VAT group registration

Copthorn Holdings Ltd

Background

HMRC's refusal to discretionally admit two group companies into the VAT group on a retrospective basis - matter referred back to HMRC.

This is the second attempt by the taxpayer to have two companies included in its VAT group retrospectively. HMRC has a discretionary power to permit backdating but the policy is to limit retrospection to 30 days unless there are exceptional circumstances, which at the time of the first appeal only meant an administrative error by HMRC. The argument by the taxpayer was that the law simply says a grouping application shall……be taken to be granted with effect from such earlier……date as the Commissioners may allow. So the discretion given to HMRC is open; that is to say, there are no conditions attached to it. The taxpayer said that by only allowing retrospection beyond 30 days in cases where there are exceptional circumstances HMRC's policy had limited the discretion in a way that was unacceptable and contrary to Parliament's intention. As this is a case about HMRC's discretion the FTT has limited powers.

The issue here was that the taxpayer thought two companies were in the VAT group, and it proceeded as though they were. However, the applications to include them had not been made due to the error of the taxpayer - 4 different people had been in charge of finance and VAT accounting over an 18 month period, resulting in some confusion.

This error had resulted in HMRC assessing for c£2m VAT incurred by the group on land that was sold by a member of the VAT group to one of the two companies that are the subject of this appeal. That VAT became attributable to a supply that was, because the parties were not grouped, exempt instead of disregarded. When the taxpayer realised, after the land sale, that the buyer was not in the VAT group, it sought to notify HMRC of a belated option to tax. HMRC refused to accept a belated option to tax because VAT had not been declared on the sale. VAT was of course not declared because it was thought at the time that the seller and buyer were VAT grouped. Had the buyer been in the group with the seller the VAT incurred on the original purchase of the land would have been recoverable as a cost of zero-rate supplies of new houses. Had the option to tax been accepted late the VAT would have washed through and been recoverable. Having had the option refused, the only way to resolve the problem was to seek grouping retrospectively, but HMRC refused that too. The £2m error is the main focus of this appeal. The failure to group the second company was much less costly.

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When the taxpayer had its retrospective grouping application refused initially, it appealed and the first FTT referred the refusal back to HMRC for reconsideration on the grounds that the discretion was open with no conditions attached to it. HMRC changed its policy on retrospection slightly but upheld the original refusal, after a year, hence the second appeal.

This second FTT has concluded that the change to the policy was a "somewhat cynical endeavour to leave the policy substantially unchanged while purportedly answering the challenge to it by the earlier Tribunal decision".

Since the taxpayer had dealt with VAT accounting on the assumption that the companies were in the group, permitting retrospection would not require any of the returns submitted to change (one of the main reasons cited by HMRC for refusing retrospection beyond 30 days except in exceptional circumstances). It was incoherent for a house building group to suffer a £2m input VAT restriction. The FTT expressed doubt about HMRC's view that all taxpayer errors around grouping applications involving retrospection were similar and common and hence not exceptional, while HMRC errors were so rare as to be most exceptional. The bar taxpayers had to get over to secure retrospection beyond 30 days in cases where the error was not made by HMRC was pretty well insurmountable and was too high for a policy where HMRC had been given an open discretion.

The FTT has therefore referred the matter back to HMRC again, in the hope that HMRC will consider the comments the Judge has made about the exceptional circumstances and the scope of the discretion and that fairness and common sense will prevail, so that a house builder is not left with a £2m VAT cost, however technically correct.

Comment

Cases like this show the need for VAT to be at the forefront of the development process. Mistakes can be costly and very difficult or impossible to rectify later down the line.