

# Duty Calls

## Introduction

While countries tend to go to war over disputes concerning oil, individuals, at least in the UK, end up instead before the VAT and Duties Tribunal, which has jurisdiction to decide on decisions issued by HMRC concerning application of the Hydrocarbon Oils and Duties Act 1979 (HODA). HODA provides the basis for charging excise duties on different categories of oils in the UK, and typically the Tribunals hear a handful of cases relating to HODA every year. The last report on these cases in this column came in July 2006, which means it is high time for an update to cover the more interesting of the cases coming to light since.

## A matter of definition

Any duty-charging provision must have, as its basis, a definition of the goods that are subject to charge. In *Afton Chemicals* E01041, the taxpayer sought to argue that mineral oil additives added to fuel to enhance its properties fell outside the definition of goods which could be subjected to excise duty under Directive 92/12/EEC. The appellant's argument relied on a strict interpretation of the legislation, which had apparently omitted from the charging provision mineral oil additives where those additives were passive (that is, they did not function as a propellant but as a cleaner). HMRC's argument relied on a purposive interpretation: it was clearly the object of the legislation to bring additives to fuels within the charge to duty, as non-mineral oil additives had been expressly included, and the legislation should be interpreted accordingly. Ultimately HMRC won out in this appeal on the basis that Community Law is interpreted broadly in accordance with purposive criteria. It would have given rise to a perverse result had the decision been given the other way, as mineral oil additives would escape from duty, whereas other additives performing the same function would still fall within the charge.

HODA recognises different categories of oil, not only by reference to their intrinsic properties ('light oil',

## *Adam Rycroft, Senior Solicitor, McGrigors LLP, looks at case law developments in the field of hydrocarbon oil and duties*

'heavy oil' and 'gas oil' being significant categories) but also by reference to the use to which the oils are put. The differentials in duty rates between fuels used for different applications are significant and so a system has been developed to mark low-duty fuels with chemical markers and dyes to assist in detection of illegal use, that fuel being commonly referred to as 'red diesel'. While red diesel cannot normally be used in vehicles constructed or adapted for use on roads, there is an excepted category which includes agricultural tractors, such as were considered in *Neales Waste Management Ltd* E01092. HMRC challenged the appellant's

movement a farmer might undertake on public roads between different fields, which is accepted by HMRC to be solely for agricultural purposes. The Tribunal allowed the appeal in part, finding that the second tractor used to pick up the pulp was used partly for a waste management function and so was excluded from the category of excepted vehicle. The first tractor, which was used in the process of spreading the pulp fertilizer, was used solely for an agricultural process and so qualified as an excepted vehicle.

*Midland Oil Refinery Ltd* E01076 concerned a company that specialised in the reclamation and processing of

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entitlement to operate on red diesel on the basis that the tractors were not used 'solely for purposes relating to agriculture' (the relevant test in HODA, Sch 1, para 1(2)).

The two vehicles were used in the appellant's business, which involved the disposal of pulp from paper mills by spreading the pulp onto farmers' fields. One of the tractor units was used to spread the pulp and to haul a JCB vehicle between farms. The other tractor was used to pick up the pulp from the paper mill and then also to spread the pulp. HMRC argued that in picking up the pulp the second tractor was performing a waste management, as opposed to agricultural, function, and that the first tractor similarly was being used for 'haulage' of the JCB and was not therefore used solely for agriculture. The appellant likened the movement of the tractors to the normal

used oils for resale, which it did by subjecting the oils to various processes, including distillation. HODA recognises a basic charge to duty arising at the time of production of oils, production being defined in s 2(4) to include 'the subjecting of hydrocarbon oil to any process of purification, or blending'. As the appellant had subjected the oil to such a process, the Tribunal found it had 'produced' the oil, meaning that the basic charge to tax had arisen. It seems the appellant came under further criticism because it had also, in breach of the terms of the relevant marking regulations (the Hydrocarbon Oil (Marking) Regulations 2002 (SI 2002/1773)), applied its own red dye to the fuel and sold it for use as red diesel. The appellant also sought to rely on the terms of a derogation that had been applied for by the UK and allowed under Community Law allowing it to charge

lower rates of duty in relation to the reuse of oil. While the Tribunal accepted the derogation existed, it concluded, quite rightly, that if the Member State did not implement legislation taking advantage of the derogation, a taxpayer had no right of action in Community Law.

### Back to basics challenges

The first question for a legal adviser to consider when reviewing any assessment is whether it has been validly made or, more particularly, whether the assessment has been raised under the correct authority and within the correct time limits. This is borne out by the facts in *Morris Young (Perth) Ltd* E01032, which concerned a 'global assessment' for duty relating to the unauthorised use of red diesel, which HMRC purported to make under the authority of HODA, s 13(1A), enacted with effect from May 2000. A global assessment is an assessment that does not clearly identify separate amounts due by reference to tax points and tax periods.

The appellant challenged the assessment on the basis that part of the assessment fell before May 2000 and HMRC had no authority to raise

the facts, of which the cases on HODA have their fair share. Many such cases that come before the Tribunal concern appellants who have been unlawfully using red diesel. Where a commercial vehicle is found to have been using red diesel, it is HMRC's practice to obtain further information concerning the mileage of the vehicle and to require the vehicle owner to produce fuel receipts. Where those receipts are not forthcoming, inevitably an assessment will be raised based on the vehicle's previous mileage. Similarly, where vehicles are utilised for private use, it is the policy of HMRC to impose fines and, if appropriate, to seize vehicles. Many of the appeals coming before the Tribunal relating to HODA concern the exercise of these powers of seizure and assessment and the inevitable excuses put forward by the vehicle owners, which often give rise to a distinct whiff of perjury.

In *Neil Willoughby* E01062, the Tribunal considered an assessment made where kerosene was found in the appellant's vehicles and then a further storage tank was found on the site containing kerosene. HMRC assessed on the basis that all 41,275 litres of

in dismissing the appeal as not having been made out on the facts.

In another case, *Morag Jackson* E01029, before the Scottish Tribunal, the Tribunal was initially convinced by a slightly fantastical story put forward by the appellant. The appeal, which concerned the seizure of two vehicles that were found to contain red diesel on the site of the appellant's farm, centred on how the fuel came to be in the vehicles. The appellant described to the Tribunal an extended family living locally, involved in red diesel fraud. These relatives, it was claimed, were pursuing a vendetta against the appellant and had deliberately filled the vehicles up with red diesel and then tipped off HMRC. The appellant also claimed that HMRC had visited on numerous occasions in the past and in each case the vehicles had tested negative for red diesel.

While it is clear the Chairman thought the decision of HMRC was wrong, the Tribunal can only review and not substitute a decision of HMRC so far as seizure and restoration of goods is concerned. In the normal course of events HMRC would usually reverse its decision, but in this instance HMRC upheld the original decision when it came to further review. Inevitably the appellant again appealed against the further decision. When the case came back to Tribunal in *Morag Jackson* E01089, HMRC presented further evidence to the Tribunal to establish that the local 'problem family' had in fact been involved in the use of kerosene and not red diesel, and that HMRC had not previously visited and tested the appellant's vehicles. No doubt suspecting the Tribunal had been spun a line, the Chairman dismissed the appeal this time.

### Conclusions

This case summary has shown that there is still a broad spread of case law arising in relation to HODA, ranging from technical arguments involving huge sums of money (the *Afton Chemicals* appeal concerned more than £2.8 million) to factual disputes involving small penalties (the *Jackson* case concerned a restoration fee of £750). Given the increasing demand for and price of oil, it might be expected that the already deep well of case law in this area will continue to grow and merit further exploration.

Adam Rycroft can be contacted on 01619 358008 or at [adam.rycroft@mcgrigors.com](mailto:adam.rycroft@mcgrigors.com).

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an assessment under s 13(1A) relating to a period before that date. While HMRC sought to amend the assessment to exclude amounts payable in relation to the period before May 2000, the appellant argued that the assessment was wholly invalid. The Tribunal agreed with the appellant on the basis that the assessment was a 'global assessment'; if an assessment is not adequately broken down by reference to tax points and periods, the assessment is not susceptible to severance (in this case the assessment could not be separated into amounts clearly falling before, and after, May 2000), with the consequence that it must be struck down in its entirety.

### Disputes on the facts

For every case of high legal principle there is another that relies only on a low-down and dirty fight on the basis of

kerosene purchased over a two-year period had been used as fuel in the appellant's vehicles. The appellant, who operated a garage, sought to argue that he had purchased the kerosene to fuel a space heater that was used year-round to make sure that glass being cut for use in his business did not delaminate. Unfortunately for the appellant HMRC sought advice from a heating engineer, who calculated that, on the basis of the fuel consumption identified in the appellant's records, the building's temperature would have risen to an unbelievable 119.6°Celsius. HMRC also referred to evidence from a technician of Autoglass Ltd, who advised that laminated glass was cut away from heated workplaces and could be cut at all temperatures, down to and below freezing. On the basis of the evidence, the Tribunal had no problem