

The devil's in the detail

A recent tribunal case shed some light on legitimate expectation, writes Les Howard.

Legitimate expectation takes many forms, from a statement on the HMRC website or a Google search, to 'legal advice' from a mate in the pub!

So, having been assured that VAT is not due on a particular transaction, how should you respond if a HMRC enquiry reaches a different conclusion?

The Upper Tier Tribunal gave some thought to this question in the case of KSM Henryk Zeman SP Z.o.o. (KSM). The substantive issue concerned the place of supply of the installation of a boiler and KSM's consequential obligation to register for VAT in the UK.

The Upper Tier decision summarises the facts of KSM's engagement with HMRC (paras 6 and 11). Certainly, the correspondence between the parties had been confusing. At one stage, HMRC had rejected KSM's application for registration. The Upper Tier agreed with the First Tier that the correspondence, viewed as a whole, contained an element of ambiguity, so KSM could not rely upon it. Further, when KSM's advisers indicated that HMRC's refusal to register was incorrect, it was unreasonable not to challenge it. Thus, the defence of legitimate expectation was not available.

Which brings us to the wider question of whether the FTT had any jurisdiction to consider the matter of legitimate expectation at all. This is a question that has been addressed before.

Like me, you may have thought that the FTT could no longer even consider the argument of legitimate expectation. Instead, the taxpayer is forced to pursue the more expensive option of a Judicial Review. HMRC certainly took that position in KSM. Counsel for HMRC "...argued that there is a distinction between a decision to assess and how the decision is then made. The latter falls within the FTT's appellate jurisdiction but not the former" (para 68). However the Upper Tier took some time to review the case law and came to an interesting and, I think, helpful conclusion.

The key is to understand the legislative process by which HMRC make a decision and issue an assessment. And, then to consider the corresponding grounds of appeal allowed by s83 of VAT Act 1994. There is a great deal of variation here, so different circumstances will produce different outcomes.

In the KSM case, the appeal was made under s83(1)(p) which grants a right of appeal with respect to an assessment under s73(1). In turn, s73(1) states that, where certain conditions are fulfilled, 'the Commissioners... may assess.' In other words, s73(1) is permissive, not mandatory (para 52). HMRC are not obliged to assess. They choose to do so. The Upper Tier considered that the Court of Appeal supported this approach in the cases of Rahman (No2) [2003] STC 150 and Pegasus Birds Ltd [2004] STC 1509. Both cases involved HMRC taking note of various factors in reaching its decision. In doing so, HMRC must exercise its judgment to weigh factors, perhaps including contradictory and inconsistent information. That is part of the 'best judgment' process, with which readers will be familiar.

The wording 'the Commissioners... may assess' requires an element of discretion and permission. Thus, the Upper Tier concluded, if the question of legitimate expectation is in play, HMRC must consider the content of their engagement with the taxpayer in the making of any decision and/or assessment. Consequently, s83(1)(p) brings that process within the remit of the First Tier Tribunal.

Does this decision open the door wide to huge numbers of appeals? Certainly not! The Upper Tier decision is clear that any appeal depends on the wording of the relevant part of s83. In turn, that may also be restricted by the section referred to by that part of s83.

In conclusion, the taxpayer has a number of options having received a decision from HMRC. The preferred option will depend on the specific details in each case. Having exhausted the initial routes of internal review and alternative dispute resolution, I suggest three options:

- Appeal to the FTT, as per the principles explained in KSM;
- A Judicial Review; and
- Complaint to HMRC and then the Adjudicator's Office.

This is where the adviser earns his corn. A careful analysis of the facts, the correspondence, statute and case law will provide a conclusion as to the best option to pursue.

The KSM decision is here: <https://tinyurl.com/2p8hfpz2>

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