



TC02655

Appeal number: MAN/2008/1577

*VAT – preliminary issue – whether assessment out of time – s 80(4) VATA
1994 - regulation 94B VAT Regulations 1995 – meaning of “payment”*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

MR MARK REID (practising as REID & CO. SOLICITORS) Appellant

- and -

**THE COMMISSIONERS FOR HER MAJESTY’S Respondents
REVENUE & CUSTOMS**

TRIBUNAL: JUDGE PETER KEMPSTER

Sitting in public at Birmingham on 18 July 2012

**Mr David Yates of counsel, instructed by Smith & Williamson LLP, for the
Appellant**

**Mr Richard Chapman of counsel, instructed by the General Counsel and
Solicitor to HM Revenue and Customs, for the Respondents**

DECISION

1. This is the determination of a preliminary issue in the appeal of the Appellant (“Mr Reid”) against an assessment to VAT in the amount of £499,083 (“the Assessment”) issued by the Respondents (“HMRC”) on 8 December 2008.

2. Mr Reid practises as a solicitor in the name Reid & Co Solicitors. As well as the usual legal services provided by a solicitor, Mr Reid has provided services as an intermediary for prospective purchasers of capital redemption bonds and he maintains that those intermediary services are exempt from VAT (by virtue of item 5, group 5, sch 9 VATA 1994). HMRC dispute the exempt status of those supplies - hence the Assessment - but that point (although central to the substantive appeal) is not yet before the Tribunal. Rather, the Tribunal is asked to determine whether the Assessment is out of time; HMRC accept that part of the Assessment is time barred but Mr Reid contends the entire amount is invalid.

3. The preliminary issue as stated by the parties is: “What amount of [the Assessment] is time barred by operation of the three year time limit set out in VATA 1994 s 80(4) in force as at 8 December 2008?”

Evidence

4. Mr Reid has been registered for VAT since 2001. His VAT quarters are 31 March, 30 June, 30 September and 31 December.

5. The Assessment relates to four invoices issued by Reid & Co (“the Invoices”). The Invoices were issued to four companies: GW223 Limited (“GW223”), Wares Hercules Limited, Hercules Limited and JMNI Limited (the last three companies together “the Three Sister Companies”). GW223 and the Three Sister Companies are all subsidiaries of a holding company called TOE Holdings Limited, of which Mr Reid owned 50%. The Invoices relate to services provided in the year ended 31 March 2005. The Invoices were issued in January 2006 but were dated 31 March 2005. It is common ground that none of the Invoices constituted formal VAT invoices within the meaning of the VAT legislation. It is also common ground that Mr Reid did not receive any cash in relation to any of the Invoices before 1 April 2006 (the significance of which date will be explained below).

6. The recording of the commission invoices in the accounting records was described by Mr Reid in his witness statement as follows:

“Recording the Reid & Co commission invoices in the books and records

10. The VAT assessment issued on 8 December 2008 concerns four invoices from Reid & Co in respect of intermediary services provided during the 12 months to 31 March 2005. These invoices were dated 31 March 2005 but were issued in January 2006 and were reflected in the audited accounts of the recipient companies for the year

to 31 March 2005. These accounts were signed by me as Company Secretary on 20 January 2006. I exhibit copies of the financial accounts of the four relevant companies for the year to 31 March 2005 at Exhibit D.

5 11. When the Reid & Co invoices were received, apart from that relating to GW223 Ltd discussed below in paragraph 12, they were entered into the books and records of the three companies (other than GW223 Ltd) by posting the invoiced amounts to the Creditors Control Account in each company, with an equal and opposite debit entry to 10 the Commissions Payable account, reflected in the relevant company's Profit and Loss Account. Book entries for the invoices were then made which debited the Creditors Control Account for that company and credited the inter-company account for GW223 Ltd. A corresponding entry in the books and records of GW223 Ltd was made debiting the 15 inter-company account with each of the three companies (Hercules Products Ltd, Wares Hercules Ltd and JMNI Ltd) and crediting the Mark Reid Directors Loan Account in GW223 Ltd for the same amount. Thus the commission due to Reid & Co was correctly reflected in the Profit and Loss Account of each company. The 20 bookkeeping was carried out in this way for administrative convenience.

25 12. The Reid & Co commission invoice to GW223 Ltd was credited to the Mark Reid Directors Loan Account in GW223 Ltd and debited to the Commissions Payable account reflected in the Profit and Loss Account.

The Mark Reid Directors Loan Account

30 13. The Mark Reid Directors Loan Account in GW223 Ltd is a ledger account recording amounts due to me including Reid & Co and how these have been dealt with. This is the only Directors Loan Account that exists; I do not have a Directors Loan Account when [*sic*] any of the other three companies concerned. At no time have I owed any monies to GW223 Ltd and the Directors Loan Account has always been in credit. Exhibit E details the postings in the Mark Reid Directors Loan Account for GW223 Ltd for the period 1 April 2004 to 35 31 March 2006.

Payments from GW 223 Ltd

40 14. Exhibit E shows the four commission invoices which are the subject of the V AT assessment, credited to the account with the date 31 March 2005 (even though the posting to the account took place in January 2006). No payments have been made in respect of these four invoices. The ledger shows four payments to me between 1 October 2005 and 31 March 2006 all of which relate to loan withdrawals and were not related to the commission invoices.

45 15. Three payments were made to me in early 2005, within the period of six months after 30 September 2004: £160,000 on 14 February 2005; £203,150 on 25 February 2005; and £100,000 on 4 March 2005. None of these payments was specifically allocated to any commission amounts due to me. The payments were made before the commissions represented by the V AT assessment were credited to the

Directors Loan Account in January 2006, with the date 31 March 2005.”

7. In his oral evidence Mr Reid stated:

- 5 (1) The accounting adopted was for administrative ease.
- (2) It was effected by a lady in the firm’s accounts department who he believed would have given no consideration to the legal niceties or legal effect of the various bookkeeping entries.
- (3) The accounts of the companies had been finalised by the auditors.
- 10 (4) Mr Reid had signed some of those accounts as company secretary of the relevant company.

8. Note 9 to the audited statutory accounts of GW223 for the year ended 31 March 2005 showed “Directors’ current accounts” balance of £8,895,080 contained in the item “Creditors: amounts falling due within one year”. Mr Reid stated that this
15 balance was approximately evenly split between himself and his co-director Mr Emblin. Note 14 to those accounts gave “Related party disclosures” as follows:

“RELATED PARTY DISCLOSURES

20 Both Mr Simon Emblin and Mr Mark Reid are directors and shareholders of the company. During the year the company has traded with both JMNI Associates and Reid and Co of which Mr Simon Emblin and Mark Reid is sole proprietor and partner respectively

25 During the year the company has traded with both businesses and been charged commission of £2,512,004 (2004: £591,586) by JMNI Associates and £2,512,004 (2004: £591,587) by Reid & Co Solicitors in respect of these transactions. Reid & Co Solicitors have recharged expenses of £48,338 to GW223 Limited

At 31st March 2005 no amounts are owed to or from Reid & Co Solicitors and JMNI Associates.

30 Exemption has been claimed under Financial Reporting Standard number 8 regarding the disclosure of group transactions and transactions with associated companies on the basis that consolidated accounts are publicly available.”

9. Mr Reid stated:

- 35 (1) JMHI Associates was the business style of Mr Emblin.
- (2) The reference to Reid & Co was really to Mr Reid himself – he was the only equity partner in the firm and so the firm was his alter ego. The Commissions were invoiced by Reid & Co.
- 40 (3) In stating that no amounts were owed to Reid & Co the note to the accounts was referring to legal fees; the firm was not owed any legal fees by the

company. The note should not be read as stating that nothing was due to Mr Reid; he certainly had not treated the commissions as satisfied.

(4) Mr Reid accepted that the 2005 and 2006 accounts of GW223 were audited accounts and had been signed by himself as company secretary on behalf of the board.

10. In the accounts of GW223 for the year ended 31 March 2006 the corresponding entries were that Note 9 gave £2,857,345 as Directors' current accounts and £3,691,158 (2005 comparative: Nil) as Amounts due to related companies, both contained in the item "Creditors: amounts falling due within one year", and Note 15 stated "Related party disclosures" as follows:

"RELATED PARTY DISCLOSURES

Mr Simon Emblin, Mr Mark Reid and Mr Stuart Drury are directors of the company. During the year the company has traded with Reid and Co Solicitors a firm in which Mark Reid is partner. The company has also traded with Redbox Associates, a business in which all directors of GW223 Limited are partners.

During the year Reid & Co solicitors have recharged expenses of £194,602 (2005:£48,338) to GW223 Limited. At the end of the year the company owes £1,922,339 to Mark Reid.

During the year Redbox Associates has charged introductory commission to GW223 Limited of £747,000 (2005 - £nil). At 31st March 2006 £1,768,819 is outstanding to Redbox Associates (2005: £Nil).

Exemption has been claimed under Financial Reporting Standard number 8 regarding the disclosure of group transactions and transactions with associated companies on the basis that consolidated accounts are publicly available."

11. Mr Reid explained that Redbox Associates was a partnership commenced after March 2005 involving himself, Mr Emblin and others.

12. At the hearing there were produced on behalf of the Appellant further documents, which I admitted. Those documents relating to the 2006 accounts of GW223 were introduced into the proceedings late, but I was satisfied that HMRC had the opportunity to consider them and, indeed, Mr Chapman for HMRC cross-examined Mr Reid on certain points and addressed the documents in his submissions. These included an email from the auditors sent to the Appellant two days before the hearing to give an explanation of the accounting entries in relation to the directors' loan accounts. It stated:

"The schedule below is re the directors loan account at 31st March 2006 from our files. The entry for £4,365,729.27 is to clear the balance to nil. In this year you reassigned many of the balances from DLA to related party balances. As far as your SAGE is concerned a one line entry would be made rather than each individual entry being made."

Legislation

13. Section 80(4) VATA 1994 as in force at the date relevant to these proceedings provided:

5 “(4) The Commissioners shall not be liable on a claim under this section—

 (a) to credit an amount to a person under subsection (1) or (1A) above, or

10 (b) to repay an amount to a person under subsection (1B) above, if the claim is made more than 3 years after the relevant date.”

14. The annex to this decision notice sets out the wording of reg 94B VAT General Regulations 1995 (SI 1995/2518) as in force at the date relevant to these proceedings. I have interpreted the purpose and effect of reg 94B as follows, which I understand is not controversial between the parties.

15 15. Regulation 94B is an antiavoidance provision. It bites where the supplier and customer are not at arms’ length (reg 94B(2)) and the customer is unable to reclaim all the VAT on the services (reg 94B(3)). The temptation in those circumstances might be to delay invoicing or paying for the continuous supplies of services, so that the time of the supply (ie the tax point) is delayed (perhaps indefinitely) and no VAT need be accounted for. To prevent such manipulation reg 94B deems there to be a supply annually - to the extent the services have been provided and unless the services have already been treated as supplied (reg 94B(5)). To remove unobjectionable cases where invoicing is performed annually, reg 94B(6) disappplies the deemed annual supply where a VAT invoice is issued, or payment is received, no later than six months after the date of supply otherwise deemed by reg94B(5).

16. The antiavoidance provision was introduced in 2003 and bites on “supplies of ... services the benefit of which was received after the coming into force of” The VAT (Amendment) (No 5) Regulations 2003 (SI 2003/3102) (reg 1(2) thereof) – which date is stated to be 1 October 2003 (reg 1(1) thereof). The parties agreed that the date on which the benefit of supplies was received was synonymous with the date on which supplies were provided. The deemed annual supply rule in reg 94B(5) takes into account this commencement date – see reg 94B(5)(a) & (b). The parties also agreed that the disputed supplies were “supplies the provision of which commenced on or before 1st October 2003”. Thus the deemed annual supply rule in reg 94B(5) can for the purposes of the current proceedings be condensed to the following:

40 “Where this regulation applies... services shall, to the extent that they have not already been treated as supplied ..., and to the extent that they have been provided, be treated as separately and successively supplied ... at the end of the period of twelve months after [1st October 2003] ... and thereafter at the end of each subsequent period of twelve months.”

17. So (for the purposes of the current proceedings) the first reg 94B deemed annual supply was on 30 September 2004, and subsequent reg 94B deemed supplies were on 30 September 2005, 30 September 2006 etc.

5 18. This deemed supply of services only arises “to the extent that they have not already been treated as supplied ..., and to the extent that they have been provided”.

19. Regulation 90 provides (so far as relevant):

10 “... where services ... are supplied for a period for a consideration the whole or part of which is determined or payable periodically or from time to time, they shall be treated as separately and successively supplied at the earlier of the following times—

(a) each time that a payment in respect of the supplies is received by the supplier, or

15 (b) each time that the supplier issues a VAT invoice relating to the supplies.”

20. Regulation 94 provides (so far as relevant):

20 “... a supply is treated as taking place each time that a payment (however expressed) is received or an invoice is issued, the supply is to be treated as taking place only to the extent covered by the payment or invoice.”

21. The meaning of “payment” for these purposes was the subject of submissions from both parties.

Appellant’s case

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22. Mr Yates for Mr Reid submitted as follows.

23. The concept of “payment” within reg 94B was not purely an English law concept but should be understood to equate to “receipt of price” – see Art 10(2) of the Sixth Directive. This had been considered by the Court of Appeal in *C&E v British Telecom plc* [1996] STC 818 and the ECJ in *BUPA Hospitals Ltd v C&E* [2006] STC 967. Simple recognition of indebtedness in a company’s accounts did not constitute “payment” within the meaning of reg 94B or Art 10. HMRC’s reliance on *Pentex Oil Ltd v C&E* (1992) (V7991) was misconceived; at best that case was supportive of the proposition that to the extent that accounting entries recognise a set-off then that constituted “payment”. That was HMRC’s own interpretation of *Pentex* as set out in its VAT Manual (at VATTOS5160):

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“To create a tax point based on the date the accounts are approved, it is necessary for those accounts to also demonstrate that the debt has been discharged. This cannot be the case if, for example, the amount in

question is also shown as an outstanding item on the respective balance sheets under debtors/creditors”

24. That was also supported by the VAT Tribunal decision in *Cater Clark v HMRC* (2008) (V20546) where (at para 35) the Tribunal stated *obiter*:

“Whilst “payment” can mean something other than the simple transfer of cash, its meaning will depend upon the context. [HMRC’s officer witness] indicated that it was HMRC’s view that the payment was made when the accounts were signed. We note that in *Customs & Excise Commissioners v Svenska International*[1999] STC 406, when an invoice was issued representing 5 years accrued supplies there seems to have been no argument that any accrual of the amounts receivable and payable constituted payment. We also note that the purpose of Regulation 94B appears to be to deal with the issue of the provision of services between group companies which are not VAT grouped where neither regular payment nor invoicing occurs, and the recipient company could not reclaim all its tax. That at the least suggests that “payment” in Regulation 90 may not encompass the accrual of rights and liabilities in the accounts of the companies concerned.”

That approach must be correct. Otherwise, other provisions of the VAT legislation – for example, bad debt relief – would become inoperable in practice.

25. HMRC’s references to certain income tax authorities added nothing to the VAT position under consideration in these proceedings.

26. The relevant loan account throughout the relevant period was only ever in credit for the benefit of Mr Reid. There was therefore no question of a set-off occurring. Simple journal entries without a payment of cash could therefore not constitute payment.

27. It followed that the entire period to 31 March 2005 was time-barred from assessment.

Respondents’ case

28. Mr Chapman for HMRC submitted as follows.

29. The case turns upon whether or not Mr Reid received “payment” within six months of 30 September 2005.

30. In Art 10 “receipt of price” means the same as “payment”, as “receipt” is to be equated with satisfaction. “Payment” need not be the transfer of a cash sum – In *Pentex Oil* the VAT Tribunal stated (fourth paragraph of decision):

“We agree with the passage in *De Voil* at A5.42 where the learned author says ‘payment may be made by offsetting a debt owed against a

5 debt due e. g. by journal transfer between purchase and sales ledger
accounts, or by making a credit entry in an inter-company current
account having a debit balance. The time of payment in these
circumstances seems to be the date on which the appropriate entry is
made in the accounting records.' It was pointed out by Lord Evershed
MR in *White v Elmdean Estates Limited* [1959] 2 All ER 605 at page
610 (affirmed by the House of Lords at [1960] 1 All ER 306)) 'the
word 'payment' in itself is one which and in the appropriate context
may cover ways of discharging obligations, it may even ... include a
10 discharge, not by money payment at all, but by what is called 'payment
in kind". In our view the tax point in this case was the date of the
respective debits and credits and that the Value Added Tax returns
were incorrect in that they did not use these dates as tax points."

15 31. "Payment" could also be satisfied by set-off of pre-existing liabilities – see *RCC
v Enron Europe Ltd* [2006] EWHC 824 (Ch) per Lightman J (at para 28).

32. The test for "payment" is whether the obligation to pay is discharged. In *CCE v
Faith Construction Ltd* [1993] 1 QB 905 Parker LJ stated (at p 917):

20 "Given that the payments, although made under arrangements which
fettered the recipient's use of the money received, discharged the
liability of the customer under the building contract and left the
recipient with no right to sue for payment thereunder, I can see no
alternative but to conclude that in each case payment was made before
1 June and accordingly that the Crown's contention that payment was
25 not received until, in the cases of *Faith* and *West Yorkshire*, there was
partial repayment of the loan and, in the cases of *Dormers* and
Nevisbrook, the money was released from the deposit account, is
unsustainable."

30 33. The passage cited by the Appellant from para 36 of the VAT Tribunal's
decision in *Cater Clark* was *obiter* and tentative, and possibly in conflict with *Faith
Construction*. In any event, the provision for rights and liabilities in respective
accounts is to be distinguished from a formal reconciliation within an inter-company
account.

34. Similar conclusions could be drawn from authorities concerning the equivalent
35 provisions in the context of income tax on employment income.

35. The accounting process adopted in the current case was sufficient to constitute
payment, for the following reasons:

1. The right to payment is Mr Reid's (trading as Reid & Co) rather than
GW223's.
- 40 2. Note 14 to GW223's 2005 accounts state that at 31 March 2005 no amount
was owed to Reid & Co – thus the four companies' obligations to pay the
commissions to Mr Reid had been treated as having been discharged.

3. There had been a two-stage accounting process whereby first the commissions were treated by the Three Sister Companies as owed to GW223, and then secondly GW223 credited the accrued rights to Mr Reid's loan account. That second stage constituted "payment" – Mr Reid obtained a benefit from GW223 that he could not have received from the Three Sister Companies because he had no director's loan account with those companies.
4. The credit by GW223 to Mr Reid's loan account also constituted payment because it replaces the obligation to pay the commissions with a credit to the loan account. As a result Mr Reid could not sue GW223 for payment of the commissions, albeit he could sue for any non-payment of his loan account.
5. The final entry on Mr Reid's loan account ledger was the withdrawal of the entire balance on 31 March 2006 – thus Mr Reid received the benefit of the whole of the loan account (including the commissions) on the last day of the relevant six month period.

Consideration

36. I agree with HMRC that the relevant test of "payment" is that given by the Court of Appeal in *Faith Construction* (see para 32 above): "payment" is an action that "discharged the liability of the [debtor] under the ... contract and left the [creditor] with no right to sue for payment thereunder".

37. HMRC accept that the period preceding 1 October 2004 is out-of-time for assessment. The parties dispute whether the period 1 October 2004 to 31 March 2005 is or is not assessable. HMRC contend that the amount relating to the period 1 October 2004 to 31 March 2005 – the calculation of which is also in dispute but calculated by HMRC at £301,815 – is assessable because "payment" occurred within six months of 30 September 2005 (ie no later than 31 March 2006).

38. I have reached my decision on the matter of "payment" by considering in turn the following three questions:

- (1) Can the 2005 accounts of GW223 be construed as evidencing "payment" of the liabilities?
- (2) Did the intercompany accounting between GW223 and the Three Sister Companies constitute "payment" of the liabilities?
- (3) Were the liabilities otherwise "paid" no later than 31 March 2006?

35 *Can the 2005 accounts of GW223 be construed as evidencing "payment" of the liabilities?*

39. Having carefully considered the accounting information available, Mr Reid's explanations, and HMRC's questions and challenges, I have come to the following conclusions, which constitute my findings on the evidence.

- 5 1. The Reid & Co invoices were booked by the four companies as liabilities. The four companies then undertook intercompany accounting to show the Three Sister Companies as owing money to GW223 (rather than Reid & Co) and GW223 owing the aggregate amount of the invoices. That liability of GW223 was booked by GW223 to the ledger account “MMR DIRECTORS LOAN ACCOUNT”. That was done even though the invoices were issued by Reid & Co. It was done by a member of the accounts staff without any deep consideration of possible implications; it was merely administratively convenient. The accounts staff, and perhaps also the auditors, appear to have taken Mr Reid and Reid & Co to be interchangeable.
- 10 2. At 31 March 2005 the balance on the ledger account “MMR DIRECTORS LOAN ACCOUNT” was £4,093,978.18. That amount is included in the aggregate directors’ current accounts of £8,895,080 included as a current (ie falling due within one year) creditor in GW223’s statutory 2005 accounts, as shown in Note 9 to those accounts. Thus the commissions were still outstanding and owed as at 31 March 2005.
- 15 3. The company and its auditors then sow some confusion in drafting the related party disclosures note (Note 14) to GW223’s 2005 statutory accounts. Having treated the commissions as amounts due to Mr Reid personally (ie as a director), they now describe the company as trading with Reid & Co and disclose the amount of commissions charged in the year. I make no finding as to whether that was correct as a matter of company law and/or GAAP, just that it is how and why it was reported as it was. Note 14 then discloses the balance due to Reid & Co at 31 March 2005 as nil – from the company’s ledgers that is correct because the commissions have been credited to the account of Mr Reid not that of Reid & Co.
- 20 25 30

40. I understand why HMRC have taken their stance in relation to the effect of the statements in GW223’s 2005 accounts, in particular Note 14. However, I consider that Note 14 is misleading. The statements in Note 14 that (i) the company was charged commissions by Reid & Co of around £2.5 million, and (ii) “At 31st March 2005 no amounts are owed to or from Reid & Co Solicitors ...”, taken together imply that a balance has built up during the year and then been discharged. In fact Note 14 is correct that GW223’s ledgers show no year-end balance is owed to Reid & Co but that is because no debts have been recorded as due to Reid & Co, not because amounts due to Reid & Co have been discharged. Note 14 is misleading in that regard because the commissions were actually booked as amounts due to Mr Reid, not Reid & Co. In fact the commissions were still outstanding (and thus undischarged and thus not “paid”) at 31 March 2005.

35 40

41. My conclusion on this first question is therefore that the information in the 2005 accounts of GW223 does not support the contention that “payment” of the commissions was made at (or before) 31 March 2005.

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Did the intercompany accounting between GW223 and the Three Sister Companies constitute “payment” of the liabilities?

42. HMRC’s contention here is that the intercompany accounting between GW223 and the Three Sister Companies resulted in the original debts due to Reid & Co from the Three Sister Companies (and possibly also the original debt due from GW223) being replaced by a different item, being the single debt due from GW223 as shown in GW223’s 2005 accounts, and that was sufficient to constitute “payment”.

43. During the hearing both counsel referred to assignments of debts. With respect to counsel, as I expressed at the hearing, I do not think that is helpful terminology. A creditor can assign to a third party the benefit of a debt due to him. However, an indebted debtor cannot transfer his liability to a third party without the agreement of his creditor to that novation. Absent such agreement the original debtor remains indebted to his creditor. In the present case the commissions were invoiced by Reid & Co to GW223 and the Three Sister Companies; thus there were debts due from those four companies to their common creditor, Reid & Co. The intercompany accounting between GW223 and the Three Sister Companies was not an “assignment” of debts. Unless the creditor (Reid & Co) agreed to any other arrangement, the position after the intercompany accounting remained as before: each of the four companies was indebted to Reid & Co for the amount on its respective invoice from Reid & Co. Without such agreement by the creditor, the position stated in the ledgers and accounts of the four debtor companies after the intercompany accounting may have been a correct reflection of what the four companies had agreed amongst themselves, but it did not change the legal position that there remained four separate debts due from the four companies (each for the amount on its respective invoice from Reid & Co).

44. Was there any such agreement by the creditor? Mr Chapman for HMRC points out that the formal accounts of GW223 for the year ended 31 March 2005 were signed on behalf of the Board of Directors by Mr Reid as company secretary. However, I consider it is too broad a leap to say that Mr Reid (as company secretary) signing the directors’ report in the 2005 accounts of GW223 (which show the aggregate invoices as a liability of GW223) can constitute an agreement by him (as principal of Reid & Co) of the novation from the Three Sister Companies to GW223 of the debts due to Reid & Co. I accept the description given by Mr Reid in his witness statement (quoted at paragraph 6 above) that: “The bookkeeping was carried out in this way for administrative convenience.” During Mr Reid’s oral evidence I asked him, if one of the four companies had defaulted on the invoice it had received from Reid & Co then who would Reid & Co have sued for the money – the original debtor or GW223? His answer was that the firm would have sued both. That does indicate to me that Mr Reid, as principal of Reid & Co, had not accepted that the original debtors had been released from their liabilities to Reid & Co by virtue of the intercompany accounting.

45. I conclude that there was no novation of the debts due to Reid & Co and thus – regardless of the intercompany accounting – there was no discharge of the liabilities and, therefore, nothing to constitute “payment” of those sums within the test given by *Faith Construction*.

Were the liabilities otherwise “paid” no later than 31 March 2006?

46. Exhibited to Mr Reid’s witness statement (as Exhibit E) was a printout of the computer ledger for the “MMR DIRECTORS LOAN ACCOUNT” maintained by GW223. That shows for 31 March 2006 a balance of £4,365,729.27 which is then
5 reduced to Nil by a single item also dated 31 March 2006 “WR ADJ Y/E 31/03/06”. That is the auditors’ year end audit adjustment - obviously made some time after 31 March but intended to adjust the 31 March final balances - described in the email from the auditors cited at paragraph 12 above. HMRC contend that entry is sufficient to constitute “payment” of the commissions.

10 47. I have found it difficult to follow fully the numerical explanation given by the auditors in their email. The auditors did not give any formal evidence themselves. Mr Chapman for HMRC fairly described it as “some complicated accounting between the companies that is difficult to understand let alone explain.” However, it is clear that the main purpose of the audit adjustment was to “reassign” (as described in the
15 email) certain balances from the directors loan account to other ledger accounts; and in particular, there is an element of around £2.5 million labelled “Commission due [*sic* presumably “due”] from GW223 to related party”. In his oral evidence Mr Reid confirmed that he understood that was a reference to the Reid & Co commissions, and I reach the same conclusion. My interpretation is that when preparing the audited
20 accounts for the year ended 31 March 2006 there appears to have been some further reconsideration as to how commissions should be booked as between the various persons, and this entailed some reallocation of balances between creditors. In particular, the issue described in relation to the 2005 accounts (see paragraphs 39 & 40 above) as to how liabilities should be reflected in Directors’ current account and
25 the Related party disclosures note was reconsidered when the 2006 accounts were audited. However, those audit adjustments do not in my opinion alter the position that the commissions were still outstanding and payable by the four companies.

48. Although there were significant debits in the year ended 31 March 2006 to the Directors’ loan account maintained by GW223, Mr Reid’s evidence was clear that
30 none of those payments related to the commissions, and HMRC accept that point. For both the 2005 and 2006 accounts of GW223 I do not express a view as to whether the best nomenclature of the outstanding commissions was “directors’ loans” or “amounts due to related companies”, nor how they should be disclosed in the “related parties transactions” note. What I do conclude is that at 31 March 2006 the commissions
35 were still outstanding. They may have been shifted by the auditors from directors’ loan account to related party creditors but they remained outstanding. In particular, I see no evidence of any formal novation of the liabilities. Those liabilities had not been discharged and thus, using the test given by *Faith Construction*, there had been no “payment”.

40 **Conclusions**

49. From my conclusions at paragraphs 41, 45 & 48 above I further conclude that the commissions were not “paid” within the meaning of reg 94B prior to 31 March 2006. Accordingly I uphold Mr Reid’s contention that the entire amount of the Assessment is time barred by s 80(4) VATA 1994.

Decision

50. The preliminary issue stated in para 3 above is answered, that the entire amount of the Assessment is time barred.

Apportionment of the Assessment

5 51. Both parties made brief submissions on how the amount of the Assessment
apportioned to the period 1 October 2004 to 31 March 2005 should be calculated.
Given my decision that the entire Assessment is out-of-time that issue does not arise.
I have considered whether I should address the apportionment issue here, despite my
10 court. However, in view of the competing arguments concerning the appropriate
method of apportionment, on balance I feel that a decision on the apportionment issue
would be better made in the context of full evidence on the nature, calculation and
attribution of the commissions, which would be considered if the substantive dispute
(ie do the commissions attract VAT?) were to come before this Tribunal.
15 Accordingly, for that reason, I make no finding on the apportionment issue.

Appeal Rights

52. 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
20 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.

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**PETER KEMPSTER
TRIBUNAL JUDGE**

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RELEASE DATE: 18 April 2013

ANNEX

Wording of reg 94B VAT General Regulations 1995 (SI 1995/2518) as in force at the date relevant to these proceedings

5

94B—

(1) This regulation applies in relation to the following supplies where they are provided in the circumstances referred to in paragraph (2) below—

- 10 • (a) supplies falling within regulation 85 above (leases treated as supplies of goods) other than any supply which is exempt by virtue of Group 1 of Schedule 9 to the Act or would be exempt but for the operation of paragraph 2(1) of Schedule 10 to the Act;
- (b) supplies falling within regulation 86(1) to (4) above (supplies of water, gas or any form of power, heat, refrigeration or ventilation);
- 15 • (c) supplies falling within regulation 90 above (continuous supplies of services) other than any supply which is exempt by virtue of Group 1 of Schedule 9 to the Act or would be exempt but for the operation of paragraph 2(1) of Schedule 10 to the Act.

(2) The circumstances referred to in paragraph (1) above are—

- 20 • (a) that the person making the supply and the person to whom it is made are connected with each other, or
- (b) one of those persons is an undertaking in relation to which the other is a group undertaking (except where both undertakings are treated under sections 43A to 43C of the Act as members of the same group), and
- 25 • (c) the supply is subject to the rates of VAT prescribed in section 2 or section 29A of the Act.

(3) But this regulation does not apply where a person can show that a person to whom he has made a supply of a description falling within paragraph (1) above is entitled under sections 25 and 26 of the Act to credit for all of the VAT on that supply.

(4) For the purposes of paragraph (2) above, any question whether a person is connected with another shall be determined in accordance with section 839 of the Income and Corporation Taxes Act 1988 and “undertaking” and “group undertaking” have the same meaning as in section 259 of the Companies Act 1985.

(5) Where this regulation applies, goods or services shall, to the extent that they have not already been treated as supplied by virtue of the regulations specified in paragraph (1) above (or any provision of the Act or other regulations made under the Act), and to the extent that they have been provided, be treated as separately and successively supplied—

- 40 • (a) in the case of supplies the provision of which commenced on or before 1st October 2003, at the end of the period of twelve months after that date;

- (b) in the case of supplies the provision of which commenced after 1st October 2003, at the end of the period of twelve months after the supplies commenced; or
- 5 • (c) where the Commissioners are satisfied that each category of supply has been adequately identified, on such other period end date nominated for each category and falling within the period specified in sub-paragraph (5)(a) or (b) above as may be notified by the taxable person to the Commissioners in writing,

and thereafter at the end of each subsequent period of twelve months.

10 (6) But where the person making the supply, within the period of six months after the time applicable under paragraph (5) above either—

- (a) issues a VAT invoice in respect of it, or
- (b) receives a payment in respect of it,

15 the supply shall, to the extent that it has not been treated as taking place at some other time by virtue of the regulations specified in paragraph (1) above (or any provision of the Act or other regulations made under the Act), be treated as taking place at the time the invoice is issued or the payment is received, unless the person making the supply has notified the Commissioners in writing that he elects not to avail himself of this paragraph.

20 (7) The Commissioners may, at the request of a taxable person, allow paragraph (6) above to apply in relation to supplies made by him (or such supplies as may be specified) as if for the period of six months there were substituted such other period as may be prescribed by them.

25 (8) A taxable person may after the start of any period to be established under paragraph (5) above—

- (a) in relation to some or all of his supplies, and
- (b) where the Commissioners give their approval,

30 select an alternative period end date falling before the end of that period (which end date but for this paragraph would be established under paragraph (5) above), from which date subsequent periods of twelve months will end.

(9) A date selected and approved under paragraph (8) above shall be the date which establishes the end of the taxable person's current period.

35 (10) For the purposes of paragraph (8) above, a reference to a period end established under paragraph (5) above includes a reference to a period end established by an earlier application of paragraph (8) above.

(11) Where the supply is one of the leasing of assets, and that leasing depends on one or more other leases of those assets (the superior lease or leases), then the reference in paragraph (2) above to the person making the supply includes a reference to any lessor of a superior lease.

40 (12) For the purposes of paragraph (11) above, a reference to the leasing of assets includes a reference to any letting, hiring or rental of assets however described, and "lessor" shall be construed accordingly.

(13) For the purposes of this regulation, goods or services are provided at the time when and to the extent that, the recipient receives the benefit of them.

(14) Where this regulation applies, the regulations specified in paragraph (1) above shall not apply to the extent that supplies have been treated as having taken place under this regulation.

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