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Indirect tax update

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Summary

Welcome to this week's Indirect Tax Update.

This week, the Supreme Court has issued a judgment in the case of London Clubs Management Ltd. The legal issue in this case concerned the correct interpretation of the gaming duty provisions of the Finance Act 1997.

Gaming duty is payable on dutiable gaming by reference to the 'gross gaming yield' (GGY). The case rested, essentially, on how the GGY is calculated. London Clubs Management Ltd runs casinos and, as an incentive or promotion, it provides certain gamblers with free gaming chips. The chips can be used to place bets and the gambler can win real money if he places a successful bet. HMRC considered that there should be a value attributed to the free chips which should be included in the calculation of the GGY.

The Supreme Court has now issued its judgment.

The Upper Tribunal has also issued its judgment in the case of Safestore Ltd. This case concerns the supply of insurance and whether the company supplied intermediary services to the Guernsey based insurer or supplied insurance itself to its customers. Under current rules there is a significant difference from a VAT perspective. As an intermediary, Safestore is entitled to reclaim input VAT whereas, as a supplier of insurance, no input VAT could be reclaimed. The First-tier Tax Tribunal ruled against Safestore and it appealed to the Upper Tribunal.

Finally this week, the Government has published a statutory instrument – the VAT (Miscellaneous Amendments to Acts of Parliament) (EU Exit) Regulations 2020 - the legislation removes a qualifying pension fund that is established in the EU from the VAT exemption contained in the UK VAT Act. From a date to be appointed (which is likely to be 31 December 2020) the supply of fund management services provided by a UK fund manager to a pension fund established in the EU will no longer be exempt from VAT.

UK Supreme Court – HMRC v London Clubs Management Ltd

Whether free gaming chips should be included in the calculation of gross gaming yield

It's not often that cases on tax and excise duty go all the way to the UK's Supreme Court. The fact that the case gets there at all means that the issue is of significant importance and deserves our attention. This case concerns the correct calculation of 'gross gaming yield' for the purposes of determining how much gaming duty is due from the operator of a casino. The case began in 2014 at the First-tier Tax Tribunal. London Clubs Management Ltd lost its appeal and appealed to the Upper Tribunal which allowed its appeal and HMRC then appealed to the Court of Appeal. In 2018, the Court of Appeal dismissed HMRC's appeal and HMRC appealed to the Supreme Court.

The issue to be resolved is relatively straightforward. London Clubs Management Ltd operates casinos. To attract gamblers to participate, it provides free gaming chips to certain gamblers. These chips are known as 'non-negotiables' (or 'Non-Negs'). The chips can be used by the gambler to place a bet and if the bet is successful, he will be paid with real money. If the bet is a losing bet, the Non-Negs are removed from the gaming table. Gaming duty was introduced in 1997 and is payable in relation to dutiable gaming (which the taxpayer accepted was the case). The amount of duty payable is calculated by reference to the gross gaming yield (GGY) which, in simple terms, is the difference between the value of bets placed less the value of winnings paid out. From 2008, the company included the 'face value' of the Non-Negs in its calculation of the GGY but, following a review, it considered that that method of accounting was incorrect. It submitted a claim to HMRC in 2012 seeking repayment of overpaid duty in the sum of £1.9 million. HMRC refused the claim.

The FTT agreed with HMRC that the correct way to calculate GGY was to include the face value of the Non-Negs in the 'banker's profits'. It accepted the argument advanced on behalf of HMRC that the value in money or money's worth of the Non-Negs was their monetary face value on the basis that the face value would be used to calculate any winnings in cash chips. On appeal, the Upper Tribunal overturned the FTT's decision. It held that the FTT had failed to have proper regard to the requirement that the value of the stakes staked (when calculating the Banker's profit) must be the value of those stakes in money or money's worth. In the UT's view, Non-Negs did not represent any money paid or deposited by the customer, nor did they have any value in money's worth by reason of being redeemable for cash or for goods or services.

The Court of Appeal dismissed HMRC's further appeal. It held that a Non-Neg was not a "stake staked" for the purposes of section 11(10)(a) of the FA 1997; and even if a Non-Neg was a stake staked, that stake had no value in "money or money's worth".

The Supreme Court has now issued its judgment. In essence, the Court has unanimously dismissed HMRC's appeal (although the judges did so for differing reasons). The expression "money or money's worth" in section 11(10)(a) emphasises that in determining the value of the stakes staked it is the actual and real world value of the stakes in the hands of the banker which matters. Section 11(10)(a) is concerned with stakes which are or represent money (as cash chips do) or which can be converted into money. Similarly, in working out the value of the prizes provided by the banker, it is the actual or real world cost to the banker of providing the prizes that must be brought into account. Non-Negs are very different from cash chips which represent money deposited by the gambler, or money which he has won or been given to encourage him to bet. Non-Negs do not represent money to which the gambler is entitled and, unlike cash chips, they cannot be encashed or exchanged for goods or services. When the casino allows a gambler to bet with a Non-Neg, it is, in a sense, allowing the gambler to bet with the casino's own money. Put another way, from the point of view of the casino, a Non-Neg amounts to a free bet and should not be regarded as stakes staked within the meaning of section 11(10)(a) of the FA 1997, nor should it be considered to have any value in money or money's worth within the meaning of that provision. HMRC's appeal was dismissed.

Comment – this was a significant gamble by the taxpayer and the stakes were high. Six years of litigation has ending with the taxpayer securing a jackpot win. Other casino operators will, no doubt, have been following this case with interest and should now also be entitled to gaming duty refunds where the value of Non-Negs have been similarly included in the calculation of gross gaming yield.

Upper Tribunal – Safestore Ltd

Whether taxpayer providing insurance intermediary services or supplies of insurance.

The taxpayer in this case (Safestore) is a well know supplier of storage facilities to both business and private customers. Its main income is derived from the fees it charges to customers for the use of lock-up storage units. This income is liable to VAT at the standard rate. The company also requires customers to take out insurance covering the risk of loss or damage to the goods stored. Safestore established a captive insurance business (Assay) which was based in Guernsey (Channel Islands). The company entered into a policy with Assay and under the terms of an unwritten agreement, it retained 30% of the premium it received from customers and forwarded 70% of that premium to Assay. The question to be answered in this case was whether, in the circumstances, Safestore acted as an insurance intermediary (ie introducing customers seeking insurance cover to a provider of insurance) or whether it simply acted as the supplier of insurance to the customer.

The First-tier Tax Tribunal (FTT) had decided that, on the facts and evidence, Safestore acted as the supplier of the insurance to its customers and dismissed its appeal. In simple terms, the Tribunal concluded that Assay provided a block policy to Safestore and Safestore supplied the insurance to its customers. The Upper Tribunal agreed with the FTT's conclusion that the parties' intention was that the Customer Goods Policy should be a contract of insurance between Safestore and Assay and, as a result, Safestore could not be regarded as providing intermediary services to Assay. As such, when it supplied insurance under the block policy to its customers, it acted as an insurance principal and not as an agent of Assay.

This finding (as with the FTT's) meant that Safestore's supplies were exempt from VAT as supplies of insurance but there was no right of input VAT recovery which would have been the case had it acted as an insurance intermediary.

Comment

The VAT rules in the world of financial services (including insurance and related services) are particularly complex.

Under general rules, when a business makes exempt supplies, there is no right of recovery in relation to any input tax incurred which is attributable to those supplies. However, for financial services, where certain services are supplied to a customer established outside the EU, a right of recovery does exist.

In this case, Safestore argued that it supplied insurance intermediary services to an insurer established outside the EU – that would have given it the right to deduct input tax in relation to its supplies of insurance. However both the FTT and now the Upper Tribunal have found that, in fact, it supplies insurance to its UK customers. This is exempt from VAT with no right of recovery.

Preparing for Brexit - Change of legislation

Supplies of fund management services to Pension Funds

This week, the Government introduced new legislation by way of a Statutory Instrument which will come into force in the UK on a day yet to be appointed. (The instrument relates to VAT rules in the UK after the end of the transition so is likely to come into force with effect from 11pm on 31 December 2020).

The statutory instrument covers a number of issues where changes to UK law are required after Brexit. In particular, the VAT exemption for fund management services provided to qualifying pension funds is to change.

From the appointed day, fund management services supplied to qualifying pension funds established in the European Union will cease to be exempt from VAT. A qualifying pension fund is a fund that meets a number of conditions including that it is solely funded, whether directly or indirectly, by pension members; the pension members bear the investment risk; the fund contains the pooled contributions of more than one pension member; the risk borne by the pension members is spread over a range of investments; and the fund is established in the United Kingdom or in a member State. It is in relation to this final condition that the law will change. From the appointed day, only the management of a qualifying pension fund established in the UK will be exempt from VAT.

The supply of fund management services supplied to pension funds established outside the UK after the appointed day will be outside the scope of UK VAT. This does mean that, as now, no UK VAT will be chargeable. Any VAT due may be subject to the reverse charge procedure in the country where the pension fund is established.

The supply of fund management services to non-qualifying pension schemes established in the UK will continue to be liable to UK VAT at the standard rate.

Comment

In reality, nothing really changes by this change in UK VAT law. Under the current rules, the supply of fund management services to a qualifying pension fund is exempt from VAT provided that the fund is established either in the UK or in a Member State of the EU.

From the appointed day, the exemption is to be removed for fund management services supplied to funds established within the EU. However from that date these supplies will be regarded as B2B supplies and the place of supply will be the place where the pension fund in question is established. In other words, the supply of fund management services will be regarded as outside the scope of UK VAT. In either scenario, no UK VAT will be chargeable by the fund manager to the pension fund.

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