

## VAT & IVAs

### **Guide to the practical implications of the Paymex decision**

The recent decision in *Paymex Limited v. The Commissioners for Her Majesty's Revenue and Customs* found that Nominees' and Supervisors' fees in consumer IVAs were exempt supplies. This document sets out the views of the bodies listed at the foot of this document.

IPs should note that legal advice is being sought by The Institute of Chartered Accountants of Scotland regarding the applicability of the Paymex decision to Trust Deeds.

This guide does not constitute legal advice nor does it seek to instruct or direct IPs in the administration of their IVAs. The bodies issuing this guide do not accept any liability in respect of actions that IPs may take in accordance with it, as it must be for each IP to be satisfied that his/her conduct meets the legal and professional requirements placed upon office-holders. However, notwithstanding the above, IPs should have regard to the regulatory as well as legal consequences of their actions. The guide should be read in conjunction with, the following:

- i. Paymex Ltd v HMRC decision [*reference 2011 UKFTT 350*]
- ii. Joint statement issued by the RPBs and R3 dated 22 July 2011
- iii. *Dear IP* letter no.50 issued by the Insolvency Service
- iv. Briefing issued by HMRC [*reference 'Revenue & Customs Brief 27/11'*  
[www.hmrc.gov.uk/briefs/vat/brief2711.htm](http://www.hmrc.gov.uk/briefs/vat/brief2711.htm)]
- v. HMRC VAT notice How to correct VAT errors and make adjustments or claims [Notice 700/45]
- vi. Clarification notice issued by HMRC (attached)
- vii. Insolvency code of ethics
- viii. SIPs 1, 3, 9, & 11
- ix. Clients' money regulations/guidance
- x. The Definitions set out as an Annexe to this document

#### 1) CHARGING VAT

IPs who have not already done so should ensure that their firms stop charging VAT on invoices for fees and disbursements in IVAs with immediate effect as these are exempt supplies. IPs should also consider the current VAT quarter and whether any adjustments are required to reflect the exempt status of these supplies.

#### 2) CLAIMING REFUNDS ON OPEN CASES

The effect of the Paymex ruling is that VAT on previous invoices for fees has been charged erroneously, albeit in good faith at the time. Accordingly, we believe IPs should take all appropriate measures to remedy the position for the benefit of creditors.

Regardless of the absence of any obligation to do so under VAT legislation, the office-holder's duty to maximise realisations requires a supervisor to seek recovery of sums that are due to the estate. Office-holders should also be mindful of creditors' expectations and the exposure to action by creditors if claims are not made. We are seeking counsel's opinion as to whether or not Supervisors are obliged to seek refunds where the recovery would be negligible.

### 3) CLOSED CASES

The duty referred to above may or may not encompass completed (closed) cases, as the IP's ongoing jurisdiction/locus is questionable. We are seeking counsel's opinion on closed cases and will make a further statement as soon as reasonably practicable. IPs considering claiming refunds in such cases may wish to await that legal opinion or take their own advice before distributing any sums received. [See also Footnote\*]

### 4) CASES ABOUT TO BE CLOSED

Having regard to the above, IPs may form the view that IVAs reaching their conclusion, whether by reason of completion or termination due to failure, are cases in respect of which refund claims may be made only for as long as those cases remain open. Office holders may therefore wish to consider whether the terms of such cases permit the continuation of them pending resolution of the VAT issue, subject also to taking into account the position of the debtor.

### 5) CLAIMS PROCESS

The claims process is set out in HMRC's Notice 700/45. The time limit for making claims is four years but not longer. Creditor agents understand this and have indicated that they will not be pressing for more.

IPs should note that time continues to run until a claim is made.

### 6) GROSS v NET

HMRC will pay a net sum comprising:

- output tax wrongly charged and identifiable to individual cases;
- input tax wrongly reclaimed and identifiable to individual cases;
- input tax wrongly reclaimed because of partial exemption rules (this tax is not identifiable to individual cases).

Only the net amounts will be refunded. Creditor agents have indicated that they will accept the net amounts as the reasonable and appropriate realisation or windfall, and that they will not be pressing for any form of top-up in respect of the input tax adjustment. As some creditors may take a different view, IPs should refer to the comment in the Summary below.

## 7) RECEIPT OF REFUNDS

In order to avoid unjust enrichment, HMRC will require confirmation from the firm that sums paid will be passed without deduction to the estates from which VAT was paid in the first place. The refunded amount(s) should be paid into designated estate accounts (or a general clients' account in respect of any closed cases) and should be transferred by the firm into those accounts as soon as they are cleared (not more than 7 days later).

These are in effect third party funds and should be segregated from those of the firm.

Where IPs are claiming refunds in respect of closed cases, they should be prepared to distribute these without delay.

## 8) ALLOCATION

Where refunds include deductions for input tax wrongly claimed either in respect of case specific disbursements or as a consequence of the partial exemption rules applying, IPs will be required to calculate the appropriate amount to be credited to each estate. The simplest and most equitable method of calculation may be one that has the effect of apportioning the input tax arising from the application of the partial exemption rules across the cases rateably, i.e. if input tax represents 40% of the output tax claimed on average and consequently only 60% of output tax claimed is refunded, then each estate should receive 60% of the output tax suffered, the balance being regarded as irrecoverable VAT.

Case specific input tax should of course be applied to that case.

## 9) FEES

HMRC has confirmed that once refunds have been paid into the estates, the normal IVA procedures apply and office holders may be remunerated out of estate monies in accordance with the terms of the IVAs in the usual way. It is arguable that VAT refunds are not, technically, realisations in the estates; however, creditor agents are prepared to permit office holders to consider them as such for the purposes of invoking existing fee approvals, and the regulators identified below ('RPB') will not regard fees drawn on this basis as improperly authorised.

In some IVAs, the nominee's fee will have been approved on a VAT-inclusive basis. Where that is the position, subject to satisfying other terms of the IVA as modified, office holders may with good reason consider that they are entitled to the element of the refund attributable to VAT on the nominee's fee. However, it may be seen as equitable by the creditors if the IP were to take into account any input tax adjustment necessary as per the example above, e.g. if only 60% of the VAT is recovered, then 60% would be the appropriate percentage of the VAT on the nominee's fee to be paid to the office holder.

## 10) VARIATIONS

Having regard to the above, ordinarily office holders should not need to instigate variations to the terms of the IVAs. Creditor agents will not be minded to approve fees at a rate higher than those already covered by the existing terms, and regulators will look very closely at the justification for variations.

## 11) QUERIES

IPs seeking further clarification on any of the points covered in this guide may contact HMRC or one of the following bodies for assistance. This guide is issued by:

Association of Business Recovery Professionals, *R3*  
Chartered Accountants Regulatory Body, *CAI* (RPB)  
Debt Resolution Forum  
Insolvency Practitioners Association (RPB)  
Institute of Chartered Accountants in England & Wales (RPB)  
The Association of Chartered Certified Accountants (RPB)  
The Institute of Chartered Accountants of Scotland (RPB)

## 12) SUMMARY

We believe the above sets out a practical way of dealing with the effects of the Paymex decision. It places an obligation on IPs to claim refunds in open IVA cases, but it seeks to deal with the process on a basis that is fair to all concerned.

Creditor agents for their part have adopted a reasonable stance in indicating their preparedness to accept net refunds and allow those monies to be subject to usual remuneration arrangements (though where firms seek to charge fees or disbursements which they consider excessive, they may reserve the right to adopt a different approach). We are liaising with creditor agents with a view to seeking statements confirming their positions. IPs will need to be mindful of the potential for challenge by dissenting creditors, and may wish to adopt a different approach in cases where creditors not represented by the main agents are involved to a significant extent.

HMRC has offered some flexibility in relation to its principle of unjust enrichment by allowing fee arrangements to be entered into, but its insistence that refunds are paid to estates without deduction remains, and is full square with the position outlined by the regulators and R3 in their initial statement.

In accordance with normal practice, IPs should document their decisions and retain details of calculations made, and make relevant clients' account and other records available to their regulators for inspection as part of the routine monitoring visits periodically undertaken by regulators.

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## ANNEXE DEFINITIONS

IP	Insolvency Practitioner authorised by an RPB or the IS
RPB	Recognised Professional Body under IA86
IS	The Insolvency Service, an executive agency of the Secretary of State for Business, Innovation & Skills acting as Competent Authority under IA86
IA86	Insolvency Act 1986, as amended
Office holder	IP acting as Nominee/Supervisor as defined in IA86 in relation to an IVA.
IVA	Individual Voluntary Arrangement as defined in IA86
HMRC	Her Majesty's Revenue & Customs
VAT	Value Added Tax
SIP	Statement of Insolvency Practice
Regulators	RPBs and the IS
Firm	VAT-registered entity, partnership or company, in association with which the IP carries out his/her office holder duties
Office a/c	Bank account in the name of the firm
Clients' a/c	Bank account satisfying the definition in the RPBs' Clients' Money Regulations
Estate	Trust managed by the office holder on behalf of creditors and/or other beneficiaries
Estate fund	Monies held in the estate
Estate a/c	Bank account operated on trust principles for an estate
TiB	Trustee in Bankruptcy – an IP acting as such in relation to a bankruptcy
trustee	IP acting as trustee of a continuing express or implied trust subsequent to completion of an IVA
Creditor	Person, corporate or otherwise, owed money by the debtor, where that person's claim is admitted by the office holder for dividend purposes
Creditor agent	Third party acting on behalf of and with the authority to exercise voting rights for one or more creditors, or a debt purchaser with such rights
Debtor	Individual subject to an IVA
Bankrupt	Debtor subject to bankruptcy proceedings subsequent to failure of an IVA
OR	Official Receiver (part of the IS) acting as TiB in the absence of an IP appointed for that purpose
Fees	Office holder remuneration (and charges for disbursements) as approved by creditors in accordance with the terms of an IVA as modified or varied
Nominee	IP's role in the period immediately prior to approval of an IVA, in respect of which an agreed fee may have been approved /modified by creditors
Supervisor	IP's role subsequent to approval of an IVA, in respect of which a fee may have been approved by creditors

### \* FOOTNOTE

The advice on closed cases will cover points about refunds flowing to debtors or to an OR/TiB where the debtor has become bankrupt, and where a debtor is due monies from a case after creditors have been paid in full, and will address concerns regarding fees, as any fee approval given by creditors in the IVA may be regarded as having expired.