TC06942

Appeal number: TC/2014/03366
TC/2017/07337
TC/2018/03211

PROCEDURE - application for issue of whether "open market value" in Article 72 of the Principal VAT Directive and section 19 VAT Act 1994 is synonymous with "arm's length price" for transfer pricing purposes to be determined as preliminary issue – whether Wrottesley v HMRC applies - application refused

FIRST-TIER TRIBUNAL
TAX CHAMBER

BETWEEN

JUPITER ASSET MANAGEMENT GROUP LIMITED

Appellant

-and-

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

TRIBUNAL: JUDGE GREG SINFIELD

Sitting in public at Taylor House, 88 Rosebery Avenue, London EC1R 4QU on 16 January 2019

Amanda Brown, of KPMG LLP, for the Appellant

Michael Jones, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This decision concerns an application, dated 1 May 2018, by the Respondents ('HMRC') for the Tribunal to make directions providing for the hearing of a preliminary issue to be determined before the parties take any further procedural steps towards the hearing of the other issues in the appeal. HMRC say that the issue of whether "open market value" in Article 72 of the Principal VAT Directive and section 19 of the VAT Act 1994 ('VATA94'), is synonymous with the concept of an "arm's length price" for transfer pricing purposes and, if so, the extent to which OECD Transfer Pricing Guidelines can be relied on to determine open market value for VAT purposes needs to be determined for the purposes of resolving the substantive dispute between the parties. HMRC contend that the nature of the issue is such that it would be fair, just and convenient to determine it as a preliminary matter.

Background

2. For the purposes of this decision, the background to the appeal can be summarised quite briefly as follows. The summary is taken from the statements of the background facts provided by the parties for the purpose of the application and should not be contentious but, as I was not provided with any evidence in relation to the factual background, none of what follows is to be taken as a finding of fact.

3. The Appellant ('JAMG') is the representative member of a VAT group ('JAMG VAT Group'). The JAMG VAT Group includes Jupiter Fund Management Plc ('JFM') and Jupiter Fund Management Ltd ('JFML'). JFM is the ultimate parent company of the corporate group.

4. JAMG holds a controlling interest in Jupiter Investment Management Group Ltd ('JIMG') which is the representative member of a separate VAT group ('JIMG VAT Group'). JIMG holds all the shares in a number of subsidiaries which are members of the JIMG VAT Group. The members of the JIMG VAT Group carry on investment fund management business in the course of which they make both taxable and exempt supplies.

5. During the relevant VAT accounting periods, a company or companies within the JAMG VAT Group provided management services to members of the JIMG VAT Group. The JAMG VAT Group charged for these services and was thus engaged in an economic activity for VAT purposes. JAMG, as representative member of the JAMG VAT Group, accounted for output tax on the supplies of management services by members of the group. The management services were priced at an arms-length value in accordance with transfer pricing principles. Various costs were incurred by the JAMG VAT Group and, in its VAT returns, JAMG deducted all the VAT incurred as input tax on those costs on the basis that it was wholly attributable to taxable supplies. During the periods in issue, the JAMG VAT Group did not make any taxable supplies to any third parties.

6. Following visits to JAMG, HMRC formed the view that the JAMG VAT Group was not entitled to recover as input tax the VAT incurred by it in relation to the management services. HMRC assessed JAMG for the input tax. In the alternative HMRC considered that JAMG had under-valued the management services supplied to the JIMG VAT Group. Consequently, on 23 May 2014, HMRC issued a Notice of Direction of Open Market Value ('OMV Direction') under paragraph 1 of Schedule 6 to the VATA94 to JAMG. The effect of the OMV Direction was that, for VAT purposes, the value of supplies of management services by the JAMG VAT Group should be taken to be the open market value of those supplies. Following the issue of the OMV Direction, HMRC issued assessments for under-declared output tax.

7. JAMG, as representative member of the JAMG VAT Group, appealed against both the input tax assessments and the output tax assessments. Since the assessments were issued, HMRC has changed its view (following the CJEU's judgment in *Beteiligungsgesellschaft Larentia + Minerva mbH & Co KG v Finanzamt Nordenham* (Cases C-108/14 and C-109/14 [2015] STC 2101) and now the output tax assessments are HMRC's "preferred" assessments. The input tax assessments are the "alternative" assessments.

8. HMRC served its Statement of Case in the appeal proceedings on 28 February 2018. In relation to the output tax assessments, the Statement of Case sets out HMRC's position as follows:

> "22. Contrary to the position adopted by JAMG in its Substituted Grounds of Appeal the concept of 'open market value' as defined in Article 72 of the Directive and s.19, VATA 1994 does not, or does not necessarily, equate with the transfer pricing concept of an 'arm's length price'.
>
> 23. Further, not only does the definition of 'open market value' make no reference to, or otherwise import, the OECD Transfer Pricing Guidelines, but the concept is an autonomous one which must be applied equally across all member states. In the latter regard it is therefore highly material that not all the member states are members of the OECD, and that even those who are may not have implemented the Guidelines into their law. An autonomous, EU-wide definition of 'open market value' cannot depend on guidelines which are, or may be, relevant in some member states and not others. JAMG's reliance on the OECD Guidelines is accordingly misconceived.
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> …
>
> 25. In this case, applying the definition of 'open market value' in Article 72, by reference to which the same term in s.19(5), VATA 1994 is to be read:
>
> (1) There is no comparable service as referred to in the first part of the definition, given that the provision of management services by a holding company to its subsidiaries will inevitably not be carried out at arm's length. Accordingly, the open market value is an amount that is not less than the full cost to JAMG of providing the service.
>
> (2) Alternatively, insofar as a comparable service can be ascertained, a supplier acting at arm's length would charge an amount at least equal to the full cost to the supplier of providing the service."

9. There then follows a separate argument in relation to the output tax assessments based on the proposition that the costs incurred by JAMG in order to provide the management services must be at least equal to the costs in respect of which it claims input tax and therefore the open market value of its supplies of management services cannot be less than the costs in respect of which JAMG makes those input tax claims. It is clear from the Statement of Case that the concept of 'open market value' and thus the value of the supplies of management services made by the JAMG VAT Group and amount of VAT for which JAMG is liable to account is central to the output tax assessments. The Statement of Case also sets out HMRC's position in relation to the input tax assessments but that is not relevant for the purposes of the application described below.

10. Following the service of the Statement of Case, it appears to be common ground that the issues to be determined in this appeal are:

> (1) What is the open market value of the supplies of management services by the JAMG VAT Group on which JAMG is liable, as representative member, to account for VAT?
>
> (2) To what extent is JAMG entitled to recover as input tax the VAT incurred by it?

HMRC's application

11. The first paragraph of HMRC's application summarises the application as follows:

> "HMRC apply to the tribunal for directions in the form appended to this application. Those directions make provision for the hearing of a preliminary issue, which, for the reasons set out below, HMRC submit it is fair, just and convenient to determine before the parties take any further procedural steps towards the hearing of the substantive issues."

12. The reason for the application is given at paragraph 4:

> "4. A key point of contention between the parties concerns the meaning of 'open market value', as defined in Article 72 of the Principal Directive and s.19 of the VAT Act 1994, and in particular:
>
> (1) whether the concept of 'open market value' for VAT purposes is always synonymous with the concept of an 'arm's length price' for transfer pricing purposes; and
>
> (2) whether, and if so then to what extent, the OECD Transfer Pricing Guidelines can properly be relied on in order to arrive at an 'open market value' for VAT purposes."

13. The application then states that HMRC's position is that "the autonomous nature of the concept of 'open market value' for VAT purposes precludes reliance on material such as the OECD Transfer Pricing Guidelines [said by HMRC to be relied on by JAMG], which do not apply in all member states of the EU." Paragraph 6 of the notice of application then states:

> "This point will therefore need to be determined for the purposes of resolving the substantive dispute between the parties, but HMRC submit that the nature of this issue is such that it would be fair, just and convenient to determine it as a preliminary matter."

14. Paragraphs 7 – 10 of the application give reasons why, in the opinion of HMRC, the issue of the meaning of open market value for VAT purposes should be determined as a preliminary matter. Paragraph 11 states that "HMRC apply for directions that the issue described in paragraph 4 … be determined as a preliminary matter."

15. The directions sought are appended to the application. The first is the standard direction that the parties provide their lists of documents on which they intend to rely and produce in connection with the appeal and provide to the other party copies of any such documents not previously provided. That direction is not controversial. The second proposed direction is:

> "**Preliminary issue hearing**: Not later than [14 days after the date of the issue of these directions] both parties shall send or deliver to the Tribunal

> and each other their dates to avoid for a one day hearing for the period beginning [4 June 2018] and ending [27 July 2018]."

Clearly, the dates must be now amended but nothing turns on that. The remaining directions relate to the preparation and service of bundles and skeleton arguments for the hearing of the preliminary issue.

HMRC's skeleton argument

16. Mr Jones, who appeared for HMRC, served a skeleton argument in advance of the hearing. The first paragraph of the skeleton states that HMRC are applying for "directions [that] make provision for the hearing of a preliminary issue, which, for the reasons set out below, HMRC submit it is fair, just and convenient to determine before the parties take any further procedural steps towards the hearing of the substantive issues." Paragraph 4 of the skeleton argument is, word for word, in the same terms as paragraph 4 of HMRC's application set out at [11] above. Save for the insertion of the word "foregoing", paragraph 7 of the skeleton argument is identical to paragraph 6 of HMRC's application, quoted in [13] above. The reasons why, in HMRC's view, the Tribunal should determine the issue of the meaning of 'open market value' for VAT purposes and whether (and, if so, to what extent) the OECD Transfer Pricing Guidelines can be relied on as a preliminary matter are found in paragraphs 8 to 14 of the skeleton argument and I discuss those below. The skeleton argument concludes with paragraph 15, which is in the same terms as paragraph 11 of the application, and the same draft directions that had been appended to the application.

Submissions at the hearing

17. Notwithstanding that HMRC's application and skeleton argument sought a direction for the hearing of a preliminary issue, the skeleton argument did not contain any reference to *Wrottesley v HMRC* [2015] UKUT 637 (TCC) ('*Wrottesley*'). *Wrottesley* is a decision of the Upper Tribunal which discusses the proper approach to the question of whether to order a hearing of a preliminary issue. The reason for this omission became apparent at the hearing where Mr Jones began by stating that HMRC were not seeking a preliminary issue hearing but a case management hearing. This appeared to come as a surprise to Mrs Brown, representing JAMG, who immediately stated that this was not the application that had been made.

18. Mrs Brown's skeleton argument (served in advance of the hearing but after HMRC's skeleton had been served) relied heavily on *Wrottesley*. At [28] of the decision in *Wrottesley*, the Upper Tribunal sets out eight key principles to be considered by a tribunal when dealing with an application for a preliminary hearing. In her skeleton argument, Mrs Brown submitted that HMRC's application failed to satisfy many of the conditions that were contained in the *Wrottesley* principles.

19. I do not need to set out the discussion of the eight key principles in *Wrottesley* or in Mrs Brown's skeleton argument because Mr Jones accepted that an application for a preliminary issue hearing must fail because it did not meet the *Wrottesley* criteria. For example, Mr Jones acknowledged that a decision on the open market value issue described in paragraph 4 of the application would not be a "knockout blow" because HMRC would still contest the appeal even if JAMG's view were upheld and whatever the FTT decided. Mr Jones was right to concede that the conditions in *Wrottesley* could not be satisfied (especially, in my view, those found in sub-paragraphs 2, 3 and 5 of [28]).

20. Mr Jones acknowledged that HMRC's application could have been better worded to make clear that it was not an application for a preliminary issue hearing in the *Wrottesley* sense

but was an application for a case management hearing. He contended that was, however, clear from paragraph 6 of the application and from the reasons given in support of the application in his skeleton.

21. I cannot read paragraph 6 of the application as referring to anything other than a preliminary issue hearing in the *Wrottesley* sense. That is the only reading that is consistent with paragraph 4 and the appended draft directions which all concern the steps necessary before a hearing to determine the issue described in that paragraph in advance of a hearing to determine the other issues in the appeal.

22. The first reason in support of the application is given in paragraph 8 of the skeleton argument. That reason is that a preliminary hearing would allow the parties to consider whether expert evidence on transfer pricing is required for the purposes of the main hearing. An alternative reason in favour of a preliminary hearing, found in paragraph 9 of the skeleton argument, is that if expert evidence on transfer pricing is required, it would enable the parties to ensure that such evidence is focussed on the appropriate issue or issues. Paragraph 10 adds that early resolution of the dispute about the relevance of transfer pricing concepts to the definition of "open market value" for VAT purposes would potentially assist in narrowing the factual evidence required for the main hearing and thereby save tribunal time and resources. Paragraphs 11 to 14 set out reasons against leaving the issue to be resolved, together with the other issues, at the substantive hearing which may be summarised as it risked wasting time and costs if evidence was called that later (assuming the Tribunal upheld HMRC's view) turned out to be unnecessary.

23. At the hearing, Mr Jones acknowledged that, effectively, HMRC were applying for a preliminary hearing because they hoped to exclude the evidence put forward by JAMG relating to the OECD guidelines from the substantive appeal. He submitted that the purpose of the application and any preliminary hearing was to determine the evidence that would be needed for the hearing of the substantive appeal. HMRC's application was based on their understanding that JAMG sought to argue that the concept of "open market value" for VAT purposes equated with the OECD/transfer pricing concept of an "arm's length price". Mr Jones pointed out that JAMG's grounds of appeal also rely very heavily on principles from the OECD's Transfer Pricing Guidelines and, in addition, JAMG had sought to adduce an independent transfer pricing review by KPMG's transfer pricing department in evidence. HMRC's position is that the OECD guidelines are simply not relevant to the determination of open market value for VAT purposes as that is defined by the terms of Article 72 of the Principal VAT Directive. Mr Jones contended that the Tribunal should determine whether expert evidence was permitted or required in relation to this issue and, if so, the nature of the expert evidence required. Mr Jones said that if the OECD guidelines could not be taken into account then that would knock out one argument in the appeal which would reduce the evidence and time required at the substantive hearing.

24. Mr Jones argued that *Wrottesley* was not relevant where the issue of law to be decided arose not as a preliminary issue to dispose of all or part of the appeal but in the course of an application for case management directions. He said that a decision on the issue of the significance of transfer pricing concepts in determining the meaning of "open market value" for VAT purposes was a necessary step in the Tribunal deciding what evidence was required for the substantive hearing. That was not the same thing, in his submission, as a preliminary issue in the *Wrottesley* sense. He pointed out that points of law often fall to be decided in interlocutory applications but these are not subject to the *Wrottesley* conditions.

25. Mrs Brown, in opposing the application, stated that the Appellant's case is not and never has been that the transfer pricing concept of "arm's length price" is necessarily synonymous with "open market value" in Article 72 of the Principal VAT Directive. JAMG's position is that the objective of both concepts is to determine what the value of services between connected parties would be if there were no such connection. JAMG contends that the approach to determining an appropriate transfer price for the management services informs the approach to be adopted in determining the open market value for VAT purposes. In summary, Article 72 provides that, where there are comparable services, 'open market value' means the amount that a customer would have to pay an arm's length supplier for the services. JAMG says that, in that context, the OECD Transfer Pricing Guidelines are useful evidence in determining what is an open market value. Mrs Brown also relied on the points made in her skeleton in relation to *Wrottesley*.

Discussion

26. Mr Jones tried to get round the hurdle placed in his way by *Wrottesley* by saying that the application was (or, perhaps, should be regarded as) an application for a hearing to give directions on the evidence permitted or required at a hearing of the substantive appeal. He submitted that, in order to determine what evidence should be permitted or required, the Tribunal would have to determine the issue of whether "open market value" for VAT purposes is synonymous with the concept of an "arm's length price" for transfer pricing purposes and, if so, to what extent the OECD Transfer Pricing Guidelines can properly be relied on in order to arrive at an "open market value" for VAT purposes.

27. Despite Mr Jones's attempts to persuade me otherwise, HMRC's application is clearly for a direction that there be a hearing to determine an issue in the appeal as a preliminary matter. It simply cannot be read in in any other way. The language of the application and the skeleton argument is clear. Whether the preliminary hearing is described as a case management hearing or a preliminary issue hearing is nothing to the point. However the purpose of the application is described, the issue to be decided at the preliminary hearing is not merely what evidence should be permitted or required at the substantive hearing but is a central (although not determinative) issue in the appeal against the output tax assessments. Nor does it matter that the outcome of the hearing would not only be a decision on the issue but also some case management directions (although, I note, no such directions are included in the application and draft directions submitted by HMRC). It follows that the principles set out by the Upper Tribunal in *Wrottesley* are relevant and, as Mr Jones conceded, the inevitable conclusion is that the conditions for directing that an issue in the proceedings should be dealt with at a preliminary hearing are not met. Accordingly, HMRC's application must be refused.

28. Although I concluded at the hearing that HMRC's application must be refused, I nevertheless also considered Mr Jones's submissions on the application on the basis that it was for a case management hearing and that, quod non, *Wrottesley* did not apply. The Tribunal may direct that an issue in proceedings can be dealt with as a preliminary issue under rule 5(3)(e) of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ("FTT Rules"). In considering whether to deal with an issue as a preliminary issue, the FTT will seek to give effect to the overriding objective of the FTT Rules to deal with cases fairly and justly (rule 2(1)). That objective includes dealing with the case in ways that are proportionate to the complexity of the issues and avoiding delay so far as compatible with proper consideration of the issues.

29. HMRC seek a direction that there should be a hearing at which the question of whether the concept of "arm's length price" and the OECD Transfer Pricing Guidelines are relevant to

the open market value issue is determined in order to decide what evidence will be required or permitted at the substantive hearing. In his skeleton, Mr Jones says that such a direction "will *potentially* assist in narrowing the factual evidence required for the main hearing and thereby save tribunal time and resources" (my emphasis). He also states that "that little additional cost will be occasioned by dealing with the point in the manner suggested" which seems to accept that there will be some additional cost.

30. In deciding whether to direct a preliminary hearing, I must consider what is the most efficient and effective way of dealing with the issues in the appeal consistent with the overriding objective. In my opinion, a preliminary hearing to determine the issue raised by HMRC would not result in any saving in the overall time required to dispose of this appeal. It might, of course, result in a shorter subsequent hearing of the remaining issues but that is not the same thing. Further, I consider that there is a real risk that, in order to resolve it, the Tribunal might have to refer the question of whether the concept of "arm's length price" and the OECD Transfer Pricing Guidelines are relevant in determining "open market value" for VAT purposes to the Court of Justice of the European Union ('CJEU'). I say that because, as both parties acknowledge, the issue raised is one of interpretation of the Principal VAT Directive and there are no existing CJEU judgments on that precise point. If there were to be a reference to the CJEU at the preliminary hearing stage then that would, inevitably, result in a considerable delay to the substantive hearing. It seems to me that as, on HMRC's own submissions, any saving of time and resources is uncertain and there would be some additional cost and, in my view, there is a real risk of substantial delay, a preliminary hearing to consider the issue in HMRC's application would not be consistent with the overriding objective. Accordingly, even if *Wrottesley* did not apply, I would have refused HMRC's application for directions for the hearing of a preliminary issue.

31. As I explained at the hearing, I can see the benefit of having case management directions that provide for the parties to agree (if possible) and set out the issues in the appeal. That is commonly done in the more complicated appeals but usually at a later stage. In an appeal such as this, I consider that there would be a real advantage to both parties in having the issues agreed at an early stage so that they could both know the case that they had to meet and consider what evidence may be required to support it well in advance of the hearing of the appeal. Accordingly, I asked the parties to agree directions for the provision of a list of agreed issues. Such a list would be useful to the parties and the Tribunal in deciding what further directions might be necessary for the effective case management of this appeal.

32. I have one final point. Although I do not know the reason why HMRC's application at the hearing differed so markedly from the way it was put in the application of 1 May 2018 and Mr Jones's skeleton argument, if HMRC had concluded, on reflection, that their application as drafted could not succeed because they could not meet the conditions set out in *Wrottesley*, the proper course was to amend the application or withdraw it and make a new one. At the very least, it would have been helpful to state that, in HMRC's view, *Wrottesley* was not relevant to the application. Only by doing so could HMRC ensure that JAMG and the Tribunal knew in advance exactly what directions were being sought and the reasons relied on in support of the application. The failure to make those things clear in the application and skeleton argument led to misunderstanding and the confusion that was apparent at the beginning of the hearing.

Decision

33. For the reasons given above, HMRC's application for directions providing for the hearing of a preliminary issue is refused. The parties are directed to submit within five days of the date of release of this decision agreed draft directions or, if agreement proves impossible, separate

draft directions for the agreement and service of a list of agreed issues within a time limit to be specified in those directions.

Right to apply for permission to appeal

34. 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.

GREG SINFIELD
TRIBUNAL JUDGE

RELEASE DATE: 25 JANUARY 2019