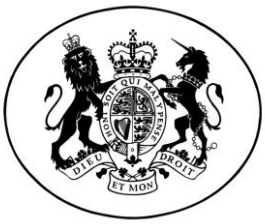
[2019] UKFTT 0715 (TC)



TC06858

Appeal number: TC/2016/05290

VAT – 'fall-back' acquisition VAT where UK registered trader uses UK VAT registration to zero rate acquisitions into another member state – whether charge applies on acquisitions into bonded warehouses – yes – whether it is chargeable on taxpayer – yes – whether VAT is recoverable as input tax – no

FIRST-TIER TRIBUNAL
TAX CHAMBER

AMPLEAWARD LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE BARBARA MOSEDALE

Sitting in public at Taylor House, Rosebery Avenue, London on 10 October 2018

Mr M Firth, Counsel, instructed by TT Tax, for the Appellant

Ms N Barnes, Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. The appellant is an alcohol wholesaler. On 19 September 2016, HMRC assessed it for acquisition VAT of £1,308, 648 in respect of acquisitions in 09/12 to 03/16.

Assumed Facts

2. The facts which were assumed for the purposes of this hearing, but were not agreed or proved, were as follows:

(a) The appellant was an alcohol wholesaler that was approved to own excise duty suspended alcoholic goods in tax warehouses in the UK from October 1999;

(b) During the period in question, the appellant received goods, from its suppliers, into its accounts in a tax warehouse in a member State other than the UK.

(c) Those goods travelled across another EU border before being placed in the appellant's accounts;

(d) Its suppliers have included the appellant's UK VAT registration number in their VAT returns to zero-rate the movement of goods across the EU border;

(e) The appellant's customers were not registered in the member State to which the appellant's suppliers despatched the goods;

(f) The appellant was also not VAT registered in the member State in which the goods were received. It did not itself account for the acquisition tax in either the member State in which the goods were received nor in the UK.

3. In summary, the goods were at all relevant times held under duty suspense, moving from one excise duty warehouse to another. The appellant acquired the goods from a trader which was VAT registered in another member State. The sale to the appellant was free of VAT as the appellant gave the seller its UK VAT registration number. The goods were delivered to the appellant (into an excise duty warehouse) in a third member state. I will refer to this as 'the Third Country'. The appellant then sold the goods to its customer(s). Neither the appellant, nor any customer of the appellant, was registered for VAT in the Third Country. Moreover, HMRC do not know and the appellant did not say, which member State was the Third Country.

4. That, at any rate, was the position at the start of the hearing. In his reply at the end of the hearing, Mr Firth said that most of the transactions at issue in this appeal would have been acquisitions into the Netherlands. He appeared to accept that acquisition VAT was payable in the Netherlands but considered it would have been 100% recoverable as input tax; he suggested the reason the appellant was not VAT registered in the Netherlands was because it used the Dutch fiscal representative system. He said the real reason why the appellant had not provided HMRC with the

requested information was because it was an expensive exercise to go through the paperwork in respect of lots of different transactions. The appellant's view was that if VAT was due in the Third Country, it was for that country's tax authorities to take action and not for HMRC to assess VAT.

Basic VAT principles

5. The parties were agreed, I believe, that the normal rule was that intra-Community acquisition of goods for consideration by a taxable person was subject to VAT. Taking away the 'VAT-speak', this meant that when a person who was (or was liable to be) registered for VAT bought goods (such as the alcohol the subject of this appeal) which had to be dispatched or transported to him from another member State, that person was liable to VAT on the goods in the Member State of arrival.

6. In brief, while any purchase of goods would normally be subject to VAT, where 'acquisitions' were concerned, acquisitions being where goods crossed a boundary between member States, the VAT was (under the normal rules) accounted for by the buyer in the country of arrival rather than the seller in the country of dispatch.

7. But that is just the normal rule; various provisions of the directive provided for a different liability in certain circumstances. And that was what the dispute was about in this case.

8. For instance, there were the rules on triangulation. It was agreed, however, that that simplification measure did not apply in this case. The effect of it would be to make the appellant's customer(s) liable to account for the VAT on the sale to the appellant. But that measure could not apply in this case because a prerequisite is that the customer is VAT registered in the country in which the goods were delivered (the Third Country). As the appellant's customer(s) was not registered in the Third Country, triangulation could not apply.

9. The appellant therefore appeared liable to pay VAT in the Third Country on its acquisitions referred to above, but that, of course, is not for HMRC to assess. While it was HMRC's position that VAT was going missing, the appellant did not accept it was in breach of the law in any country. At the same time, it did not, at least until the very end of the hearing, explain on what basis it considered it did not have any outstanding VAT liability in the Third Country.

10. The issue in this appeal was its liability to the assessment for UK VAT: the question was whether the appellant was liable to account for VAT in the UK in circumstances where it did not seek to prove that it had properly accounted for VAT in the Third Country. The appellant, as I have said, insisted that it was properly accounting for VAT within the Third Country but its position was that it did not have to prove this simply to avoid an assessment to UK VAT. HMRC's position was that the UK legislation should not be interpreted in the way put forward by the appellant as that facilitated fraud within the EU irrespective of whether the appellant itself was properly accounting for VAT.

11. I note in passing, by way of explanation for how the assessment the subject of this appeal came about, that while it was unclear whether the Third Country would even know of the delivery of the goods into a warehouse on its territory, HMRC were aware of the sale to the appellant because of EC Sales Lists. Traders selling goods cross border are required to make returns recording the identity of the buyer: HMRC therefore knew from the seller that the appellant made VAT-free acquisitions using its UK VAT registration number. HMRC then purported to assess the appellant under s 13(3) of the Value Added Tax Act 1994 ('VATA').

12. The appellant's position is that there is no power to assess it under VATA. A preliminary hearing was called in this appeal to decide four agreed questions which would have the potential of resolving this appeal without the need for any finding of facts.

Preliminary issues for determination

13. Those four issues were:

(1) Does VATA s 18(3) take precedence over VATA s 13(3) if both provisions would otherwise apply?

(2) If VATA s 13(3) takes precedence over VATA s18(3) is the occurrence of the acquisition subject to VATA s 18(4)?

(3) Is s 18(7) limited to goods warehoused in the UK?

(4) Is acquisition VAT due under s 13(3) recoverable as input tax in accordance with the rules in VATA ss 24-26?

The relevance of these questions will become apparent from the below discussion of the applicable EU and UK legislation.

The EU law provisions

14. The dispute is over how s 13 and s 18 of VATA should be interpreted. The answer to that may depend on the EU provisions which they were intended to implement. So I will set out both s 13 and 18 and the relevant related provisions of the Principle VAT Directive ('PVD').

The normal place of supply

15. Article 40 of the PVD provided the normal rule for the place of supply of goods despatched between VAT registered businesses. The 'place of supply' is the place where the tax is due:

> The place of an intra-Community acquisition of goods shall be deemed to be the place where dispatch or transport of the goods to the person acquiring them ends.

16. Under this rule, the place of supply would be the Third Country. The dispatch of the goods ended there: that is the country in which the supplier delivered the goods. It was not the UK and under this rule the UK could not tax the supply.

The fall-back place of supply

17. However, there is a rule in the PVD, which the parties referred to as the 'fall-back rule', which provided an exception to the normal rule, as follows:

> **Article 41**
>
> Without prejudice to Article 40, the place of an intra-Community acquisition of goods as referred to in Article 2(1)(b)(i) shall be deemed to be within the territory of the Member State which issued the VAT identification number under which the person acquiring the goods made the acquisition, unless the person acquiring the goods establishes that VAT has been applied to that acquisition in accordance with Article 40.
>
> If VAT is applied to the acquisition in accordance with the first paragraph and subsequently applied, pursuant to Article 40, to the acquisition in the Member State in which dispatch or transport of the goods ends, the taxable amount shall be reduced accordingly in the Member State which issued the VAT identification number under which the person acquiring the goods made the acquisition.

18. The Directive therefore establishes a seemingly simple rule: while the actual place of supply is where the dispatch ends, where a trader uses a VAT registration number of a different member state, that member state will be deemed to be the place of supply (and entitled to collect the VAT) unless and until the trader can demonstrate that the VAT was actually 'applied' in the member State to which the goods were dispatched.

19. I note in passing that the appellant seemed to suggest that 'applied' in Article 41 did not mean paid but simply referred to liability to pay: that must be wrong as it would make a nonsense of the fall-back provision as it was intended as a rule to ensure VAT was paid somewhere within the EU. 'Applied' must mean that VAT has been properly accounted for: it would not necessarily require VAT to be paid in hard cash, but it would require proper accounting and to the extent that a balance of VAT was due, for the VAT to have been paid.

20. Moving on, if article 41 could be relied on by HMRC, on the facts of this case, the assessments the subject of the appeal would be valid: the appellant has not proved that it has properly accounted for VAT in the Third Country, which was the actual place of supply. So under the 'fall back' rule of Article 41, VAT was due in the UK which was the member State which issued the appellant with the VAT registration number which it utilised to receive a VAT-free supply from its supplier. I will refer to such VAT as 'fall-back VAT' to distinguish it from normal acquisition VAT.

21. The appellant does not accept that that is the correct outcome because its case is that the UK has not properly implemented Art 40 and Art 41 and/or because it does not accept that article 41 has any application where a member State has implemented article 157(1)(b), as the UK has done.

The UK's fall-back rule

22. Section 13 VATA sets out the rules on the normal and fall-back place of supply and is clearly intended to implement Articles 40 and 41 of the PVD. The normal place of supply rule is in s 13(2). The fall-back rule is in s 13(3) - (5) as follows:

> (3) Subject to subsection (4) below, the goods shall be treated as acquired in the United Kingdom if they are acquired by a person, who for the purposes of their acquisition, makes use of a number assigned to him for the purposes of VAT in the United Kingdom.
>
> (4) Subsection (3) above shall not require any goods to be treated as acquired in the United Kingdom where it is established, in accordance with regulations made by the Commissioners for the purposes of this section, that VAT –
>
> > (a) has been paid in another member State on the acquisition of those goods; and
> >
> > (b) fell to be paid by virtue of provisions of the law of that member State corresponding, in relation to that member State, to the provision made by subsection (2) above.
>
> (5) The Commissioners may by regulations make provision for the purposes of this section –
>
> > (a) for the circumstances in which a person is to be treated as having been assigned a number for the purposes of VAT in the United Kingdom;
> >
> > (b) for the circumstances in which a person is to be treated as having made use of such a number for the purposes of the acquisition of any goods; and
> >
> > (c) for the refund, in prescribed circumstances, of VAT paid in the United Kingdom on acquisitions of goods in relation to which the conditions specified in subsection (4)(a) and (b) above are satisfied.

As I will explain below, it was accepted by both parties that the UK has not made any regulations as referred to in s 13(4) or (5).

The VAT warehousing regime

23. S 18 VATA also provided an exception to the normal rule contained in s 13. It only applied to goods in a warehousing regime. Precisely what that meant was in dispute between the parties but s 18(3) clearly only applied to 'dutiable goods' and it was accepted that the goods the subject of this appeal were dutiable goods. They were alcohol.

24. S 18 in so far as relevant provided as follows:

> (2) Sub-section (3) below applies where –
>
> (a) any dutiable goods are acquired from another member State; or

(b) any person makes a supply of –

(i) any dutiable goods which were produced or manufactured in the United Kingdom or acquired from another member State; or

(ii) any goods comprising a mixture of goods falling within sub-paragraph (i) above and other goods

(3) Where this subsection applies and the material time for the acquisition or supply mentioned in subsection (2) above is while the goods in question are subject to a warehousing regime and before the duty point, that acquisition or supply shall be treated for the purposes of this Act as taking place outside the United Kingdom if the material time for any subsequent supply of those goods is also while the goods are subject to the warehousing regime and before the duty point.

(4) Where the material time for any acquisition or supply of any gods in relation to which sub-section (3) above applies is while the goods are subject to a warehousing regime and before the duty point but the acquisition or supply nevertheless falls, for the purposes of this Act, to be treated as taking place in the United Kingdom –

(a) that acquisition or supply shall be treated for the purposes of this Act as taking place at the earlier of the following times, that is to say, the time when the goods are removed from the warehousing regime and the duty point; and

(b) in the case of a supply, any VAT payable on the supply shall be paid (subject to any regulations under subsection (5) below)-

(i) at the time when the supply is treated as taking place under paragraph (a) above; and

(ii) by the person by whom the goods are so removed or, as the case may be, together with the duty or agricultural levy, by the person who is required to pay the duty or levy.

25. The effect of s 18 was to deem the place of supply to be outside the UK in certain circumstances. So s 13(3) deemed the place of supply to be *within* the UK in circumstances which both parties agreed applied to the goods in this case, but s 18(3) deemed the place of supply to be *outside* the UK, in circumstances which the appellant said applied to the goods in this case. Hence, it was agreed that this Tribunal should determine as a preliminary issue which of these two provisions took precedence and whether or not s 18(3) did apply in the agreed circumstances of this appeal.

26. Unlike s 13, s 18 did not enact a compulsory provision of the PVD. S 18 was intended to enact an optional provision of the PVD and that was Art 157. As it is highly relevant, I set it out here:

Article 157

1 Member States may exempt the following transactions:

a. The importation of goods which are intended to be placed under warehousing arrangements other than customs warehousing;

b. The supply of goods which are intended to be placed, within their territory, under warehousing arrangements other than customs warehousing.

Article 162

Where Member States exercise the option provided for in this section, they shall take the measures necessary to ensure that the intra-Community acquisition of goods intended to be placed under one of the arrangements or in one of the situations referred to in Art 156, article 157(1)(b) or Article 158 is covered by the same provisions as the supply of goods carried out within their territory under the same conditions.

27. One oddity was that article 157(1)(b) provided for an exemption from VAT; s 18 which (apparently) implemented it moved the place of supply outside the UK. I will revert to this point below. Another point to note is that while s 157(1)(b) referred to exemption, Article 169 made it clear that it was an exemption with refund. In other words, it was effectively equivalent to a zero-rate: the trader was not liable to account for VAT on its sale but could recover any attributable input tax. A zero-rate was truly a complete exemption from VAT. Where I refer below to 'exemption' I mean exemption with refund, or, in other words, a zero rate.

28. The appellant's case was that s 18(3), which apparently was intended to implement article 157(1)(b), did apply in the circumstances of this case and did take precedence over s 13, so the acquisition by it in the Third Country of excise goods was exempt from UK fall-back VAT. However, its last point was that, if it was wrong on that, then the UK fall-back VAT was immediately recoverable by it because of the directly effective provisions of the PVD which allow input tax recovery:

Article 168

In so far as the goods and services are used for the purposes of the taxed transactions of a taxable person, the taxable person shall be entitled, in the Member State in which he carries out these transactions to deduct the following from the VAT which he is liable to pay:

(a) the VAT due or paid in that Member State in respect of supplies to him of goods or services, carried out or to be carried out by another taxpayer person.

29. By way of explanation, it was accepted that the appellant had made a supply of the goods to its customer(s) so it appears it was its case that if article 168 applied, it was entitled to make a self-cancelling entry in its UK VAT account and, therefore, the assessment would be invalid. Whether it was right on this was not a question I was asked to consider. I move on to the questions I was asked to rule on.

Question 1: which of the provisions has precedence?

30. The first question was whether s 13(3) (the fall-back provision) or s 18(3) took precedence in circumstances where both appeared to be applicable on the facts. The appellant's case was that the answer is plain on the face of VATA as s 13 provided:

> **13 Place of acquisition**
>
> (1) This section shall apply (subject to sections 18 and 18B) for determining for the purposes of this Act whether goods acquired from another Member State are acquired in the United Kingdom.
>
> ….

As a matter of law, therefore, said the appellant, the statute clearly provided that s 18 took precedence over s 13.

31. HMRC did not accept that answer. It seemed that their reasons for saying so could be divided into two: on the one hand, HMRC argued that s 18 did not apply to the facts of this case; on the other hand, HMRC argued that s 13 and s 18 must be interpreted so that s 18 was seen as subject to s 13. I deal with each in turn but first consider the applicable principles of statutory interpretation.

32. HMRC's case was that s 13 and s 18 must be interpreted in the manner in which any provisions implementing EU directives must be interpreted, and the correct approach was that was set out by the Court of Appeal in *Vodafone II* [2009] STC 1480 at [37-38] –

> [37]…… 'in summary, the obligation on the English courts to construe domestic legislation consistently with Community law obligations is both broad and far-reaching. In particular:
>
> (a) it is not constrained by conventional rules of construction…
>
> (b) it does not require ambiguity in the legislative language…
>
> (c) it is not an exercise in semantics or linguistics….
>
> (d) it permits departure from the strict and literal application of the words which the legislature has elected to use….
>
> (e) it permits the implication of words necessary to comply with Community law obligations….
>
> (f) the precise form of the words to be implied does not matter….
>
> [38] … 'the only constraints on the broad and far-reaching nature of the interpretative obligation are that:
>
> (a) the meaning should 'go with the grain of the legislation' and be 'compatible with the underlying thrust of the legislation being construed'….An interpretation should not be adopted which is inconsistent with a fundamental or cardinal feature of the legislation since this would cross the boundary between interpretation and amendment…..
>
> (b) the exercise of the interpretative obligation cannot require the courts to make decisions for which they are not equipped or give rise to

> important practical repercussions which the court is not equipped to evaluate…..'

33. I did not understand the appellant to seek to suggest these principles were in any way wrong or inapplicable. So I will bear in mind these principles as I consider each parties' case.

S 18 did not apply as provisions mutually exclusive?

34. HMRC had two grounds for saying that s 18 did not apply. The first was their case that s 13(3) and s 18(3) could never apply to the same factual position because s 13(3) only applied if acquisition VAT was due in another member State and s 18(3) only applied if acquisition VAT was not due in another member State.

35. This argument relied on the provisions of s 18(7) and therefore was very much an argument which relied on the words used by the UK Government to implement the derogation contained in article 157(1)(b) ('the bonded warehouse exemption'). It was a case that the UK had placed a limited interpretation on warehousing arrangements by its definition of 'warehousing regime' which was:

> (7) references in this section to goods being the subject to a warehousing regime is a reference to goods being kept in a warehouse or being transported between warehouses (whether in the same or different member States) without the payment in a member State of any duty, levy or VAT; and references to the removal of goods from a warehousing regime shall be construed accordingly.

36. HMRC's point was that s 18(7), and therefore s 18(3), only applied if the goods were transported from one warehouse to another without there being any liability to pay <u>any</u> excise duty, customs duty or VAT. HMRC's point was that, while all the warehouses concerned were bonded warehouses in the sense that no excise duty was payable on movement from one to another, even across national borders, that was not true of VAT.

37. In particular, it was HMRC's case that *only* the UK and Republic of Ireland had implemented article 157(1)(b) of the PVD so only the UK and Ireland had warehouses between which goods could move free of all excise duty, customs and VAT. Their case was that the goods in question in this appeal were not subject to a warehousing regime as they would have been subject to VAT in the Third Country under the normal rule referred to above, as s 157(1)(b) would not have been implemented (assuming that the Third Country was not the Republic of Ireland).

38. The law in another country is, of course, a matter of fact, and this preliminary hearing was called only to determine points of law. While HMRC did produce a statement from the French tax authorities which said French TVA would be due on an acquisition into a French bonded warehouse, I cannot make any finding about this evidence. While at the end of the hearing, the appellant indicated that most of the supplies were to bonded warehouses in the Netherlands and also appeared to accept

that VAT was due on acquisitions into the Netherlands, the hearing was not called to resolve matters of fact.

39. I will proceed on the basis of the point of principle and make the assumption that the goods were delivered to a bonded warehouse in a member State which had not implemented s 157(1)(b). Making that assumption, is it right to say s 18(3) would not apply?

40. The appellant did not agree that s 18(3) would not apply. It criticised HMRC's interpretation of 'warehousing regime' on two grounds. Firstly, it said s 18(7) should not be read as requiring all duties and taxes to be deferred on entry into the warehouse, as that was not consistent with s 18(6) which defined a warehouse as

> …any warehouse where goods may be stored in any member State without payment of any one or more of the following, that is to say –
>
> (a) customs duty;
>
> (b) any agricultural levy of the European Union;
>
> (c) VAT on the importation of the goods into any member State;
>
> (d) any duty of excise or any duty which is equivalent in another member State to a duty of excise.

To be consistent with s 18(6), s 18(7) must be read as meaning 'any one or more' by the use of the word 'any'.

41. I agree with the appellant that its interpretation is a much more natural construction under ordinary rules of statutory construction but I have to bear in mind the rather different rules required when construing legislation implementing the directive and so this point is far from conclusive.

42. The appellant's second and more fundamental criticism of HMRC's construction was that it made s 18(3) a somewhat nonsensical provision that could not really apply in any circumstances. In particular, as interpreted by HMRC, for s 18(3) to apply, it required the goods to move from one bonded warehouse to another in circumstances where no VAT or other duties were charged: but whether VAT was chargeable on the movement into a UK warehouse depended on whether s 18(3) itself applied. S 18(3) was the only provision which granted the VAT 'exemption'. It was a 'chicken and egg' situation that was incapable of resolution.

43. In conclusion, by adopting HMRC's interpretation, I would deprive s 18(3) of all application, and the result would be that I would be amending (by deleting) rather than interpreting legislation, contrary to what was said in *Vodafone II.* I can see the force in what the appellant says here. The Government clearly intended to implement article 157(1)(b) and adopting HMRC's interpretation would result in reversing that implementation. It would certainly have important practical implications for other traders that this Tribunal is ill-equipped to evaluate. I reject HMRC's interpretation.

S 18(3) did not apply because it was of limited application?

44. HMRC's second line of attack on the appellant's interpretation of s 18(3) was to point out that the UK's implementation of article 157(1)(b) in s 18 was not entirely in accordance with the PVD. Its case was that s 18 should be interpreted, in accordance with *Vodafone II,* to be consistent with article 157(1)(b).

45. I have already noted that article 157(1)(b) did not permit the UK to move the place of supply outside the UK. S 157 only permitted the UK to confer an exemption with recovery (effectively a zero rate). Nevertheless, the effect of s 18(3) moving the place of supply was to confer something that operated in much the same way as the exemption with refund actually permitted by article 157(1)(b). HMRC did not, therefore, suggest this was a relevant discrepancy between article 157(1)(b) and s 18(3).

46. The appellant's case was that this discrepancy was relevant to its appeal: I will revert to this point at §§57-60. In the meantime, I consider the other discrepancies.

47. HMRC did rely on the fact that article 157(1)(b) only permitted the UK to derogate from the normal rules in articles 40 and 41 in relation to goods which 'are intended to be placed, *within their territory,* under warehousing arrangements'. If the appellant's interpretation that s 18(3) took precedence over s 13(3) was correct, the result was that the UK had derogated from the normal rules in articles 40 and 41 in respect of goods moving from warehousing between two other member states, and not within the territory of the UK. By doing so, the UK would have exceeded the derogation granted to it by article 157(1)(b).

48. The appellant did not accept that the words 'within their territory' was intended to limit the derogation to goods within the member State granting the exemption. It pointed out that article 157(1)(b) referred to intra-State movements, and article 162 to acquisitions (inter-State movements). The words 'within their territory' did not qualify article 162: the requirement was simply to treat acquisitions in the same way as the supply of goods *within their territory* would be treated. It was just the usual provision insisting on equality of treatment for traders from other EU member States with the member States' own traders.

49. But that interpretation, it seems to me, makes a nonsense of art 157(1)(b) and article 162. It is also a mis-reading. While it is true that the phrase 'intra-Community acquisition of goods' in Art 162 is not qualified by the words 'within their territory', nevertheless it is a necessary implication that the obligation is so limited. And that is *because* Article 162 is the equality provision: it was intended to do no more than require a member State, choosing to give its own traders the optional bonded warehouse exemption, to extend the same exemption to all EU traders.

50. Logically, therefore, article 162 only required the member state to exempt acquisitions into *that member state's bonded warehouses*. To give EU traders the right to exemption when moving goods to a bonded warehouse in a different member state goes well beyond the exemption permitted to national traders by article 157(1)(b), which is clearly limited to bonded warehouses *within* that member state.

51. Article 162 was only a provision which required equality of treatment: it was not a provision which was intended to confer further exemption beyond that contained in article 157(1)(b). Nor would there be any reason for it to permit a member state to confer exemption on movements between bonded warehouses entirely beyond its own national borders.

52. That this is the correct interpretation of article 157(1)(b) and article 162 is made plain by article 155 which applied to the entire section of the PVD under which articles 157 and 162 fell. It provided:

> **Article 155**
>
> Without prejudice to other Community tax provisions, Member States may, after consulting the VAT Committee, take special measures designed to exempt all or some of the transactions referred to in this Section, provided that those measures are not aimed at final use or consumption and that the amount of VAT due on cessation of the arrangements or situations referred to in this Section corresponds to the amount of tax which would have been due had each of those transactions been taxed within their territory.

53. The very first words of Article 155 makes it clear that the derogations were not intended to prejudice other Community tax provisions; while the derogation in article 157(1)(b) certainly does appear to derogate from the normal rule in Article 40, it is in practice consistent with the remainder of Article 155 as the derogation does not authorise rules which lead to less tax being paid overall than under the normal rules set out in article 40 and 41. It is not, in effect, prejudicial to articles 40 and 41.

54. However, the same could not be said of the appellant's interpretation of article 157(1)(b) and 162. The appellant's interpretation overrides article 41. Article 41 is a rule that is designed to prevent tax avoidance or evasion: it makes a trader liable to pay VAT in its member state of registration if it cannot prove it has paid the VAT due in the member State which was entitled to collect it. Therefore, the Directive could not have intended the effect of article 162 to override the fall-back provision of article 41, the purpose of which was to prevent VAT loss.

55. The appellant suggested that such an interpretation would cause problems: but the only alleged problems postulated by the appellant were all ones where a trader sought to move goods from a warehouse in one member state to a warehouse in another member using the VAT registration number of a third member state. This seemed rather to prove HMRC's point. The directive permits such behaviour but article 41 requires VAT to be paid in the member state of registration except to the extent that the trader can prove it properly accounted for VAT in the member state of actual arrival. Article 157(1)(b) was not intended to permit a member state to derogate from this as on its face it only applied to bonded warehouses within the national territory, nor would it make any sense for the Directive to be read in a way which facilitated VAT loss.

56. One further point on this is the appellant's example of an acquisition into a UK bonded warehouse using a third country's VAT registration number: the UK would regard it as VAT free but HMRC's interpretation of the PVD would see the fall-back

provision being used by the third member state. That third member state would not remit the VAT because there would be no evidence of VAT 'applied' in the UK because no VAT was payable in the UK, at least at that point in time, because the UK had adopted the bonded warehouse exemption. But it seems to me that the problem here postulated by the appellant is not with the predominance of article 41 over the derogation permitted by article 157(1)(b), but whether article 41 is read to mean that VAT must be paid in the third member State even if it is not payable in the UK. Properly, art 41 should be read as meaning fall-back VAT is only due if VAT was not properly accounted for in the Third Country. But even if article 41 is read as applying in a situation where no VAT was payable because the Third Country (in this example, the UK) had adopted s 157(1)(b), ultimately VAT would become due in the UK (on duty point or departure from warehouse) so the fall-back VAT ought eventually be remitted under article 41(2). Therefore, this example does not suggest that in order to facilitate such a situation and avoid the need to pay and later reclaim VAT, the EU must have intended to take the risk of complete VAT loss by subordinating Article 41 wherever a member state chose to enact a derogation only intended to apply within its territory. So I reject the appellant's point on this.

57. Another point made by the appellant was that Articles 155-162 permitted the UK to introduce an exemption with refund; what the UK chose to do was to move the place of supply. Doing so created a conflict with the normal rules on place of supply in s 13 (enacting articles 40-42) and the need to state precedence in s 13(1). That did not happen in the PVD where articles 40-42 dealt with place of supply and articles 155-162 with exemption.

58. While I agree with the appellant that the UK's method of implementing the derogation appears inept, I do not think it helps the appellant's case. As I have already said, even though there is no need for explicit precedence to be given in the PVD between articles 40-42 and articles 155-162, the PVD (art 155) nevertheless has made it clear that the exemptions in 155-162 cannot be used to result in less VAT being payable. Implicitly, article 41 cannot be overridden by a derogation because it would result in less VAT being payable.

59. The CJEU has already considered how article 41 should be interpreted. It is a rule to prevent VAT loss and to encourage compliance with the normal place of supply rule (see *Facet* discussed below at §§85-6). It is clear that articles 155-162 must be read as subject to article 41.

60. In conclusion, I agree with HMRC that the PVD did not permit a member state to implement article 157(1)(b) in such a way that article 41 was effectively overridden. Article 157(1)(b) only permitted a member state to exempt intra-state supplies between bonded warehouses and acquisitions into the bonded warehouses within that particular member state.

61. Reverting to *Vodafone II*, the rules of construction I am required to apply permit me to depart from the strict and literal application of the words which the legislature has elected to use where necessary to comply with Community law obligations. I find the UK had no power under s 157(1)(b) to exempt from VAT a dispatch and acquisition of goods which actually occurred outside the UK nor did it have power to

derogate in those circumstances from the fall-back provisions of article 41. It seems s 18(3) should be read to make it consistent with article 157(1)(b) if doing so would not be incompatible with the grain of the legislation nor give rise to important practical repercussions the tribunal could not evaluate.

62. Reading s 18(3) as limited to goods which are already within, or arrive within, a bonded warehouse the UK, does not deprive s 18(3) of its intended meaning; on the contrary it limits s 18(3) to the derogation that Parliament no doubt intended to implement. Parliament cannot have intended to go beyond the permitted extent of article 157(1)(b) and indeed the references to 'goods… acquired from another member State' in s 18(2) suggests the author was envisaging the goods would be present or arrive in bonded warehouses in the UK and had merely overlooked the fall-back provision which deemed goods to be acquired in the UK even if never actually present in the UK.

63. Reading s 18(3) as limited to goods actually supplied or acquired in the UK rather than deemed to be acquired in the UK does little or no violence to the language used and might even have been permitted under the normal rules of statutory construction in any event. As s 18(3) can only be read consistently with the Directive as if it did not apply to transactions only deemed to be within the UK, then that is the reading it should have.

64. The appellant's interpretation of s 18(3) is literal but inconsistent with articles 41, 155 and 157(1)(b). Applying *Vodafone II* means that s 18(3) must be read as limited to goods physically within, or transported to, bonded warehouses in the territory of the UK. In conclusion, I agree with HMRC that s 18 did not apply to the goods at issue in this appeal as they were never in a UK bonded warehouse.

Article 41 has precedence

65. HMRC's last argument was that s 13(1) should be read as if the words 'subject to sections 18 and 18B' were not there because those words were inconsistent with the Directive which stated, on the contrary, that the derogation in article 157(1)(b) and other derogations in that section of the PVD were 'without prejudice to other Community tax provisions' (see article 155 cited above).

66. I have already largely dealt with this argument. My interpretation of s 18(3) is that, as it is limited to goods actually in, or acquired into, UK bonded warehouses, it is not in conflict with article 41 and, although it is necessarily a derogation from article 40, it does not lead to less tax being due overall than otherwise. It is merely a simplification measure. That conclusion makes it unnecessary to consider whether it would be right under *Vodafone II* to read those words out of existance; as to do so would plainly affect other provisions, and therefore impact on traders in different positions, I would be reluctant to do so as again it might lead to practical repercussions this Tribunal could not evaluate.

67. HMRC's next case was that 'subject to sections 18 and 18A' should be read as only qualifying s 13(2) and not s 13(3). They say the qualification was essential for s 13(2) as it is essential to treat inter-member State acquisitions the same as domestic

supplies, but that it is not essential for s 13(3). I do not really follow the logic of this argument as the exemption was contained in s 18(3): making s 18(3) subordinate to s 13(3) would deny EU traders selling goods into a UK bonded warehouse the same favourable treatment as UK traders selling into a UK bonded warehouse. The Directive does not permit differential treatment: see article 162. So I reject that interpretation as well.

Conclusion

68. My conclusion is that s 18(3) does not apply on the agreed facts of this appeal. While I agree with the appellant that s 18(3) predominates over s 13(3), in the circumstances of the agreed facts of this case, my conclusion is that s 13(3) applies simply because s 18(3) is not applicable. While VATA does provide that s 18 and 18B predominate over s 13, that is only the case to the extent that s 18 or 18B are actually applicable. On the facts of this case, s 18(3) does not apply because the acquisition was not into a UK bonded warehouse. The acquisition was into a bonded warehouse in a different EU member State.

69. That conclusion does not conclude the appeal. The appellant's next argument was that even if the supply was deemed to take place in the UK, the time of supply was shifted.

Question 2: Assuming s 13(3) takes precedence over s 18(3), is the occurrence of acquisition subject to s 18(4)?

70. The appellant's case was that even if s 13(3) applied rather than s 18(3), nevertheless its acquisitions were still within s 18(2) (as 'dutiable goods acquired from another member State…') and therefore, although s 13(3) deemed the acquisitions to be in UK, s 18(4) still applied to (a) shift the time of supply to the time which was the earlier of the duty point or departure from bonded warehouse and (b) to shift the liability to pay the VAT to the person required to pay the duty or who removes the goods.

71. Were the appellant correct, I presume it would be its case it could not be shown to be liable to the assessments as HMRC do not know if and when the goods became liable to duty or left the bonded warehouse; not do they know who was liable to pay the duty or moved them from the warehouse. I do not comment on whether or not this is correct, but deal with the proposition that s 18(4) applies even if s 18(3) does not.

72. I assume the basis of the appellant's argument was that, if it lost on Question 1, that could only be because s 13(3) predominated over s 18(3). Therefore, s 18(3) applied but the appellant had liability under s 13(3); but because s 18(3) applied, s 18(4) also applied.

73. However, my view is that on a proper reading of s 18(3), s 18 does not apply where the acquisition is actually in another member state and only deemed under s 13(3) to be within the UK. S 18(4) only applies in circumstances 'to which subsection (3) above applies' so s 18(4) cannot apply as s 18(3) does not apply on the agreed facts of this appeal.

74. In support of its case, the appellant relied on SI 1995/2518 r 41 which provided:

> Where in respect of –
>
> (a)….
>
> (b) an acquisition by any person from another member State of dutiable goods,
>
> The time of …acquisition….precedes the duty point in relation to those goods, the VAT in respect of that …acquisition shall be accounted for and paid….by reference to the duty point or by reference to such later time as the commissions may allow.

75. However, this is not a provision which operates independently of s 18. On the contrary, it was enacted under s 18(5) which only gave HMRC power to make regulations in respect of persons falling within s 18(4). While on its face it might appear to apply to the appellant who has made an acquisition within the UK from another member State, as I have said, under the principle of conforming interpretation, s 18(3), and this regulation, must be understood as only applying to actual acquisitions rather than deemed acquisitions into the UK.

76. I dismiss the appellant's case on this. Neither s 18(3) nor s 18(4) applies as the acquisition was not into a UK bonded warehouse.

Question 3: Is s 18(7) limited to goods warehoused in the UK?

77. While the question of s 18(7) is posed separately, it seems to me it is really a subset of the first question. The appellant's point is that on its face, s 18 applied to goods moving between foreign member States' bonded warehouses as it expressly said so:

> (7) references in this section to goods being the subject to a warehousing regime is a reference to goods being kept in a warehouse or being transported between warehouses (<u>whether in the same or different member States</u>) without the payment in a member State of any duty, levy or VAT; and references to the removal of goods from a warehousing regime shall be construed accordingly. (my emphasis)

78. The appellant's conclusion is that it follows that s 18(3) was intended to refer to goods kept in a bonded warehouse in any member State.

79. There are two problems with this position. Firstly, s 18(3) does apply to acquisitions from non-UK warehouses into UK warehouses. So the definition is not otiose even on the interpretation of s 18(3) given by this Tribunal at §§50-51. Secondly, s 18 must be read to conform with the Directive so in the same way that s 18(3) must be understood only to apply to goods which arrive in a UK bonded warehouse, s 18(7) must be read to be consistent with that interpretation.

80. So although s 18(7) does apply to goods which move between warehouses in different member states, s 18(3) and (4) for the reasons already given only apply where the warehouse of arrival is in the UK. The effect is that the appellant is liable to fall-back VAT under s 13(3) on the facts which it seeks to prove.

Question 4: Fall-back VAT is recoverable in the UK

81. The appellant's last argument, in case it was found wrong on the first 3 questions, was to say that even if it was liable to UK VAT under s 13(3) it was entitled to recover it as input tax so it was only obliged to make a self-cancelling accounting entry in its VAT books: it had no actual liability to pay any VAT at all. The assessment, said the appellant, should be discharged.

82. It points out that VAT on acquisitions is 'input tax' under s 24:

> **S 24 VATA Input tax and output tax**
>
> (1) Subject to the following provisions of this section, 'input tax' in relation to a taxable person, means the following tax, that is to say -
>
> ….
>
> (b) VAT on the acquisition by him from another member State of any goods; and
>
> ….
>
> being (in each case) goods or services used or to be used for the purposes of any business carried on or to be carried on by him.

83. Input tax is recoverable to the extent it is used or to be used for the purposes of transactions that would be taxable if made in the UK:

> **S 26 VATA Input tax allowable under section 25**
>
> (1) the amount of input tax for which a taxable person is entitled to credit at the end of any period shall be so much of the input tax for the period (that is input tax on supplies, acquisition and importations in the period) as is allowable by or under regulations as being attributable to supplies within subsection (2) below.
>
> (2) The supplies within this subsection are the following supplies made or to be made by the taxable person in the course or furtherance of his business –
>
> …..
>
> (b) supplies outside the United Kingdom which would be taxable supplies if made in the United Kingdom.

84. I have already said that the appellant has given HMRC no information about what has happened to the goods. I presume that its case is that if it made supplies with the goods, those supplies would have been taxable if made within the UK and therefore it only has to show that it sold the goods, and not that it accounted for VAT on the sales. In any event, the appellant could not rely on s 26 unless it can and actually does show that it made supplies of the goods which would have been taxable if made within the UK. I will precede on the basis it can demonstrate this (but it remains to be proved).

The ruling in Facet

85. Even if the appellant could demonstrate that it made a supply of the goods which would have been taxable if made within the UK, HMRC does not accept that

the appellant is entitled to recover the fall-back VAT it is liable to pay in the UK on the acquisitions at issue in this appeal. For this HMRC relies on the ruling in *Facet* C-539/08). In *Facet*, the CJEU made it clear that tax charged under article 41 is not recoverable as input tax. Having recited the effect of the provisions of the Directive (then the Sixth VAT Directive [6VD] but now contained in the PVD), the CJEU said:

> [35] It follows that [what is now Article 41 PVD] seeks first to ensure that intra-Community acquisition in question is subject to tax and, secondly, to prevent double taxation in respect of the same acquisition.
>
> ….
>
> [39] The question therefore arises whether a taxable person must be allowed a right to immediate deduction in the case where [in accordance with what is now Art 41] having failed to establish that the intra-Community acquisition in question has been subject to VAT in the Member State of arrival of the dispatch or transport, that taxable person is subject to that tax in the Member State which issued the identification number.
>
> [40] [the right to deduct VAT] is subject to the condition that the goods and services acquired are to be used for the purpose of the taxable person's taxable transactions.
>
> [41] However…the goods….did not actually enter that Member State.
>
> [42] In those circumstances, those transactions cannot be regarded as giving rise to a 'right to deduct'…consequently, such intra-Community acquisitions cannot benefit from the general regime of deduction…
>
> …
>
> [44] Furthermore, the granting of a right to deduct in such a case would risk undermining the effectiveness of [what is now Article 41] in view of the fact that the taxable person, having had the right to deduct in the Member State which issued the identification number, would no longer have any incentive to establish that the intra-Community acquisition in question had been taxed in the Member State of arrival of the dispatch or transport. Such a solution could ultimately jeopardise the application of the basic rule that, in the case of an intra-Community acquisition, the place of taxation is deemed to be the Member State of arrival of the dispatch or transport, that is to say, the Member State of final consumption…..
>
> [45] In view of the foregoing considerations, …a taxable person coming within [what is now Article 41] does not have the right immediately to deduct the input VAT charged on an intra-Community acquisition.

Can HMRC rely on ruling in Facet?

86. The answer under EU jurisprudence to the fourth question is clear: there is no right to deduction of fall-back VAT. The *only* way to recover the VAT is to show that VAT was properly accounted for in accordance with article 40 in the member State of arrival of the dispatch or transport. This is because, explained the CJEU:

(a) It is contrary to 6VD/PVD to give right to deduct VAT in member state the goods did not enter; and in any event

(b) Giving a right to deduct undermined the entire purpose of the fall-back provision which was to ensure VAT was paid in the member State of acquisition

87. The appellant does not agree that UK can refuse it input tax recovery by reliance on this decision by the CJEU: its point is that (it says) the *Facet* ruling is no part of the jurisprudence of the UK. While it does not and could not suggest that the CJEU's interpretation of the 6VD (now the PVD) was wrong and/or not binding on the UK, the appellant does say that it is not possible for the UK to rely on a part of a Directive it has not chosen to implement. And there is nothing in VATA or any other UK legislation which directly implements *Facet*. There is nothing in s 24 or s 26 VATA, says the appellant, which excludes s 13(3) VAT from the definition of input tax.

88. It relies on the decision of the CJEU in *Marshall* C-152/84 for the proposition that a state may not rely on the provisions of a directive against an individual:

> With regard to the argument that a Directive may not be relied upon against an individual, it must be emphasised that according to Art 189 of the EEC Treaty the binding nature of a Directive, which constitutes the basis for the possibility of relying on the directive before a national court, exists only in relation to each member State to which it is addressed. It follows that a directive may not of itself impose obligations on an individual and that a provision of a Directive may not be relied upon as against such a person.

89. It also relies on the *Zurich Insurance* case [2006] EWHC 593 (Ch) for the proposition that *Marshall* applies to VATA:

> [15] *[Marshall]* was not a VAT case, but the principle certainly applies to VAT. It should be read subject to the 'principle of consistent interpretation' under which a national law (like the VATA) should so far as possible to construed so as to conform to the meaning of the directive. Nevertheless, when a question arises as to whether a person had been lawfully assessed to pay an amount of VAT in the United Kingdom, the first question which logically arises is whether the liability assessed has been imposed by a charging provision of the domestic law. If, even after the impact of the principle of consistent interpretation, it has not, the taxpayer cannot be made liable by an argument that, on the facts of the case, a liability is imposed by the Sixth Directive.

90. While HMRC accept these two cases are applicable to VATA, they do not consider they assist the appellant. HMRC's case is that national law excludes any right to recover because (a) the principle of conforming interpretation is, as set out in *Vodafone II* above, very wide and (b) it is clear restrictions can be read into s 26 because the Court of Appeal in *Mobilx* found the right of recovery contained in s 26 VATA implicitly excluded persons who knew or ought to have known that their transactions were connected to fraud. In other words, HMRC's case is that they do

not need to rely on a provision of the Directive against the appellant: UK law is against the appellant.

The analysis in Mobilx

91. The analysis of the Court of Appeal in *Mobilx* was as follows. The CJEU interpreted the Sixth VAT Directive to arrive at the conclusion that the provisions of the 6VD dealing with the right to deduct implicitly did not permit VAT recovery to persons who knew or ought to have known that their transactions were connected to fraud although there was no express provision in the 6VD to that effect. Therefore, reasoned Moses LJ at [45], because VATA transposed the provisions dealing with the right to deduct, it follows that national law also transposed the implicit restriction on the right to deduct by such persons. It did not require any legislation to impose that implicit restriction: [47]. This led to the conclusion at [49]:

> It is the obligation of domestic courts to interpret [VATA] in the light of the wording and purpose of the [6VD] as understood by the ECJ…..In relation to the right to deduct input tax, Community law and domestic law are one and the same.

92. HMRC say that the same applies here. Article 41 has been transposed into national law as s 13(3). Properly understood, as explained in *Facet*, there is no right to deduct the VAT charge incurred under Art 41 and therefore that must be true under national law as 'in relation to the right to deduct input tax, Community law and domestic law are one and the same.'

93. The appellant's response is two-fold. Firstly, it says that the analysis in *Mobilx* only applies where there is actual or constructive knowledge of participation in fraud. However, I reject that. It is clear that the analysis adopted by the Court of Appeal in *Mobilx* was not fraud-specific. As explained above, the analysis (set out at [45]) was based on the fact that the UK had transposed the Directive and therefore had transposed its implicit exceptions. Moreover, in the summary given at [49], the Court of Appeal cited cases which were nothing to do with fraud and Moses LJ said:

> '…the application of the *Marleasing* principle may result in the imposition of a civil liability where such a liability would not otherwise have been imposed under domestic law.'

While it is true fraud is mentioned in the analysis, that is because the case was one of participation in fraud: but the analysis of why the UK did not need to enact *Kittel* did not depend on the fact that *Kittel* was a case about participation in fraud.

Principle of conforming interpretation

94. The appellant's second objection was the UK's (alleged) failure to properly transpose article 41(set out above at §17). The first paragraph of article 41 (I will refer to it as Art 41(1)) provided that the trader was only liable to VAT under the full back provision to the extent that VAT was not paid in the Third Country. The second paragraph of article 41 (which I will refer to as Art 41(2)) provided that a trader could recover VAT paid under the full back provision to the extent that it could prove it had subsequently paid VAT in the Third Country on the acquisition.

95. The appellant's position was that there did not appear to be any in force provisions in the UK legislation which gave a taxpayer any right to either avoid the payment of fall- back VAT if it had already paid acquisition VAT in the Third Country nor recover fall-back VAT if it subsequently paid acquisition VAT in the Third Country.

96. The equivalent of the right in Art 41(1) to avoid payment of fall-back VAT where acquisition VAT had been paid in the Third Country appeared to be in s 13(4)(a); the right to recover fall-back VAT on subsequent payment of acquisition VAT in the Third Country appeared to be in s 13(5)(c). However, said the appellant, neither of these sections were in force as both depended on regulations being made by HMRC to bring them into force, and, as HMRC conceded, there were no such regulations.

97. Therefore, reasoned the appellant, no restricted interpretation could be given to the right to recover VAT under s 26 because otherwise the UK would have failed to implement the right to recovery under s 41. And many cases have established that the right to recover input tax is a fundamental principle of the 6VD.

98. I do not agree with the appellant on its interpretation of s 26. Firstly, while the right to recover input tax is a fundamental principle of the 6VD and PVD, it is clear from *Facet,* that the 6VD/PVD does not see fall-back VAT as input tax. Under the PVD, the appellant only has a right to recover fall-back VAT to the extent that it has paid acquisition VAT in the Third Country and in no other circumstances. The appellant has not proved that it has paid acquisition VAT in the Third Country, so it has no rights under the PVD on which it can rely.

99. Secondly, even if the appellant was right to say that the UK had not implemented the right to recover under Art 41(1) and (2), it is a well-established principle that a trader can rely on directly effective rights under the Directive. Article 41(1) and (2) appear to me to be sufficiently clear and precise to be directly effective and it could therefore be relied upon. However, as I have just said, the appellant has no directly effective rights because it has not proved that it has paid acquisition VAT in the Third Country.

100. Thirdly, I do not agree that the UK did fail to transpose either Art 41(1) or (2). The appellant relied on the need for secondary legislation as s 13(4) applied '…where it is established, in accordance with regulations made by the Commissioners…..' and s 13(5) commenced with the words 'The Commissioners may by regulations make provision for the purposes of this section….'. However, the principle of conforming interpretation of legislation is broad.

101. It seems to me that, in the absence of such regulations, s 13(4) must be read as if the words 'in accordance with regulations made by the Commissioners for the purposes of this section' either were not there or were, as Ms Barnes suggests, qualified by the word 'any' in front of 'regulations'. *Vodafone II* requires the Tribunal to depart from the strict and literal application of the words which the legislature has elected to use where necessary to comply with Community law obligations. The UK was obliged to enact article 41 in full and therefore s 13(4)

should be read (as it was clearly intended to do) as giving effect to the tail-end of article 41(1). Doing so is clearly not incompatible with the grain of the legislation as Parliament clearly intended to enact article 41; nor does doing so give rise to important practical repercussions which the tribunal could not evaluate.

102. It is less easy to read s 13(5)(c) as compliant with the requirement for national legislation to provide for repayment of the national VAT when it is proved that VAT has been paid in the Third Country. S 13(5)(c) would make no sense in the absence of regulations if the words 'The Commissioners may by regulations make provision for the purposes of this section….' were omitted or if the word 'regulations' was prefaced by the word 'any'. However, *Vodafone II* shows how wide-ranging the obligation of conforming interpretation is: not only must the tribunal depart from the strict and literal application of the words which the legislature has elected to use, it must imply words necessary to comply with Community law obligations and the precise form of those words does not matter. As Parliament clearly did intend to confer the right to recover UK VAT if it was proved acquisition VAT was paid in the Third Country, s 15(5)(c) must be read as conferring that right even in the absence of regulations setting out precise conditions on how to make the reclaim.

103. In conclusion, a trader in the position of the appellant is not liable to pay UK VAT if he can prove he has paid VAT in the Third Country; or, having paid UK VAT, is entitled to recover it as and when he pays the acquisition VAT in the Third Country. That is because this is how s 13 must be read under a conforming interpretation; in any event, those rights are directly effective. In any event, the appellant cannot complain about the inadequate transposition by the UK because the appellant, having not proved it properly accounted for acquisition VAT in the Third Country, has no directly effective rights to recover fall back VAT.

104. There is no need to read s 26 as conferring the right to recover fall-back VAT. In *Facet*, it was found to be implicit that there was no general right to recover fall-back VAT (other than under article 41), and so, applying *Mobilx*, the same restriction applies to s 26. S 26 does not apply to fall-back VAT. Fall-back VAT is not input tax as it arises on what is merely a deemed acquisition. Moreover, to interpret s 26 in such a way would be inconsistent with the Directive as explained in *Facet.*

105. I agree with HMRC for the reasons given by HMRC. The principle of conforming interpretation must be taken to mean that s 26 must be read not only as excluding the right to deduct where the claimant knew or ought to have known its transaction was connected to fraud, but also where the VAT sought to be deducted was chargeable under s 13(3). No legislation is required: it is simply how the existing legislation must be understood.

Conclusion

106. That concludes the preliminary issue against the appellant.

107. I comment that the hearing proceeded on the basis that acquisition VAT had not been paid in the Third Country; the explanation given by Mr Firth at the end of the hearing (see §4) was that no acquisition VAT was due to be paid. His suggestion was

that the VAT law in the Third Country had been complied with by self-cancelling entries made in the appellant's fiscal representative's books. I consider, and both parties appeared to accept, that no fall-back VAT would be due where acquisition VAT was not actually paid but liability had been cancelled by way of set-off. So, it seems to me, that if what Mr Firth said was correct, the appellant can simply defeat the assessments by proving to HMRC that the appropriate self-cancelling entries were made and the Third Country's tax authorities were satisfied no VAT remained due. Instead, it has chosen to litigate over the ability of HMRC to charge fall-back VAT. Having now failed in that challenge, there is nothing to prevent it seeking to demonstrate to HMRC, if it can, that VAT in the Third Country has been properly paid and to avoid liability for the assessments in that way.

This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

BARBARA MOSEDALE
TRIBUNAL JUDGE

RELEASE DATE: 11 FEBRUARY 2019

11 February 2019: Original paragraph 106 set-aside and new paragraph 106 inserted, and keynotes corrected on grounds original paragraph 106 procedurally wrong.