

Court of Session Clarifies Taxpayers' Remedies

In *NHS Lothian Health Board v. HMRC* [2020] CSIH 14, the Inner House of the Court of Session (Scotland's highest civil court) held that the First-tier Tribunal and Upper Tribunal had wrongly rejected the Health Board's claim to recover historic input tax. In its unanimous judgment, the Court provides important clarification of the law of evidence as it applies to VAT recovery and overpayment claims. The problem in many such cases is that it is plain that there had been an overpayment or under-recovery, but its precise quantification is uncertain. The Court also explains the role of both HMRC and the First-tier Tribunal in determining the sums which HMRC is required to pay back. This is based on the general principles of EU law, notably the principles of effectiveness, proportionality and legal certainty. These principles are linked. As Lord Drummond Young observed, '*the application of the effectiveness test generally involves a form of proportionality exercise*'.

The Court allowed Lothian's appeal from decisions of the First-tier Tribunal and the Upper Tribunal. They had both concluded that the burden of proving overpayment claims was solely on the taxpayer and even the best evidence available to calculate the amount of an historic overpayment was insufficient to satisfy the normal standard of proof in civil cases.

The Court concluded that the lower tribunals had not given the principle of effectiveness the weight which EU law required in historical overpayment claims. In its judgment, the Court considers the CJEU's landmark decision in Case 199/82, *San Giorgio*, which establishes the right to restitution of taxes and levies paid in breach of EU law.

As recent events have highlighted, since its foundation in 1948 the statutory function of the NHS has been to provide medical care from the cradle to the grave free at point of delivery.

Some 96% of the NHS's activities come within its role as a public authority, and are outside the VAT system. In the case of these 'non-business' activities, a special public sector VAT refund scheme operates, known as Contract-Out Services (COS) VAT. This has operated since 1983.

However, NHS bodies also carry on 'business' activities, such as catering, car parking and – in this particular case- the provision of laboratory services, which come fully within the VAT system. Following the *Fleming* case, NHS bodies lodged some 700 claims to recover input tax incurred but not recovered in the *Fleming* period. 200 are still outstanding. HMRC had resisted these claims on a wide variety of grounds, in particular, insufficient or inadequate

evidence to substantiate the claim. Many claims had foundered on this ground, including claims by the Lothian NHS Board.

As Lord Drummond Young observes in his wide-ranging Opinion:

'As in many such cases, the primary issue is not the existence of the taxpayer's claim to recover overpaid value added tax but the quantification of that claim, and in particular whether the claim can be quantified with sufficient accuracy to permit an order for repayment of tax to be made.'

The Heath Board argued that, if the evidence was the best available, and a reasonable methodology was adopted, it was wrong to reject such a claim in toto. The Court of Session held that these arguments were *well-founded*.

The Court of Session explains how both HMRC and the tribunals should approach these cases in order to achieve the determination of overpayment amounts, given the fundamental EU law right to recover overpayments of tax paid in breach of EU law. As part of their statutory function, the Tribunals had duties to use their best endeavours to determine amounts of overpayments when it was accepted that there had been an overpayment. It was not sufficient compliance with EU law simply to apply the burden and standard of proof to dismiss claims without consideration of the overriding duties on the state to comply with the effectiveness principle.

In their successful Court of Session appeal. David Southern QC had represented Lothian Health Board, and numerous other NHS bodies in earlier cases, leading up to the Court of Session judgment.

By David Southern QC

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