

# Tolley's

## Practical VAT Newsletter

YOUR MONTHLY GUIDE TO THE LATEST VAT DEVELOPMENTS

# The pinball wizard – it all goes back to 1969

### The taxation of gambling – are you up to date?

There has been a plethora of business briefs, tax cases and European Court rulings, as well as the US Congress, all cracking down on the online gambling business. This makes it worth a gallop through the changes. From 1 November 2006 the application of VAT to pinball machines has been restored.

In September 2006 the US Congress passed the Unlawful Internet Gambling Enforcement Act. In a single day this US legislation apparently wiped £3.7bn off the value of a market previously worth £6.5bn.

### The non-recreational 'pro-punter'

The 'exchanges'/online gambling/internet gambling have created a new personality – the 'non-recreational player'. What is the tax position of the pro-punter?

In practice, if HMRC tried to assess the gambling 'winners' to tax there would be a deluge of loss claims. The cautious tax practitioner should advise clients to keep a record of their winnings in case evidence is required at a later stage. HMRC always like to verify sources of income and windfalls in an enquiry situation so it is important to keep records to avoid any future problems over the identification of any capital introduced into a business. The money laundering provisions also have a large potential impact for tax advisers and their clients and illustrate the need for information on gambling activities to be provided by the taxpayer to their professional adviser.

The tax question has to be asked, where does all the gambling revenue come from? If profits are made, what are the disclosure requirements and taxation considerations?

The current case law is set out in *Graham v Green* (1925) 9 TC 309, a case which concerned a man whose sole means of livelihood came from betting on horses at starting prices. This was deemed to be 'betting, pure and simple ... he is addicted to betting. There is no tax on a habit. I do not think "habitual" or even "systematic" fully describe a trade'.

### The bookmaker

Betting by professional bookmakers is assessable to tax even if carried on in an unlawful way (*Southern v AB* (1933) 18 TC 59). Private betting is not assessable, however habitual it might be. Private profits, if any, are also exempt from capital gains tax (*TCGA 1992, s 51 (1)*). Receipts from newspaper articles based on a betting system were, however, held to be assessable to income tax in *Graham v Arnott* (1941) 24 TC 157.

### The gaming machine

Business brief 15/06 dated 27 September 2006 and Business brief 16/06 dated 12 October 2006 have concentrated on the VAT position of the gaming machine.

Essentially, the placing of a bet (betting) is an exempt supply for VAT. However, the income from gaming machines is a VATable supply.

It appears that an HMRC direction in December 2005 might have caused a

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### POINTS OF LAW

*Mayflower Theatre Trust; Kalron Foods Ltd; Dunwood Travel Ltd; Ford Motor Company Ltd; Atlantic Holidays Ltd; Lymington Power Boat Charter; Caledonia Motor Group Ltd; Premier Foods (Holdings) Ltd*  
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muddle. The problem seems to arise from the interaction with machines that provide a game of chance. Clarity is given in the briefs and indeed two new Treasury Orders come into effect on 1 November 2006, whereby the definition of 'gaming machine' and 'game of chance' are established, and the application of VAT to pinball machines is restored.

The key tax planning advice has to be that for all those businesses, sports clubs, social clubs, public houses and bookmakers with any form of gaming machine they must check that the VAT has been treated/charged correctly.

### **The bookmaker and the provision of TV services**

Business Brief 17/06 dated 19 October 2006 deals with the provision of TV services by bookmakers. Betting is an exempt supply for VAT and gaming machines are not. Do we pity the bookmaker who has to deal with the partial exemption computation? There is more complication from the Brief, but in the bookmakers' favour. The Business Brief follows Tribunal decisions in *Town & Country Factors* (19616). The Tribunal

found in favour of the company on the principle that the TV facilities had a direct link to TV racing service. Again, here is an interaction with the gaming machine which highlights the need to correctly establish the VAT position on the ancillary services provided by the bookmaker.

### **The tax rock of Gibraltar**

On the basis that online (internet) gaming companies are all essentially 'dotcom' businesses, it has been relatively simple for these companies to establish themselves in the low tax jurisdiction of Gibraltar. Such establishment presents a significant tax saving, as they do not have to pay the UK corporation tax rate of 30%. Online gaming companies generally have low staff and premises costs and therefore escape the disadvantages of Gibraltar's tax focus. This could be considered a substantial advantage for shareholders.

The European Union has been trying hard to abolish Gibraltar's exempt company tax regime. The European Commission deemed that these tax rules provide companies domiciled in Gibraltar with a rather distinct unfair tax advantage.

It was actually described as 'regional selectivity'. Could this mean that the online gaming companies based in Gibraltar could find themselves paying 30% corporation tax? No. A recent European Court ruling stated that Gibraltar's 1969 constitution provides Gibraltar with fiscal autonomy and it should be able to continue to provide companies with a low cost tax regime up until the end of 2010.

### **Blink and it all changes**

The gambling industry is changing and growing on a daily basis. It is essential that the tax adviser keeps in touch with all that is happening in the UK gambling industry.

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# VAT time bomb for farms' diversified activities

**Once upon a time barns and farm buildings were full of farm produce and machinery, and farm cottages were full of farm workers.**

It would appear that very few farmers and landowners have calculated their VAT partial exemption calculations correctly. Indeed, many do not even realise that they *are* partially exempt traders. Historically, the farming VAT return was a simple affair. Agricultural outputs were zero-rated, so there was virtually no output VAT and the maximum input VAT could be claimed, subject to minor debates about the private use of telephones and the dreaded 'scale charge' for motor vehicles. The only other problem was 'blocked' input tax on non-business activities.

How times have changed. The majority of farmers have moved away from the pure trade of farming and into the 'land and property' sector. The implications include not only charging tax on standard-rated supplies but also restricting input tax claims to take account of exempt supplies (the 'partial exemption' calculation), not to mention consideration of the 'option to tax'. Many farmers have not enjoyed a VAT inspection for some time (in some cases, for as long as ten years) and there could be a potential time bomb.

The first step must be for the farmer

to list all the supplies made by the farm and note any which are standard-rated or VAT-exempt. So what qualifies as standard-rated?

Examples are income from holiday cottages, caravan and camping pitches; from parking and sporting facilities; and from selling the right to fell and remove standing timber. The farmer must then ensure that VAT is charged and accounted for on all standard-rated supplies. However, more complex and serious problems are likely to arise when the farm generates substantial VAT-exempt income.