

TRUST DEEDS

Guide to the practical implications of the Paymex decision

The decision in *Paymex Limited v. The Commissioners for Her Majesty's Revenue and Customs* [2011]UKFTT 350(TC) found that Nominees' and Supervisors' fees in a consumer IVA were exempt supplies. Reference should be made to the joint statement issued by The Responsible Professional Bodies (RPBs) on 31 August 2011 and to further guidance on IVAs and CVAs issued by the RPBs.

ICAS has obtained an Opinion which confirms that the decision **does apply to Trust Deeds**. The Opinion states that "the supply of services by a trustee under a trust deed for creditors is an exempt supply for the purposes of VAT on the basis that it constitutes a single supply of services of which the predominant element is payment handling".

This guide does not constitute legal advice but is offered as a reference point in considering issues that arise from the ruling. The Bodies issuing this guide do not accept any liability in respect of actions that Insolvency Practitioners (IPs) may take in accordance with the guide. Each IP must be satisfied that his/her conduct meets the legal and professional requirements placed upon office-holders. IPs should also have regard to the regulatory and legal consequences of their actions.

The guide should be read in conjunction with:

- i. Paymex Ltd v HMRC decision [*reference 2011 UKFTT 350*]
- ii. Dear IP letter number 50 issued by the Insolvency Service
- iii. Briefing issued by HMRC [*Brief 27/11*]
- iv. HMRC VAT notice How to correct VAT errors and make adjustments or claims [*Notice 700/45*]
- v. Clarification notices issued by HMRC [*Brief 35/11*]
- vi. Revenue & Customs Notice on Finance issued in November 2011 [*Notice 701/49*]
- vii. Insolvency Code of Ethics
- viii. SIPs 1, 3, 9, & 11
- ix. Clients' Money Regulations/guidance

GENERAL

1. Office holders should carefully review the terms of individual Trust Deed documents to ascertain what impact the terms of the Trust Deed may have on the way in which they are required to act as trustee. It is recommended that if in doubt the trustee should seek approval from creditors prior to taking any particular action.

CHARGING VAT

2. With immediate effect VAT should not be charged for fees and disbursements in Trust Deeds as they are exempt supplies. IPs should review the current quarter's VAT return to decide whether any adjustments are required to reflect the exempt status of these supplies.

CLAIMING REFUNDS IN OPEN CASES

3. The effect of the Paymex ruling is that VAT on invoices for fees already rendered has, in good faith and on the instructions of HMRC, been charged erroneously. Where the fees and disbursements have been paid out of the trust deed estate the

VAT element suffered is considered to be an asset of the estate. Trustees have a duty to realise the debtor's assets and therefore it is incumbent on the trustee to submit a refund claim regardless of the absence of any obligation to do so under VAT legislation.

4. In terms of VAT rules such refund claims must be submitted within four years, see HMRC Vat notice 700/45.
5. The office holder should consider each Trust Deed on a case by case basis. Where a debtor (partnership or individual) is or was VAT registered it will not usually be necessary to make a VAT reclaim as the VAT will have been recovered as input tax. Where, however, the debtor is either unregistered or partially exempt consideration should be given to seeking a recovery of the VAT wrongly paid.
6. There may be cases in which the amount of the potential VAT refund would be outweighed by the allowable costs involved in submitting a refund claim. Office holders must give such cases careful consideration and refer to the Trust Deed document to verify whether or not it's terms provide for the trustee abandoning an asset. Even if it does so provide the trustee should obtain the approval of creditors prior to such abandonment failing which the trustee could be in breach of his/her duties. A distinction is drawn here between the powers contained in the Trust Deed document and the obligations of a trustee. Without the consent of creditors (that the trustee should not pursue a refund claim) a failure by the trustee to pursue a claim could lead to liability on the part of the trustee for any resulting loss to creditors, thus practitioners are advised to seek authority from creditors to abandon the claim.
7. Office holders should review their cases to establish whether or not their fees had been paid out of the trust estate, for example were they paid by a third party. In such cases there would be no asset to pursue and, in view of the pronouncements made by HMRC, it is suggested that there may be difficulty in obtaining any refund as it would not fall to be paid into the estate. Office holders would need to liaise with HMRC direct.

CASES ABOUT TO BE CLOSED

8. As in open cases there may be cases about to close in which the amount of the potential VAT refund would be outweighed by the costs involved in submitting a refund claim. In those cases office holders should refer to the comments made in paragraph 6 above.
9. Office holders should consider whether the terms of the Trust Deed permit the continuation of the case pending resolution of the VAT issue, subject to consideration of whether the debtor should nevertheless receive a discharge. The Trust continues until the Trustee receives his discharge however extending the period may have a detrimental effect on the debtor by virtue of the provisions relating to acquirenda since those provisions do not come to an end after the debtor's discharge. Where appropriate and if there is no bar on extending the period of the Trust Deed the office holder should take urgent steps to advise creditors of the reasons for the extension and a VAT refund claim should be submitted.
10. There could be practical issues arising from delaying closing cases which should be given careful consideration. The obvious one being the question of fees which is addressed under section 23 of this guide. The trustee may also find that he is faced with having to make more than one distribution in the case, for example where he was about to pay a dividend but now finds that he has to submit a VAT refund claim.

CLOSED CASES

11. If all the assets have been realised, available funds distributed, where the Trust has terminated and the trustee has obtained his discharge it is difficult to see how the former trustee would have a duty or any locus to act. Office holders should refer closely to the terms of the Trust Deed which may contain provisions on termination.

SEQUESTRATION AFTER A TRUST DEED OR FAILURE OF THE TRUST DEED

12. The position where there is a subsequent sequestration is not clear. In the case of *Salaman v Rosslyn's Trs (1900) 3 F 298* it was held that the trust was suspended until the sequestration process was complete. If the trust continues to subsist due to a failure in its terms to automatically terminate on sequestration, or where on sequestration no steps have been taken to bring the trust to an end, it is suggested that the trustee under the Trust Deed would have a duty and locus to act whereas the trustee in sequestration would not have the information available to allow a refund claim to be submitted. In such a situation the trustee under a Trust Deed would have to discuss the matter with the trustee in sequestration with a view to reaching a pragmatic agreement on the way forward.
13. In view of the above it is recommended that practitioners ensure that the Trust Deed document makes provision for the termination of the trust on sequestration.

CLAIMS PROCESS

14. The claims process is set out in HMRC's Notice 700/45. The time limit for making claims is four years. Office holders should note that this time cap is already running therefore refund claims need to be treated as priorities.
15. Office holders should take note of HMRC guidance which states:

"If the IP was fully taxable for the period covered by the claim then making a claim for a refund of wrongly declared output VAT will have the effect of making him partially exempt for the period of the claim. In that event, he will have to calculate the percentage of overhead or residual input VAT that should have been blocked. The input tax that will be deducted for the amount claimed will be both the input tax that was directly attributable to the supplies of services in question and, if the IP was already partially exempt, the appropriate percentage of the overhead or residual input VAT."
16. Any claim for wrongly charged VAT should be made by the Trustee. Thus where the trustee is not the registered person for VAT purposes the claim will be against the Firm which charged the VAT to the estate, which will in turn make a claim to HMRC.

RECEIPT OF FUNDS

17. In order to avoid unjust enrichment HMRC has stated that only net amounts will be refunded and that the whole amount of the refund is required to be paid into the insolvent estate from which the VAT was paid. In these circumstances it is understood that the major creditors' agents will not expect the office holder to make good the input tax adjustment. Office holders should be mindful of the potential for dissent from creditors who are not represented by agents and should take steps to obtain agreement from creditors to the proposed course of action.

18. Refunds received are in effect third party funds that in terms of the Client Money Regulations require to be segregated from those of the firm. Such funds should be distributed at the earliest opportunity.

ALLOCATION OF FUNDS RECLAIMED

19. Case specific input tax recovered must be applied to the respective cases.
20. Where refunds include deductions for input tax wrongly claimed as a consequence of the partial exemption rules applying, office holders are required to calculate the appropriate amount to be credited to each estate. It is recommended that the simplest and most equitable method of calculation is to apportion the input tax arising from the application of the partial exemption rules rateably across the cases.

FEES

21. Given that any refund claims are assets of the insolvent estate office holders are entitled to seek recompense for pursuing claims. Fee requests must be made in accordance with legislation and with the relevant Statements of Insolvency Practice.
22. A practical problem arises in instances in which a fixed fee was agreed prior to the *Paymex* decision being published. Office holders will have proposed a fixed fee based on an assessment of the case at commencement which would have excluded pursuing the refund claim. There could now be resistance from creditors to allow a further fee on the basis that the fixed fee should cover all assets. Office holders will need to consider whether or not to seek approval for a fee in respect of claiming the refund and how best to approach the matter.

PROTECTION AGAINST CHALLENGE FROM A CREDITOR

23. Where the office holder has concluded that it would not be in the interests of creditors to pursue a refund claim he must retain details of his reasoning and of what steps he took to obtain the consent of creditors to his course of action.
24. It may be possible for the office holder to argue that failure to pursue a claim did not result in actual loss to the trust estate however the office holder requires to take account of the time and effort involved in rebutting any action that might be brought against him. The office holder might consider whether he should seek the authority of the court not to ingather the asset, but clearly there are attendant costs.
25. Where the terms of the Trust Deed contain a specific power for the trustee to abandon an asset the trustee would be entitled to decide against pursuing the refund. If the trustee decides not to pursue the VAT refund he must ensure that his decision is properly documented and can be justified.
26. The Trust Deed document itself may contain an immunity or indemnity clause however such clauses do not offer protection against a positive breach of duty on the part of the trustee.
27. Office holders who propose not to pursue refund claims are advised to seek legal advice to protect their positions.