

The Royal Bank of Scotland Group plc v the Commissioners for Her Majesty's Revenue & Customs (2006) 19429

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Input tax – proportion deductible where no specific attribution possible – standard and special methods – rounding up – whether applicable to special method – “next unit” – EC 6th Directive Articles 17 and 19 VAT Regulation 1995 paras 101 and 102

Regulation 101 of the Value Added tax regulations 1995, prescribes a “standard method” for the attribution of input tax to taxable supplies. It provides a method for arriving at a percentage of all input tax which may be attributed to taxable supplies. In terms of regulation 101(4) it is provided that if that percentage is not a whole number it shall be rounded up to the next whole number.¹ Regulations 102 and 103 allow the Commissioners to approve or direct the use of a method other than that specified in regulation 101, a “special method”. No stipulation is made as to rounding up of percentages arrived at by use of a special method.

Regulations 101 to 103 are intended to give effect in the UK to Articles 17 and 19 of the Sixth Directive.

In 2002 a framework agreement, referred to as a “template” was agreed between the Appellant, (“RBS”), and other Scottish banks on the one hand and the Respondents, (“HMRC”), on the other. That provided for the use of a special method of calculating residual input tax for various sectors of the banks’ businesses. It also provided, specifically, for rounding up of the percentage to 2 decimal places.

RBS argued that, notwithstanding the terms of the Framework Agreement, the rounding in respect of each sector should conform to the nearest whole number. RBS argued that, properly construed, Article 19(1) required rounding up to the next nearest

¹ [It requires to be noted that on 16 March 2005 Regulation 101(4) was amended by the addition of a new regulation 101(5).]

whole number of percentages arrived at both by the standard method and by other methods. In so arguing it relied on the direct effect of Article 19 and argued that regulations 101 to 103 failed properly to implement the Sixth Directive.

Article 17(5) provides

As regards goods and services to be used by a taxable person both for transactions covered by paragraphs 2 and 3, in respect of which value added tax is deductible, and for transactions in respect of which value added tax is not deductible, only such proportion of the value added tax shall be deductible as is attributable to the former transactions.

This proportion shall be determined, in accordance with Article 19, for all the transactions carried out by the taxable person.

However, Member States may:

- (a) authorise the taxable person to determine a proportion for each sector of his business, provided that separate accounts are kept for each sector;*
- (b) compel the taxable person to determine a proportion for each sector of his business and to keep separate accounts for each sector;*
- (c) authorise or compel the taxable person to make the deduction on the basis of the use of all or part of the goods and services;*
- (d) authorise or compel the taxable person to make the deduction in accordance with the rule laid down in the first subparagraph, in respect of all goods and services used for all transactions referred to therein;*
- (e) provide that where the value added tax which is not deductible by the taxable person is insignificant it shall be treated as nil.*

Article 19 provides – Calculation of the deductible proportion

- (1) The proportion deductible under the first subparagraph of Article 17(5) shall be made up of a fraction having:*
 - as numerator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions in respect of which value added tax is deductible under Article 17(2) and (3),*
 - as denominator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions included in the numerator and to transactions in respect of which value added tax is not deductible. The Member States may also include in the denominator the amount of subsidies, other than those specified in Article 11(A)(1)(a).*

The proportion shall be determined on an annual basis, fixed as a percentage and rounded up to a figure not exceeding the next unit.

In agreeing the template, HMRC had used its powers under subparagraph 3 of Article 17. RBS, however, argued that the proportion deductible under the template was, nevertheless, "The proportion deductible under the first subparagraph of Article 17(5)" on the ground that all derogations permitted by Article 17(5) fell within the principle set out in the first subparagraph, namely that only such proportion of the VAT shall be deductible as is attributable to transactions in respect of which VAT is deductible.

The Tribunal held that the UK VAT Regulations 1995 properly and fully implement the provisions of Articles 17-20 of the Sixth Directive; the first sub-paragraph of Article 17(5) provides for a standard method of calculating the appropriate percentage deduction whereas the third sub-paragraph allows member states to derogate from the standard method in the manner specified in paragraphs (a) to (e) of that third paragraph.

Comment

This case provides an interesting example of a taxpayer arguing that the UK legislation fails to comply with the Sixth Directive seeking to rely on its direct effect. The particular issue of whether HMRC are empowered to agree rounding up to less than the next whole number of the percentage to be applied in a special method remains live notwithstanding the introduction of regulation 101(5). The Tribunal's decision has been appealed to the Court of Session which may be invited to make a reference to the ECJ.

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