TC02337

Appeal number: TC/2009/10391

FIRST-TIER TRIBUNAL
TAX CHAMBER

DIXONS RETAIL PLC **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE THEODORE WALLACE
JULIAN STAFFORD FCA

Sitting in London in public on 2-4 November 2011 and 22 and 23 March 2012

Amanda Brown, of KPMG LLP, for the Appellant

Peter Mantle, instructed by the Solicitor for HMR & C, for the Respondents

ORDER FOR REFERENCE

1.

UPON the appeal against the refusal of a repayment claim made on 5 February 2009 in respect of £1,940,921 declared on sales in the period 13 November 2005 to 30 November 2008

UPON HEARING Amanda Brown, of KPMG LLP, for the Appellant and Peter Mantle, instructed by the Solicitor for HM Revenue and Customs

AND UPON CONSIDERING further written submissions

IT IS HEREBY ORDERED that the questions set out in the Schedule hereto be referred to the Court of Justice of the European Union for a preliminary ruling concerning the interpretation of Articles 14.1 and 73 of Council Directive of 28 November 2006 (2006/112/EU)

AND IT IS DIRECTED that the proceedings before the Tribunal be stayed pending the said preliminary ruling.

THEODORE WALLACE
TRIBUNAL JUDGE

RELEASE DATE: 26 October 2012

SCHEDULE

REQUEST FOR PRELIMINARY RULING OF THE COURT OF JUSTICE OF THE EUROPEAN UNION BY THE FIRST-TIER TRIBUNAL (TAX CHAMBER) OF THE UNITED KINGDOM

I. INTRODUCTION

1. The First-tier Tribunal (Tax Chamber) of the United Kingdom ("the Tax Tribunal") seeks a preliminary ruling of the Court of Justice of the European Union ("the Court") pursuant to Article 267 of the Treaty on the Functioning of the European Union on questions concerning the interpretation of Articles 14.1 and 73 of Council Directive of 28 November 2006 (2006/112/EU) ("the Principal VAT Directive").

2. The questions relate to situations where a retailer has accounted for VAT on sales of goods for which customers have presented credit or debit cards fraudulently without the authority of the issuing banks and where the retailer has received payment from American Express Europe Ltd ("Am Ex") in respect of AmEx cards or from the merchant acquirer in respect of other cards and where the retailer has not been obliged to repay the payments once the frauds have been discovered.

3. The present proceedings before the Tax Tribunal have concerned the issues of principle and have not addressed the quantification of the claim.

II. THE QUESTIONS REFERRED

4. The Tax Tribunal seeks a preliminary ruling on the following questions:

> 1. Is Article 14.1 to be interpreted as applying when the physical transfer of goods is obtained by fraud in that the payment provided by the transferee is by means of a card which the transferee knows he has no authority to use?
>
> 2. When the physical transfer of goods is obtained by fraudulent use of a card, is there a "transfer of the right to dispose of tangible property as owner" within Article 14.1?
>
> 3. Is Article 73 to be interpreted as applying when payment is obtained by the transferor of goods under an agreement with a third party to make such payment in respect of card transactions notwithstanding that the transferee of the goods knows that he has no authority to use the card?
>
> 4. When payment is made by a third party pursuant to an agreement between the transferor of the goods and the third party as a consequence of the presentation to the transferor of a card which the transferee of the goods has no authority to use is the payment obtained from the third party "in return for the supply" within Article 73?

III. THE PARTIES

5. The Appellant, Dixons Retail PLC ("Dixons"), is registered for VAT as the representative member of a VAT group and claims repayment of VAT which was paid by members of the group which sold electrical items under brands such as Dixons, Currys and PC World.

6. The Commissioners (and their predecessors, the Commissioners of Customs and Excise) were and are responsible for the collection and management of VAT in the United Kingdom.

IV. THE RELEVANT FACTS

7. The proceedings concern a repayment claim made on 5 February 2009 in respect of £1,940,921 declared on sales in the period 13 November 2005 to 30 November 2008. The repayment claim was made and the appeal against the refusal was lodged by the predecessor of Dixons as representative member of the group, DSG International Plc.

8. The cards were issued or purportedly issued by banks using card schemes of which the largest were Visa and Mastercard and by AmEx. Dixons had a direct agreement with AmEx under which Dixons obtained authorisation from AmEx for charges and, subject to complying with the required procedures, was paid by AmEx.

9. Dixons did not contract directly with the banks using the other card schemes but contracted with National Westminster Bank plc as merchant acquirer; the trade name for the merchant acquiring activity of National Westminster Bank plc was "Streamline" and that name is used when referring to its merchant acquiring activities in order to avoid confusion with issuing banks.

10. For the transactions, other than those with AmEx, Dixons obtained prior authorisation from the issuing banks via Streamline and was paid by Streamline the value of all card transaction data presented subject to complying with the required procedures.

11. Under the agreements with AmEx and Streamline Dixons was obliged to honour all cards presented under the agreements as means of payment.

12. In respect of the transactions giving rise to these proceedings Dixons obtained authorisation and complied with the other requirements and was paid £1.12 million by AmEx and £11.91 million by Streamline, sums which included the VAT attributable to the sales. The transactions were in the main face to face, although some involved the use of internet to place an order, and at the time the transactions were believed by Dixons to be legitimate, having been authorised accordingly. Subsequently it was discovered that the cards had been presented fraudulently; usually this was discovered when the legitimate card member disputed the transaction on receiving an account from the issuing bank.

13. The frauds took a variety of forms which included identity theft, card cloning and obtaining cards by providing false information. In all cases the persons presenting the cards to Dixons knew that they were not entitled by the card issuer to

present the cards as the means of payment for the goods obtained. The proceedings did not cover transactions where a genuine card holder subsequently sought dishonestly to avoid payment to the card issuing bank.

14. When a transaction was disputed by the card member, the issuing bank notified Streamline which was entitled to issue a chargeback to Dixons in specified circumstances which included failure to produce evidence of the card holder's authority for the debit.

15. In relation to AmEx transactions AmEx had full recourse for any charge for which authorisation was refused, not properly requested or obtained, or for which no approval code was given.

16. These proceedings concerned transactions for which Dixons was paid by Streamline or AmEx but for which, although the cards were used fraudulently, no chargebacks were made by Streamline and no recourse was exercised by AmEx so that Dixons retained the payments including the VAT element.

17. When Streamline paid Dixons for the card transactions it deducted a merchant services charge covering three elements: the issuing bank's interchange fee, the card scheme fee and Streamline's fee as merchant acquirer. The merchant services charge over the period of the claim varied between £14.4 million in 2005 and £13.2 million in 2008, the interchange fee element representing over 90 per cent. The interchange fees were set by the card schemes based on costs which included processing of transactions, the free-funding period between the card holder incurring the charge and paying the issuing bank and the loss incurred by issuing banks from fraud when sums paid to merchants were not recovered from card holders but no chargeback to Dixons was possible. The obligation to pay Dixons regardless of recovery from card holders in circumstances where no chargeback was possible was described by the Appellant as a guarantee. The cost to the issuing banks of this obligation was a significant element of the interchange fee and was therefore a significant component of the merchant services charge paid by Dixons to Streamline although it was not quantified or identified in the card handling agreement between Dixons and Streamline.

18. The multi-lateral interchange fee ("MIF") under the Visa rules and regulations was the subject of a Commission Decision of 24 July 2002 (Case No. COMP/29.373).

19. The MIF under the UK domestic rules of Mastercard was the subject of a decision of the Office of Fair Trading on 6 September 2005 (No. CA 98/05/05).

20. There was no separate merchant acquirer in respect of transactions with AmEx cards. AmEx paid Dixons within three banking days of submission of the charge data less a service charge, based on electronic submissions and calculated as a relatively small percentage of the transaction value.

21. Fraud as a percentage of Dixons' turnover varied from 0.07 to 0.2 per cent in respect of Streamline transactions and from 0.07 to 1.13 per cent for AmEx transactions.

V APPLICABLE LAW

22. The submissions by the parties were based entirely on the Principal VAT Directive. There were no submissions based on domestic law. Part of the period covered by the repayment claim was before 1 January 2007 when the Sixth Directive

was replaced by the Principal VAT Directive. The submissions by the parties were on the basis that the enactment of the Principal VAT Directive involved no substantive change in the relevant law.

23. There is a possible tension between the words in the English version of Article 14.1 "the transfer of the right" and the French wording "le transfert du pouvoir", in that "pouvoir" can mean either power or authority whereas "right" would not normally encompass power without authority.

24. Section 1(1)(a) of the Value Add Tax Act 1994 provides that VAT shall be charged, in accordance with the provision of the Act, "on the supply of goods or services in the United Kingdom". Section 2(1)(a) provides for VAT to be charged on the supply of goods by reference to the value of the supply. Schedule 4, paragraph 1(1) provides that "any transfer of the whole property in goods is a supply of goods…." Section 5(2)(a) provides " 'supply' in this Act includes all forms of supply, but not anything done otherwise than for a consideration." Section 19 contains provisions for the determination of the value of a supply; section 19(2) provides that if the supply is for a consideration in money "its value shall be taken to be such amount as, with the addition of the VAT chargeable, is equal to the consideration".

VI SUMMARY OF THE RELEVANT SUBMISSIONS OF THE PARTIES

Submissions by Dixons

25 (a) Regarding the first question, the presence of a legal relationship requiring reciprocal performance is a fundamental criterion to the identification of a "supply of goods" within the meaning Article 14.1. This follows from the case law of the Court, in particular the judgment of the Court in *Tolsma* (C-16/93) [1994] ECR I-743 (in this respect see paragraphs 14 to 20).

(b) The existence of a supply will primarily to be determined by the terms of the agreement between the retailer and the cardholder. That follows from the approach adopted by the Court in *Chaussures Bally SA v Belgian State* (C-18/92) [1993] ECR I-2871 where the Court determined the "taxable amount" by reference to the agreement between the supplier and the customer and not by reference to the card payment system. An obligation to make payment through the card payment system does not, *ipso facto*, give rise to a supply under Article 14.1, which, as with any supply for VAT purposes, requires reciprocal performance.

(c) In connection with the second question it has already been held by the Court that obtaining goods by illegal means (*theft*) does not equate to a transfer of the right to dispose of tangible property as owner (see *British American Tobacco International Limited and another v Belgian State* (C-435/03)) [2005] ECR 1-7077. There is no legitimate distinction to be drawn between goods obtained illegally by theft and those obtained by fraud by reference to the objective facts associated with card fraud and theft.

(d) With respect to the third question and in accordance with the settled case law of the Court, any payment only forms part of the "taxable amount" to the extent that there is a direct link between the goods provided and the consideration received (for example in *Naturally Yours Cosmetics Ltd v Customs and Excise Commissioners* (C-230/87) [1988] ECR 6365. In the circumstances of a fraudulent card transaction there is no reciprocal assumption of any obligation by the fraudster in connection with the payment for the goods and thus no direct link between any sum received by the retailer and the release of the goods.

(e) With respect of the fourth question, it will be critical to identify what the payment is made for. The Court has already determined that the payments made by retailers through the card payment system are made in return for, inter alia, a payment guarantee (see paragraph 9 of the judgment in ***Bally*** and paragraph 73 of the opinion of the Advocate General in *Finanzamt Essen-NordOst v GFKL Financial Services AG* (C-93/10)). The payment of a sum against that guarantee is not a payment in discharge of any third party obligation (i.e. one owed by the fraudster or the cardholder) and is not part of the taxable amount for the goods.

Submissions by the Commissioners

26. (a) Questions 1 and 2 ask essentially whether, when a transaction involves the transfer of goods by a retailer to a customer, there is not a supply of goods if the customer commits a fraud, by using a credit or debit card which he knew he was not authorised to use.

(b) The Commissioners contend that there is plainly a supply of goods. It is then necessary to go on to consider Questions 3 and 4, which concern the consideration for that supply of the goods.

(c) Addressing Questions 1 and 2: typically, as agreed in the course of the transaction, the relevant goods were handed over to the fraudulent customer by the retailer, in the same way as they would have been to any other customer, that other customer then being free to use or actually dispose of the goods however he chose to. Such a transfer by the retailer is a supply of goods within Article 14.1.

(d) The transactions in the issue in the main proceedings are not identical to the theft of goods. The latter is a unilateral taking by the thief, with nothing agreed and no relationship between the thief and owner. Dixons' assertion that there is no distinction between this case and *British American Tobacco* is not correct.

(e) The state of mind, motive, or dishonest intent of a customer is not relevant to whether there is a supply within Article 14.1. An objective approach is required. A transaction is also not prevented from being a supply because it involves some fraud and is therefore "unlawful"; see e.g. *Optigen* (Case C- 354/03) [2006] ECR I - 483 at paragraphs 44, 45 and 49.

(f) Addressing Questions 3 and 4: the supplier received payment of the price of the goods from the third party bank. That payment was directly linked to the making of the supply of the goods to the customer, who had used a card as the means of payment for the goods. The Commissioners submit that payment from the third party bank constituted consideration obtained by the supplier, in return for the supply, from a third party. This is the analysis that is consistent with the Court's reasoning and ruling in *Chaussures Bally*. Again, the state of mind, motive, or dishonest intent of the customer is not relevant.

(g) It does not follow from the fraudulent intent of the customer, who knew that he was not authorised to use the card, that the payment by the third party bank is not "in return for the supply". Rather, the payment of the price by the bank constitutes consideration for the supply of the goods in that case, as in other instances where a card is used. The supplier was, in this transaction, obliged to accept the card as a means of payment for the goods handed over. The payment is manifestly directly linked to the transaction constituting the supply, and, in particular, the transfer of the goods to the customer by the supplier. The fact that the service provided by a third

party bank can be described as a “payment guarantee service”, and is paid for, does not support the conclusion that the payments received by the supplier are not consideration for the transfer of goods to the customer within the meaning of Article 73 (see *Chaussures Bally* at paragraph 9, 17 and ruling).

27. This case involves difficult issues of principle on which the Tribunal considers that a decision by the Court is necessary to enable the Tribunal to give judgment.