Cause and effect

Indirect Tax



01 September 2016

Michael Conlon QC examines the impact of the CJEU decisions in *Bookit* and *National Exhibition Centre*

Key Points

What is the issue?

The CJEU has clarified, and arguably narrowed, the VAT exemption for card handling services where payment is made by credit card, while also suggesting they are ancillary to the underlying supply.

What does it mean to me?

For exemption to apply, the service must actually effect the transfer, not merely be an indispensable part of the transaction chain.

What can I take away?

A careful analysis of the exemption is required to determine functionality.

On 26 May 2016, the Court of Justice delivered the long-awaited judgment in Case C-607/14, *Bookit Limited v HMRC (Bookit)* and Case C-130/15, *National Exhibition Centre Limited v HMRC (NEC)*. The judgment came as a shock to businesses providing card handling services and overturned previous UK decisions. A month later, the United Kingdom voted to leave the European Union.

Facts

In *NEC* the taxpayer owns venues which it hires to promoters who stage events. NEC operates a box office and call centre where it sells tickets to customers, as agent of the promoter. Tickets may be sold over the counter, by post or via the internet. Where the customer pays by credit card or remotely by debit card, NEC charges the customer a booking fee. The stages of the transaction are:

1. NEC checks availability of the ticket and obtains the customer’s card details.
2. NEC transfers the details electronically to the merchant acquirer.
3. The merchant acquirer transfers the details to the card issuer.
4. If the card issuer accepts the transaction, it sends an authorisation code to the merchant acquirer.
5. The merchant acquirer sends the authorisation code to NEC.
6. NEC informs the customer of the sale and allocates the ticket.

At the end of each day, NEC creates an electronic file of all transactions and transfers the file electronically, via the merchant acquirer, to the card issuers. The

card issuers make payment to NEC via the merchant acquirer.

NEC remits the moneys to the promoter, less its booking fees.

In *Bookit*, the taxpayer was a subsidiary of Odeon Cinemas. The facts were similar to *NEC*, though complicated by the interposition between Bookit and the merchant acquirer of a third party, Data Cash. This difference, however, was immaterial. It is convenient, therefore, to focus on the *NEC* facts, as set out above.

The issues

Article 135(1)(d) of the Principal VAT Directive (PVD), formerly Article 13B(d)(3) of the Sixth Directive, exempts: 'transactions, including negotiation, concerning deposit and current accounts, payments, transfers, debts, cheques and other negotiable instruments, but excluding debt collection.' The issues were whether both taxpayers' services fell within the exemption. They argued that by obtaining the customer's card details and authorisation, confirming the booking and creating a file by which payment was automatically made, they had performed the function of debiting one bank account and crediting another. This was a transaction concerning a payment or transfer. NEC also argued that the service was not a debt collection service, as it was performed for the customer not the creditor. HMRC's case was that the service did not possess the essential characteristics identified in Case C-2/95, *Sparekassernes Datacenter* [1997] STC 932 (SDC) but comprised a ticketing service or debt collection.

Approach of the Court

The Court gave substantially similar judgments in each case, but without the benefit of an Advocate General's Opinion. Adopting observations made by the European Commission (but not by the parties), it questioned first whether the card handling operation was a supply separate and distinct from the underlying supply of tickets. In Case C-279/09, *Everything Everywhere* [2011] STC 316, an additional charge for card handling made by the supplier of mobile phone services to customers who paid by credit card was held to be part of the supply of phone services. This was because the card handling service could not be accessed separately and was not an end in itself. In *NEC/Bookit*, the Court suggested the same analysis: the processing formed

part of the promoter's infrastructure and was intrinsically linked, or ancillary, to supply of the tickets. This was left for the national court to decide on the facts.

Assuming, however, that there was a separate supply, the Court went on to analyse its nature as comprising three main elements: (1) obtaining card details and transmitting that information; (2) obtaining and transmitting the authorisation to proceed with the sale on behalf of the promoter; and (3) re-transmitting summary information at the end of each day to the banks to effect the transfer of funds. The Court repeated the customary 'mantras': financial exemptions constitute autonomous concepts of EU law; are to be construed strictly; are defined according to the nature of the service, not the identity of the supplier. It went on to affirm the test laid down in SDC. A 'transfer' is a transaction consisting of the execution of an order for the transfer of a sum of money from one bank account to another. In particular, it involves a change in the legal and financial situation existing, on the one hand, between the person giving the order and the recipient and, on the other, between those parties and their respective banks and, in some cases, between the banks. The transfer is simply the transfer of funds between accounts. The functional aspects are decisive. In *SDC*, the Court had also held that the Directive did not preclude the transfer from being broken down into separate services. However, to gain exemption, the services must, viewed broadly, form a distinct whole, fulfilling in effect the specific and essential functions of a transfer and entail changes in the legal and financial situation. A mere physical or technical supply is not enough. In Case C-350/10, *Nordea Pankki Suomi* [2011] STC 1956, however, the Court emphasised the need to examine the extent of the supplier's responsibility, namely: does it extend to the specific and essential aspects of the transfer, or is it restricted to technical aspects? But, in Case C-464/12, *ATP PensionService* [2014] STC 2145, the Court stated that 'intervention' by way of accounting entries on the account of payer or recipient is capable of falling within the exemption if it is an essential (indispensable) part of the transfer of funds. It does not presuppose use of a particular method.

Reasoning from these cases, in *Bookit/NEC* the Court held as follows. A card handling service may be described as 'indispensable' (because it results in the execution of a payment or transfer). However, the taxpayer in each case 'neither debits or credits directly the accounts concerned, nor intervenes by way of accounting entries, nor even orders such a debit or credit.' The taxpayer merely applies technical and administrative means to collect information and make a demand for payment in

electronic form. It is the customer who, by using his card, decides his account will be debited. Accordingly, neither Bookit nor NEC succeeded in gaining exemption. In light of its answer, the Court did not address the issue of whether a service supplied to the debtor can amount to debt collection.

Conclusions

The Court has attempted to resolve the tensions between SDC and later case law. It is now clear that a service forming part of a chain of transactions resulting in a transfer of funds is not necessarily exempt, even if it is an indispensable part. A 'but for not' test is not correct. It is not sufficient for the service merely to result in, or *have the effect of*, such a transfer. What is required is for the service to *effect* the transfer. The provider must actually debit or credit the accounts or intervene by causing the transfer and it must assume contractual responsibility for the transfer. Given that the Court's clarification involves a stricter test, it is not easy to see how in practice such a function might be broken down. The decision will have an impact on existing UK case law. *Bookit Limited v HMRC* [2006] STC 1367 (Bookit No. I) involved somewhat different facts, but the Court of Appeal's reasoning is now cast in doubt. So is the FTT's decision in *Way Ahead Group Limited v HMRC* [2104] UKFTT (TC) and aspects of the Upper Tribunal's reasoning in *HMRC v DPAS Limited* [2015] UKUT 585 (TCC). *CCE v FDR Limited* [2000] 672 remains correct, it would appear, as the taxpayer made payments out of its own funds. DPAS also raised the scope of 'debt collection' but, regrettably, this remains unclear. The impact of *Bookit/NEC* on developing payment systems (such as phone apps) will need to be carefully assessed.

Perhaps the most disturbing aspect of the Court's decision, however, is its reliance on *Everything Everywhere* to suggest a single supply analysis. That case is distinguishable on the facts because the same person was supplying both the mobile phone services and the card handling, whereas in Bookit/NEC they were supplied by separate legal persons. Is the Court in fact saying that there can be a single composite supply made by two different suppliers? If so, this would overturn longstanding Court of Appeal authority in *Telewest Communications plc v CCE* [2005] STC 481. Or is the Court merely saying that in real terms there was no supply at all by the taxpayers to the customers, their fees being part of the consideration for the ticket sales?

If BREXIT goes ahead, where will that leave us? During any transitional period the courts should, strictly speaking, continue to apply EU law principles and case law. But will there be more emphasis on precedents which favour the tax authorities? As the EU harmonised VAT system is unpicked from our domestic law, will there be more scope to reshape the law in a way more favourable to UK business? Will it be possible to reconcile Bookit No. 1 with *Bookit/NEC*? Time will tell. But, as in *Bookit/NEC*, we may see a marked difference between cause and effect.