr Fitzpatrick submitted that the evidence is lengthy and complex, which should be understood as complicated (see *Capital Air Services* at [8]). JSM has served witness statements from five witnesses and has produced four lever arch files of documentary evidence. HMRC do not intend to call any witnesses. Mr West contended that the appeal did not require lengthy or complex evidence. Mr West stated that the bundle of

documents produced runs only to some four lever arch files which is a modest and by no means exceptional amount of evidence by the standards of cases heard by the tribunal.

20. Despite an initial difference of views as to the time required, both parties eventually agreed that the hearing of the appeal should be listed for six days in January 2016. Mr Fitzpatrick submitted that this was a lengthy hearing as it is out of the ordinary for an input tax appeal and was lengthy by comparison with most cases before this tribunal. Mr West submitted that, even if the hearing requires the full six days estimated, that is by no means excessive in terms of many of the appeals which proceed as Standard cases before the tribunal and should not be regarded as a lengthy hearing.

21. As can readily be seen, the parties did not disagree about the nature or volume of the evidence in the case or the likely length of the hearing but, on the same view of the facts, one party, JSM, urged me to regard the evidence as lengthy and complex and the six day hearing as lengthy while the other, HMRC, sought to persuade me to regard the evidence as straightforward and the hearing as nothing out of the ordinary. Having regard to the guidance in *Capital Air Services* and *Dreams* and the submissions of the parties, I am left to form my own view. I do not regard five witness statements, none of which seemed to be particularly long, and four or five lever arch files of documents as at all out of the ordinary in the context of a case concerning entitlement to deduct input tax or in the context of cases in this tribunal generally. The volume of documents is determined by the number of invoices that are subject to challenge and the amount of correspondence between the parties. That volume does not indicate complexity as may, for example, be found in cases that involve evidence of complicated transaction chains and circular payments such as MTIC fraud cases. In my view it cannot be said that this appeal involves lengthy or complex evidence for the purposes of rule 23(4)(a). A hearing of six days is longer than the vast majority of hearings in the tribunal but, in my view, not so lengthy or unusual (especially not for a case concerning whether or not supplies in respect of which input tax has been claimed were actually made) as to justify re-allocating the appeal as a Complex case when considered on its own. In conclusion, I do not consider that this appeal involves lengthy or complex evidence or a lengthy hearing for the purposes of rule 23(4)(a) and, accordingly, it does not satisfy this criterion.

Does the case involve a complex or important principle or issue?

22. Mr Fitzpatrick submitted that the appeal raised an important principle or issue relating to the jurisdiction of the tribunal, conferred by section 83(1)(c) VAT Act 1994, to consider the amount of input tax that may be credited by JSM. The point is whether the unilateral act of a third-party issuing a credit note to a taxpayer deprives the tribunal of jurisdiction to consider whether the taxable person is entitled to deduct input tax on supplies made by the third party. Mr Fitzpatrick referred to HMRC’s statement case which states that the tribunal is “bound to have regard to the results of an insolvency procedure conducted under the relevant legislative provisions and cannot either effectively reconsider the relevant matters itself or reach a contrary conclusion.” He contended that HMRC’s position is that the issue of the credit note by Mr Katz is sufficient to dispose of the appeal because it means that no VAT was charged to JSM by Goldflex. Mr Fitzpatrick contended that the consequence of HMRC’s primary argument, if correct, would be that the tribunal’s jurisdiction was ousted by the credit note issued by Mr Katz. Mr Fitzpatrick also observed that HMRC's position raised issues of EU law in relation to a taxable person’s right to deduct input tax. Mr

Fitzpatrick referred to the decision of the Court of Appeal in *Brunel Motor Company Limited v HMRC* [2009] STC 1146, at [31], and contended that it showed that a credit note is not sufficient in itself to justify a decrease in the consideration for a supply for VAT purposes but there must be some underlying legal entitlement to the decrease in consideration of which the credit note is merely evidence. In the absence of such underlying legal entitlement, to the decrease in consideration, a credit note purporting to reflect such a decrease is ineffective for VAT purposes. As the Chancellor observed in Brunel, at [32], "the task of the Tribunal … was to ascertain whether Brunel had a legal right to the discharge of the original supply."

23. Mr Fitzpatrick contended that HMRC's alternative case also raised an important point, namely whether HMRC may impose, after the supply has been made, specific or general requirements on a taxable person as to the documents that must be held in order to establish a right to deduct input tax incurred on that supply. Mr Fitzpatrick contended that such a requirement is contrary to the decision of the tribunal in *Maliha Group Limited v HMRC* [2011] UKFTT 10 (TC). In that case, the tribunal held that it is not open to HMRC to give directions under regulation 29 of the VAT Regulations 1995 after the time that the right to deduct has arisen.

24. Mr West submitted that the case did not raise any important principle or issue. He stated that HMRC do not see the cases giving rise to any challenge to the tribunal's jurisdiction. HMRC's position is simply that the tribunal must have regard to the fact that the credit note has been issued issued and is not challenged when considering whether Goldflex supplied services to JSM. Mr West submitted that if JSM is correct in its interpretation of *Brunel* then it is a simple and straightforward issue that just requires the reasoning of the Court of Appeal to be applied to the facts of this case. Mr West said that HMRC had not appealed *Maliha Group Limited* but they were not obliged to do so and could still raise the issue which is a simple point which the tribunal can resolve.

25. It is clear from [14] of *Capital Air Services* that what is complex or important must be assessed in the context of taxation and tax appeals. I do not consider that the principal issue in this appeal, ie whether JSM is entitled to deduct the VAT shown on the Goldflex invoices, is complex or important in the context of VAT or tax appeals although it is, of course, very important to JSM. It is sort of issue that is considered by the tribunal on a regular basis. That does not conclude the question of whether the appeal meets the criterion in rule 23(4)(b) because JSM maintains that the subsidiary issues raise important principles or issues. While I accept that the jurisdiction of the tribunal and the status of credit notes are important issues in the general scheme of VAT, the points that arise in this case are neither new nor, in my view, particularly complex (in the sense of complicated). As submitted by Mr Fitzpatrick, issue of the status of a credit note has already been considered by the Court of Appeal in *Brunel* which, unless it can be distinguished, would seem to provide powerful support for JSM's position. There are many authorities on the right to deduct under EU law and the tribunal is familiar and well able to deal with them. As to the issue in relation to regulation 29 of the VAT Regulations 1995, I accept Mr West's submission that it is a straightforward point which the tribunal can decide with or without reference to the earlier decision in *Maliha*. In conclusion, I do not consider that this appeal involves any complex or important principle or issue for the purposes of rule 23(4)(b) and, in my view, it does not satisfy this criterion.

Does the case involve a large financial sum?

26. Mr Fitzpatrick submitted that the amount in dispute, £226,845, is a significant financial sum in the context of tax appeals. He also submitted that I should take account of the fact that JSM has been assessed to corporation tax in the sum of £601,971 seemingly on the basis that if there were no supplies between Goldflex and JSM, JSM had overstated its deductions and understated its profits. Mr Fitzpatrick referred me to be decision of the tribunal in *Babergh District Council v HMRC* [2011] UKFTT 341 (TC) ('Babergh') where, at [34], the tribunal stated:

> "Although the Council's case itself concerns only a relatively small amount of VAT, the legal issues of the case are important and complex, and the outcome of the case involves a very considerable sum of money for the taxpaying community as a whole. A large number of similar appeals have been lodged which, the parties submit, have the potential to be affected by the Tribunal's decision in respect of the Council's appeal."

That led the tribunal in *Babergh* to conclude, at [41], that "having regard to the accepted similarity of a large series of other appeals regarded as depending on the outcome of the council's appeal, the case indirectly satisfies the conditions in rule 23(4)(c)." Mr Fitzpatrick submitted that I should have regard to the wider financial implications for JSM of the outcome of the appeal and not just the VAT amount at issue in the appeal when considering whether this criterion is satisfied. Mr West submitted that the decision in *Babergh* that rule 23(4)(c) was indirectly satisfied was flawed. In any event, HMRC contended that the amount of £226,845 was not a large financial sum and, unlike *Babergh*, there were no other cases stayed pending the outcome of this one.

27. It is clear from [17] of *Capital Air Services* that, in the absence of special factors, it is not appropriate to take into account the financial circumstances of the parties. In *Capital Air Services*, the Upper Tribunal observed, at [24], that "[i]t would be perverse to say a case involving tax of £1,000 involved a large financial sum or that a case involving tax of £100 million did not do so." The FTT in *Dreams* considered how to determine what is a large financial sum in the context of tax appeals. The FTT concluded, at [30], that:

> "… the sum should be large by comparison with the median value of the cases which come before the [Tax] Chamber and are allocated to the Standard and Complex categories. The adoption of that approach, it seems to me, represents a simple and straightforward means of applying the condition."

The FTT concluded that the amount at issue in *Dreams*, £5 million, was a large sum and met the criterion in rule 23(4)(c).

28. The amount at issue in this appeal is £226,845. There are no published statistics that give the median value of appeals before the tribunal and so any judgment as to whether a particular amount is more or less than the median is necessarily one of experience and impression. In my experience and impression of the value of appeals to the FTT generally, I do not consider that this appeal involves a large financial sum. I gain support for my conclusion from (although do not base it on) the fact that Judge Cannan reached a similar conclusion in relation to a slightly greater amount in *Elder v HMRC* [2014] UKFTT 728 (TC).

29. I do not accept Mr Fitzpatrick's submission that I should take account of the fact that JSM would potentially be liable to corporation tax of £601,971 if its appeal is

unsuccessful. The assessment to corporation tax is not the subject of this appeal (nor of any appeal to the FTT) and I do not consider that it would be proper to take it into account for the purpose of deciding whether or not to categorise this appeal as a Complex case. It appears to me that the facts of *Babergh* were very different and the considerations that led the tribunal to take account of wider financial implications do not apply in this case. . In conclusion, I do not consider that this appeal involves a large financial sum for the purposes of rule 23(4)(c) and, accordingly, it does not satisfy this criterion.

Decision

30. In the light of my conclusion that the appeals do not satisfy any of the criteria in rule 23(4) of the FTT Rules, I have no discretion to categorise JSM's appeal as a Complex case and JSM's application must be refused.

Right to apply for permission to appeal

31. 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 under Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must normally be received by this Tribunal not later than 56 days after this decision is sent to that party but, in order to avoid the possibility of either parallel proceedings or a delay in the final resolution of the substantive appeal, I extend the time limit for appealing this decision until 56 days after the release of the decision of the First-tier Tribunal that determines the substantive appeal. 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.

GREG SINFIELD
TRIBUNAL JUDGE

RELEASE DATE: 24 SEPTEMBER 2015