TC03093

Appeal number: TC/2012/07408, TC/2012/04710, TC/2012/07413, TC/2012/07416 & TC/2012/07419

Value Added Tax*: Bingo Clubs; whether door entry promotion costs can properly be set against door entry charges or whether only against the clubs total income including exempt supplies; European Communities law and VATA s.26.*

FIRST-TIER TRIBUNAL
TAX CHAMBER

(1) BUCKINGHAM BINGO LIMITED **Appellants**
(2) HAMBLINS LEISURE SERVICES LIMITED
(3) BUCKINGHAM HUYTON LIMITED
(4) BUCKINGHAM MIDDLETON LIMITED
(5) BUCKINGHAM HUNTS CROSS LIMITED

- and -

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

TRIBUNAL: JUDGE CHRISTOPHER HACKING
JUDGE DAVID DEMACK

Sitting in public at Manchester on 7 October 2013

Ms Valentina Sloane, counsel instructed by KPMG LLP for the Appellants

Mr Richard Mansell for and on behalf of the Respondents

DECISION

1. This appeal concerns a decision of HMRC made on 21 June 2012 and communicated to the appellants by letter of that date by which HMRC attributed input tax in the purchase of certain promotional gifts and related costs to all supplies made by the appellants, some of which were taxable supplies and some of which were exempt.

2. The relevant part of the letter of 21 June 2013 reads as follows:

> "Promotional door gifts
>
> The calculation of input tax restriction for Mainstage bingo included a review of all input tax treated as directly attributable to taxable supplies of bingo (MCB and MSB). The review specifically considered the treatment of input tax incurred relating to promotional door gifts.
>
> I understand that it is the business view that promotional door gifts relate exclusively to door admission fees and the input tax incurred should be recoverable in full; however HMRC maintain the view that such input tax is attributable to all supplies made by Buckingham Bingo and consequently fall to be residual."

(Note: MCB and MSB refer respectively to Mechanised Cash Bingo and Main Stage Bingo respectively)

3. As a result of that decision recoverable input tax on promotional goods and related costs such as advertising flyers was calculated in line with the partial exemption recovery rate for the VAT periods covering 1 August 2004 to 31 March 2009

Bingo and the appellants clubs

4. Bingo is a popular activity. The game probably needs little in the way of introduction or explanation. Suffice it to say that it is a game in which players mark off numbers on cards as the numbers are drawn randomly by a caller, the winner being the first person to mark off all their numbers. Charges for playing bingo are VAT exempt.

5. Bingo is played in a number of environments but probably the most popular is the Bingo Club. These are members-only clubs which will feature a main hall in which the game is played. Frequently too their will be a foyer area before entry to the bingo hall itself. Such areas will often provide refreshments and accommodation for their consumption. The appellants' premises offered customers the opportunity to use a licensed bar and to order food and alcoholic beverages including light refreshments

to be taken at tables and chairs provided for the purpose. There were also vending machines, toilet facilities and an ATM machine within the foyer area.

6. It was explained by Ms Sloane for the appellants that the foyer areas were used socially as meeting places where friends could get together for a chat and some refreshment in a pleasant setting without necessarily being obliged to play bingo, something which would then involve paying a further fee for entry into the main hall.

7. Membership of the appellants' clubs was stated to be free (although it is noted that the club rules do suggest that a fee may be payable). A copy of the Buckingham Bingo Club rules was included in the appeal bundles. Entry into the foyer area was subject to verification of membership and a modest charge (understood to be less than £1).

8. Having become a member and paid the entry charge members then had a choice: they could either pay an additional charge to play bingo or they could make use of such of the facilities in the foyer area as they might wish or they could do both. There was no obligation on a member to participate in the bingo games in the main hall. Many members simply used the foyer facilities as a convenient place to meet and socialise.

9. It is the appellants' case that both activities, that is to say, the attraction of customers into the foyer area and sales to them from the facilities available and, separately, the attraction of customers into the bingo hall to play bingo were important to them and their business. The particular importance of the component of the appellants' income which relates to admission fees into the foyer area can be seen in the analysis of the appellants' management accounts which separately identifies that income and the costs discretely related to that activity. For example the admissions alone into the foyer area, excluding any income from admission to or playing bingo, totalled £99,800 for just one location over the year to 29 March 2009.

The matters at issue between the parties

10. The dispute between the parties is in essence a simple one. Should the costs of a promotion which the appellants say were related to the income derived from admissions to the foyer area be allowed as a taxable input against the income from such admissions or should the costs of the promotion be set against the clubs' general income and as such be considered as residual.

11. The nature of the promotion itself needs to be considered. It was what is termed a "Stamper promotion" of a type which is, we were told, not uncommon. The object of the promotion was to attract members into the club premises by offering gifts to them if they paid the taxable entrance fee on a specific number of occasions. Each time the member paid the entrance fee to the club his or her card would be stamped. Once the requisite number of stamps had been collected the member was entitled to a free gift.

12. This type of promotion is, say the appellants, to be distinguished from other promotions which the club ran including promotions aimed more generally at generating brand awareness such as money-off vouchers or its free gift promotions related more particularly to the bingo games themselves. Some of these promotions were run concurrently with the admission promotions referred to above. It has not been disputed that the appellants have always accepted that VAT on the costs of its promotions designed to increase brand recognition generally or to encourage the playing of bingo constitute part of the appellants overheads and fall to be treated as such.

13. Examples of the appellants' flyers promoting brand awareness and bingo related promotions as well as the Stamper card admission promotion were exhibited in the appeal bundles. The distinctions to be made between these different types of promotion appeared to the tribunal to be self evident.

The legal background

14. The relevant law concerning the approach to be taken in considering this matter includes both European and domestic legislation.

15. It was not in dispute that the conditions relating to the right to deduct which must be satisfied are those which appear in Article 17 of the 6th Directive (77/388/EEC) which provides:

> "1. The right to deduct shall arise at the time when the deductible tax becomes chargeable.
>
> 2. In so far as the goods and services are used for the purposes of his taxable transactions, the taxable person shall be entitled to deduct from the tax which he is liable to pay:
>
> (a) value added tax due or paid in respect of goods or services supplied or to be supplied to him by another taxable person;

16. Subsequently Article 168 of the Principal VAT Directive 2006/112/EC in dealing with the origin and scope of the right of deduction uses slightly different language in referring to, instead of "goods and services **used**…." *(emphasis added)* to "goods or services **carried out**….." *(emphasis added)* The distinction is not considered to change the fundamental conditions for deductibility.

17. The above European provisions find expression in domestic UK law in section 26 of the Value Added Tax Act 1994 and regulation 101 of the Value Added Tax Regulations 1995 which provides that a taxable person shall be entitled to deduct so much of his input tax as "is attributable to taxable supplies"

18. The above provisions have been considered in a number of cases of which *BLP Group plc and Customs and Excise Commissioners Case* C-4/94 [1995] STC, a case heard in the Court of Justice of the European Communities, is generally regarded as

the leading authority and in which the expression "used" was given particular consideration. At paragraph 19 of its judgment the court said that in order "*to give the right of deduction under para 2, the goods or services in question must have* ***a direct and immediate link*** *with the taxable transactions and that the ultimate aim pursued by the taxable person is irrelevant in this respect"(emphasis added)*

19. A useful summary of other authorities was provided by Carnwath LJ in *Mayflower Theatre Trust Ltd v Revenue and Customs Commissioners* [2006] EWCA Civ 116, [2007]STC from which he drew principles which have application to cases similar to the appeal before the tribunal. Those principles were stated in the following terms:

> "(i) input tax is directly attributable to a given output if it has a "direct and immediate" link with that output (referred to as "*the BLP*" test); (ii) that test has been formulated in different ways over the years, for example whether the input is a "cost component" of the output; or whether the input is "essential" to the particular output. Such formulations are the same in substance as the "direct and immediate link" test; (iii) the application of the BLP test is a matter of objective analysis as to how particular inputs are used and is not dependant upon establishing what is the ultimate aim pursued by the taxable person. It requires more than mere commercial links between transactions, or a "but for" approach; (iv) the test is not one of identifying what is the transaction with which the input has the most direct and immediate link, but whether there is a sufficient direct and immediate link with a taxable economic activity; and (v) the test is one of mixed fact and law, and is therefore amenable to review in the higher courts, albeit the test is fact sensitive."

20. On the facts of *Mayflower Theatre Trust* there was held to be no sufficient link between the costs of a theatre production and the opportunity of selling catering and merchandise to those who attended the theatre.

21. It was at the core of the respondents' case that there was no sufficient direct and immediate link between the promotional costs relating to admissions and the taxable income derived from admissions such as to justify the deduction of the promotional costs. The costs of the promotion would, say the respondents, have the general effect of promoting the club in all of its activities. Consequently, say the respondents, there is a direct and immediate link between the costs of admission and the supply of bingo and all of the supplies made available by the appellant including those related to door admissions.

22. Mr Mansell suggested that the correct approach was that applied in the ECJ decision in *Kretztechnik AG v Finanzamt Linz* (C-465/03) (opinion of the Advocate General) which was to look through events which are not the making of supplies (in that case the business gift to the customer which was not a supply for VAT purposes) until a use of the costs in making supplies is reached. It was further proposed by Mr Mansell that the case of *Midland Bank PLC v Commissioners of Customs and Excise* (C-98/98) demonstrated that deductibility excluded costs incurred as a result of making a supply. Such costs were not directly linked to the supply as the taxpayer

cannot know whether or not he will actually give the gift until the customer has reached the required level of supplies.

23. Applying the decision in *Dial-a-Phone Ltd v Customs and Excise Commissioners* (C-4/94) is said by the respondents to teach that the granting of admission to the premises constitutes a "commercial link" between that grant and the full range of the Appellant's activities. It is consequently right to categorise those costs as residual.

24. Ms Sloane argued however that the problem with this last contention in particular is that it effectively ignores the very precise test that there requires to be shown "*a direct and immediate link*" between, in this appeal, the admissions promotional gifts and the exempt supplies. The commercial link between the two cannot in her submission be sensibly described as "direct and immediate" but rather "indirect and subsequent".

The tribunal's consideration of the appeal

25. This was not an appeal in which the essential facts were disputed. The nature of the promotion had been made clear and was correctly described in paras 19 to 26 of the agreed statement of facts at Tab 8 of the agreed bundle. No formal evidence was called by either party. This was an appeal which concerned the application of the relevant legal principles to the agreed facts. The tribunal was required to decide the issue of principle only. No question of quantum was involved.

26. The principles set out in Carnwath LJ's summary are accepted as the proper guide to determination of the matters in issue between the parties. *BLP,* which was explicitly endorsed in *Mayflower Theatre Trust* as the leading authority and must be followed by the tribunal.

27. The Tribunal does not seek to dismiss the potential relevance of *Kretztechnik* but does distinguish it on the facts. In that case there was no taxable supply against which to set the costs of the capital raising exercise as the issue of shares was tax exempt (the raising of capital was not an activity taxable within the 6th Directive). It was necessary to look further for an economic activity of the taxable person against which the relevant costs could be set.

28. In this appeal it is suggested by the respondents that as the making of promotional gifts is an exempt supply it is necessary, following *Kretztechnik*, to look more generally at the broad based activities of the appellant some of which are exempt and to consider those costs as residual.

29. It is not contended by the appellants, however, that the relevant supply against which the promotional costs should be set is the supply of the promotional gifts themselves. Such gifts do not bear VAT. The relevant supply is the taxable admission charge with which, the appellants say, the promotional costs have a direct and

immediate link. Both as a commercial matter and based on the evidence of the management accounts that link is, in the finding of the tribunal, well established.

30. Objection is also taken by Mr Mansell to the timing of the supply of the promotional gifts. The distinction is drawn in *Midland Bank plc v Customs and Excise Commissioners* [2000] STC 501 (C-98/98) between costs which are and costs which are not, a component of the taxable supply. Mr Mansell contends that in the present case the appellants will not know whether or not they will be giving away a business gift until the requisite level of attendance has been reached.

31. Again, the facts in *Midland Bank* are distinguishable from the present appeal. That case concerned legal and other expenses incurred by the bank in what turned out to be an abortive takeover transaction which led to the bank being sued for negligence. The legal and other expenses were held to relate generally to the activities of the bank and as such were residual. There was no direct and immediate link between the claimed costs and expenses and the costs of the particular claim for damages made against the bank. The costs were not a component of the supply and fell to be residual as part of the general overheads of the bank.

32. In the present appeal the costs of purchasing the promotional gifts and the related costs of flyers are costs which directly relate to the promotion of door entry charges. The link is clear and unequivocal. The timing point raised by Mr Mansell is not one with which the tribunal has any great sympathy. It is true that the precise effect of the promotion in any given individual instance is not necessarily known at the time the Stamper cards are issued but their connection with the taxable door entry charges is clear – indeed obvious. Looking at any one instance as Mr Mansell invites the tribunal to do and surmising as to its likely future effect seems to the tribunal to be an otiose activity unrelated to the principles identified in *Mayflower Theatre Trust.*

33. Reference has also been made by the respondents in their Statement of Case to *Dial-a Phone Limited v Customs and Excise Commissioners* [2004] STC 987. In that case telephone sales staff employed by a marketing company sought to persuade customers firstly to enter into "airtime" contracts for mobile telephones and as an additional matter to take out insurance against the loss of or damage to telephone handsets. Customers were told that they would receive 3 months free insurance if they entered into an airtime contract straight away and signed a direct debit mandate. The services of the company acting as an insurance intermediary constituted exempt supplies for VAT purposes.

34. The issue concerned the application of regulation 101 (2) VAT Regulations, namely, whether as the marketing company had contended its services were attributable exclusively to taxable supplies made by it in which case the input tax on the supply of such services was deductible in full against output tax charged on taxable supplies which it made or whether, as proposed by the Commissioners, the supply of such services was attributable to both taxable and exempt supplies and as such was residual within regulation 101 (2) (d).

35. It was held in that case, by Jonathan Parker LJ in the Court of Appeal, that the supplies by the marketing company embraced both taxable (airtime sales) activities and exempt (insurance intermediary) activities and that accordingly those costs became residual as contended for by the Commissioners. Dial-a-Phone had sought to argue that the sales activities related to its insurance intermediary role was separate from its principal sales activity and it was against the income derived from that activity (airtime sales) that its costs could properly be set. The Tribunal held that the appellant engaged in both taxable and exempt supplies and that its costs required to be apportioned accordingly using what is now known as the "standard method" (regulation 101 (2) (d)). The Court of Appeal upheld the tribunal decision.

36. What is interesting is that in the course of this decision, a decision which endorsed and followed the approach in *BLP,* it was held that even though the insurance intermediary services might be made after the taxable supplies there was a sufficient direct and immediate link between those supplies and the marketing costs such as to render those costs residual. This addresses Mr Mansell's timing point above.

37. Mr Mansell suggests that what Dial-a-Phone teaches is that the granting of admission to its premises by the appellants creates a "commercial link" between that grant and the full range of the appellants' activities. The appellants would not and have not denied that there it is a likely consequential effect of the admissions promotion that increased attendance at its bingo sessions may be realised. That however is, in the view of the tribunal, not the proper test when there is a clear link which is both direct and immediate to another part of the appellants' business. The connection of the Stamper card promotion with the more general business of the appellant is, as Ms Sloane contends, indirect and subsequent rather than direct and immediate.

38. A number of other cases were considered by the tribunal including notably that of the *Royal Agricultural College v Customs and Excise Commissioners* [2001] (VTD 17508). In many of these cases the same theme appeared to the tribunal to be pursued by the respondents who contend that the main purpose of the promotion has to be looked at generally. It is clear from the guidance in *Mayflower Theatre Trust* however that purpose or intent is not relevant nor is there any authority for a hierarchy of purpose. Were it so then this would require quite complex enquiries to be made by HMRC as to the history and management arrangements within companies or other entities to determine such purpose or intent. This may be thought to be impractical.

39. To "look through" an intermediate activity, as Mr Mansell suggests is taught by *Kretztechnik,* may have some merit in the particular context of that case but that does not require that HMRC can ignore and look past a perfectly legitimate taxable activity in respect of which directly related costs have been incurred.

40. What is required is the identification of a link to an activity, taxable or not, which is direct and immediate. If that activity is taxable then eligible input tax can be set off against it. If the activity is exempt then such costs cannot be set off. If the

activity is partly taxable and partly exempt then the standard method of apportioning the tax input will be employed.

41. In the matter of this appeal the tribunal is satisfied that the costs of the door promotion were directly and immediately linked to the taxable supply of door entry charges and that accordingly such costs must be applied against those charges in arriving at a proper assessment of the appellants' VAT liability.

42. The appeal is allowed.

43. 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.

CHRISTOPHER HACKING
DAVID DEMACK
TRIBUNAL JUDGES

RELEASE DATE: 2 December 2013