# Kluwer International Tax Blog

## The Contents of Highlights & Insights on European Taxation, Issue 3, 2023

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**Highlights & Insights on European Taxation**

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(comments by **Dilpreet K. Dhanoa**) (H&I 2023/63)

As always, it is important to note the statutory framework. The UK VAT Act and Regulations largely follow the VAT Directive, which in turn provides the following (in Article 26(1)):

- Each of the following transactions *shall* be treated as a *supply of services for consideration*:
- Goods which form part of a business's assets for the *private use* of a taxable person or his staff or, more generally, for purposes *other than those of his business*, where VAT on such goods was

wholly or partly deductible (Article 26(1)(a) of the VAT Directive).
- The supply of services is *carried out free of charge* by the taxable person for his private use or for that of his staff or, more generally, for purposes other than those of his business (Article 26(1)(b) of the VAT Directive).

The UK Regulations (specifically, Value Added (Supply of Services) Order 1992, Article 3) condenses the VAT Directive and makes clear that:

- where a taxable person is carrying on a business; and,
- puts services supplied to him to *any* private use *or* uses them, *or* makes them available to any person for use;
- for a purpose *other than a purpose of the business*;
- [such person] shall be treated as supplying those services in the course or furtherance of the business.

The matter originally started in the FTT on the basis that GEAES stated that no standard-rated supply arose by operation of Article 26(1)(b) of the VAT Directive. Instead, it argued that the 'Above & Beyond' programme was simply an 'overhead of GEAES's economic activities in the UK', and thus any benefit to its employees was secondary. In seeking to draw a distinction between GEAES's *purpose* in providing vouchers to some employees, and the subsequent (private) use of the same *by* the employees, GEAES argued that it had a business purpose in providing the vouchers and thus the provision of the same rendered it outside the scope of Article 26(1)(b) of the VAT Directive. Accordingly, it argued that there was no taxable supply of services.

In relying on the CJ's decisions in *Danfoss* (CJ 20 October 2011, C-94/10, ECLI:EU:C:2011:674) and *Fillibeck* (CJ 16 October 1997, C-258/95, ECLI:EU:C:1997:491), GEAES advanced the case that its core objective as a taxpayer was to ensure the smooth running of its business. In the case of *Danfoss* (C-94/10), the CJ concluded that where meals were provided for a strict business purpose (on account of vouchers being provided for staff to acquire lunch), no charge should arise. In examining the underlying factual matrix, the CJ came to this conclusion on the following bases:

- the lack of choice by the employee of what, when and where to eat;
- the relatively basic nature of the fare; and, critically,
- the fact that the meals were provided to ensure the smooth running of business meetings.

In other words, the strict business purpose test was met.

In *Fillibeck* (C-258/95), an employer recovered VAT on the cost of providing transport to his staff to get them from their homes to construction sites. Commuting expenditure is generally considered private, and the CJ was asked to consider whether it was appropriate to apply a charge to reflect the private use by the employees. The CJ's starting point was that, in principle, a charge applied. Having closely examined the underlying factual matrix, however, it concluded that it was practically impossible for the employees to get to the site on their own, and, accordingly, a private use charge should *not* be applied. The principle to be drawn from this case was therefore whether it is *necessary* for the taxable person to provide goods or services that are enjoyed privately in order for them to make their taxable supplies ('the necessity test').

HMRC asserted that Article 26(2)(b) of the VAT Directive applied on the basis that the vouchers supplied to staff were provided for their private use. In other words, the provision of the vouchers was not essential to the smooth running of the business, and nor were the vouchers necessary.

Furthermore, HMRC argued that the fact that there may be some business purpose was not sufficient in and of itself, and was irrelevant. In other words, HMRC's assertion was that because the requirement of Article 26(1)(b) of the VAT Directive was met (namely, private use by employees), there was no further need to consider whether the vouchers were being supplied for a business purpose. The basis for this argument was that, in HMRC's submission, Article 26 of the VAT Directive should be construed objectively, and thus it was of no relevance as to what GEAES considered the purpose of its provision of the vouchers to be.

In departing from the Opinion of Advocate General ('AG') Capeta, the CJ held that the scheme was, in fact, implemented for a business purpose (and was thus outside the scope of the VAT Directive). In setting out its clear and robust analysis of the position, the CJ made clear that the VAT Directive treats certain transactions for which *no* consideration is *actually receivable* as a supply of services for consideration. This is to ensure that the *purpose* of the provision is actually met: namely, that there is equal treatment between, on the one hand, a taxable person who applies goods or services for his or her own private use or for that of his or her staff and, on the other hand, a final consumer who acquires goods or services of the same type. The CJ made clear that if that objective was borne in mind, Article 26(1)(a) of the VAT Directive 'prevents a taxable person who has been able to deduct VAT on the purchase of goods used for his or her business from escaping payment of that tax when he or she applies those goods from his or her business for his or her own private use or that of his or her staff and from thereby enjoying advantages to which he or she is not entitled by comparison with an ordinary consumer who buys goods and pays VAT on them.'

In setting out the approach to the first part of Article 26(1) of the VAT Directive in this way, the CJ stated that Article 26(1)(b) of the VAT Directive similarly 'prevents a taxable person or members of his or her staff from obtaining, free of tax, services provided by the taxable person for which a private individual would have to have paid VAT…'.

In closely examining the underlying factual matrix, the CJ held that the way in which the 'Above & Beyond' programme was designed, operated and structured leant towards it being 'aim[ed] at improving the performance of its employees and, therefore, of contributing to better profitability of the business.' As a result, the CJ's robust conclusion on this aspect was that 'the setting up of that programme was dictated by considerations relating to the proper conduct of that undertaking's business activities and the pursuit of additional profits, the resulting advantage for employees being merely incidental to the needs of the business.'

Furthermore, the CJ specifically noted that the retail vouchers in question gave employees receiving them the right to benefit from them (by obtaining goods and/or services) from specific retailers. Accordingly, the retail voucher 'by its nature is *no more than a document evidencing the obligation* assumed by the referenced retailers to accept that retail voucher, instead of money, at its face value …'.

Another fact of strong persuasive value for the CJ was that GEAES (in its capacity as the employer) did not intervene in the choice of goods or services made by employees when using the vouchers from the specific retailers. Accordingly, the CJ's position was that 'if account had to be taken only of the use made of them, the retail vouchers at issue would have to be regarded as being for the employees' private use.'

Finally, the fact that GEAES awarded the vouchers *without remuneration and not in return for any consideration* on the part of the employees who received them – that is, GEAES bore the cost of

the vouchers – was a strong indication that the 'supply of services gives GEAES an advantage in the form of the prospect of increasing its turnover as a result of the greater motivation of the employees and, as a result, an improvement in their performance.' Any personal advantage to the employees was again, therefore, seen as incidental.

Although the FTT was encouraged by the CJ to ensure that it, too, undertook a proper finding of the facts, the CJ's clear position was that the tests set out in Article 26(1)(b) of the VAT Directive were *not* met, given that:

- the 'Above & Beyond' programme was intended to increase employee performance;
- therefore leading to the 'proper functioning and profitability of the business'; and
- with the result being that a supply of services is *not* carried out.

The reason for such detailed consideration of the CJ's position is that it throws into sharp relief the contrast with the position of the AG. While both considered this to be a case concerning the principle of fiscal neutrality, and ensuring this was applied in GEAES, the AG held that, in applying *Fillibeck and AstraZeneca* (Case C-371/07), the test of 'necessity' should be applied and that this required two objective elements:

- first, the existence of a link between a service provided free of charge and the taxable person's economic activity; and,
- secondly, the presence of control over the use of that service to ensure that it is indeed used in relation to or in the furtherance of the taxable person's economic activity.

The AG's Opinion focused principally on two issues: the language of Article 26(1)(b) of the VAT Directive and the application of the business purpose test. Notably, in respect of the latter, she considered the legal conundrum from a slightly different angle to that of the CJ: in particular, whether the transfer of the vouchers (free of charge) to the employees amounted to a chargeable event subject to VAT and, if so, whether such a VAT charge would lead to double taxation of a single supply. In addressing these issues, the AG, like the CJ, looked at whether the service provided was 'necessary' for the taxable person's business. In adopting a different position to the decision subsequently handed down by the CJ, the AG held that there was a risk in permitting the taxable person too much of an opportunity to determine what could be identified as 'necessary' in its business and that this would put courts in an 'awkward position' of having to second-guess a business's decision with respect to 'true necessity'. The focus of her analysis revolved around this and the application of Article 62 of the VAT Directive (that is, what amounts to a 'chargeable event'); she concluded that the supply of the vouchers fell within the embrace of Article 26(1)(b) of the VAT Directive and that it was 'of no significance … that the taxable person has a business purpose for the issuance of such vouchers.'

The author respectfully disagrees with the position advanced by the AG and considers the robust and purposive approach adopted by the CJ to be more in line with the body of authority and application of the fiscal neutrality principle – which gives effect to the wording of Article 26(1)(b) of the VAT Directive – rather than simply stating it to be of no significance. It cannot be the case that when the wording of a provision makes it clear that 'business purpose' is a central element, such is then considered to be of no consequence.

*Dilpreet K. Dhanoa*

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