[2017] UKFTT 634 (TC)

# TC06070

**Appeal number: TC/2015/00890**

***Customs duty – classification – optical fibre splitters – whether optical fibre cables – no – choice of alternative classification – principles on which to be determined by Tribunal – held, classification by HMRC the appropriate one – appeal dismissed***

**FIRST-TIER TRIBUNAL**
**TAX CHAMBER**

**NETWORK CRITICAL SOLUTIONS LIMITED** **Appellant**

**- and -**

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

**TRIBUNAL: JUDGE JOHN CLARK**

**Sitting in public at Reading Employment Tribunal on 30 June 2016**

**David Pinder, Director, for the Appellant**

**Ewan West of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents**

DECISION

1. The Appellant ("NCS") appeals against a decision of the Respondents ("HMRC"), upheld on review, to classify imported fibre optic cable splitters under commodity code 9013809000, and to issue a C18 Post Clearance Demand Note in respect of Customs Duty and VAT.

## The background facts

2. The evidence consisted of a bundle of documents. This included witness statement given by Alistair Hartrup, the Managing Director of NCS, and David Harris of HMRC's Tariff Classification Service ("TCS"). Both witnesses also gave oral evidence. From the evidence, I find the following background facts.

3. On 17 June 2014 Mr Howard, an officer in HMRC's Local Compliance International Trade & Excise division visited the NCS premises. In the course of the visit he requested technical specifications of the splitters imported under a particular entry. On the same date Mr Pinder of NCS sent an email to Mr Howard attaching a copy of the datasheet for the splitters imported from Opterna.

4. On 18 August 2014 Mr Howard wrote to Mr Pinder indicating that TCS had provided a ruling in respect of both splitters. (These were described as "MM 1x2 Splitter 50/50" and "MM 1x2 Splitter 70/30".) They had been classified to commodity code 9013809000, so were subject to a 4.7 per cent rate of duty. As a result, a debt had been incurred under Article 201 of Council Regulation (EEC) 2913/92. A C18 Post Clearance Demand Note would be issued for a total of £1,659.16 (£1,386.35 duty and £272.81 VAT). If NCS had any further evidence or arguments that could change this decision, these should be sent to HMRC within 30 days.

5. On 22 August 2014 Mr Pinder sent Mr Howard an email attaching a letter dated 21 August 2014 responding to Mr Howard's letter. NCS disagreed with the TCS decision. The code that was used for these imports was 8544700000, for optical fibre cables. Mr Pinder stated that the manufacturer of these products selected the latter code, which NCS considered to be the appropriate one. He asked that HMRC's decision should be reversed.

6. On 16 September 2014 Mr Howard replied to NCS with a summary of the TCS decision. This included the following view:

> "The TCS contend that the splitters are not merely optical fibre cables, although they consist of cables that carry light; that is not their sole function."

The TCS further contended that the splitters met the terms of Chapter 90, and were therefore excluded from chapter heading 8544 by way of Section Note 1(m) to Section XVI. Reference was also made to three Binding Tariff Information ("BTI") rulings made by other EU Member States.

7. In a letter dated 17 September 2014, Mr Howard stated that the arguments which NCS had put forward in its letter dated 21 August 2014 had not changed his view. He indicated that a C18 Post Clearance Demand would be issued. He indicated that NCS could either request a review of the decision by another HMRC officer not previously involved in making the decision, or could appeal direct to the Tribunal. On the same date the C18 demand was issued in the amounts set out above.

8. On 15 October 2014, NCS requested a review of HMRC's decision, providing detailed reasons and information in support of the original classification code 8544700000 and commenting on the three BTI rulings referred to by HMRC. On 27 November 2014, the Review Officer asked for additional information, and pending the receipt of this, on 1 December 2014, he asked for the deadline for his written response to be extended. On 3 December 2014, NCS provided the additional information. Subsequently, the Review Officer requested a further extension, and further information.

9. On 9 January 2015, the Review Officer wrote to NCS with the results of his review. His conclusion was that he should uphold the original decision to classify the splitters under commodity code 9013809000 and to issue the C18 demand.

10. On 4 February 2015, NCS lodged a Notice of Appeal with HM Courts & Tribunals Service ("HMCTS"). In that Notice, the amount of tax was stated to be £5,199.57.

**Arguments for NCS**

11. Mr Pinder argued that the appeal raised two issues. The first was whether the classification used by HMRC was or was not correct. The second was when it was appropriate to apply such a classification.

12. Mr Pinder made detailed submissions on the facts. I deal with these later, together with those made by Mr West on behalf of HMRC. Mr Pinder described Mr Hartrup's witness statement as a synopsis of the arguments put by NCS.

13. In relation to the second issue, Mr Pinder submitted that it was totally unreasonable for the classification decision to have been applied retrospectively.

**Arguments for HMRC**

14. Mr West emphasised that there was no suggestion in any way that NCS had done anything wrong. The law required HMRC to apply Council Regulation (2913/92/EEC) establishing the Community Customs Code ("the Code"). The way in which this worked was that HMRC had to look at a particular item and decide on its classification. The protective mechanism for the person importing the item was the appeal procedure. HMRC did not have any discretion to decide that they could waive a classification.

15. Mr West did not think that there was any dispute between the parties as to the legal principles. The question was one for the Tribunal.

16. On the question of retrospectivity, HMRC had to apply the Code as a matter of EU law. This was not a matter of discretion.

17. Mr West made submissions as to the facts concerning the classification and the application of the relevant headings. I consider these below.

**Consideration and conclusions**

18. In his detailed Skeleton Argument, Mr West set out a summarised account of the legal framework relevant to the classification of items under the Code. I have reviewed this in the light of the more detailed information set out in the Authorities Bundle and by reference to the various CJEU judgments referred to and included in that bundle. As the parties did not differ in their views as to the operation of this framework, I do not think it necessary to describe it in any detail in this decision.

19. In his witness statement Mr Hartrup explained that NCS manufactures a range of network access equipment that allows its customers to monitor the performance and manage the security of their data networks. Typical customers are banks, telecommunications companies and major corporations, both in the UK and internationally.

20. He stated that the network equipment that NCS manufactures falls under the Tariff code 85, Electrical machinery and equipment, sub-heading 17 – other apparatus for the transmission or reception of voice, images or other data.

21. NCS had classified the items in question in the appeal under Tariff code 85, sub-heading 44 700000 Optical fibre cables. It had been the belief of NCS that this description was a clear indication of the correct code. NCS had also been aware that the major exporters of these products from China and India into Europe all used this code.

22. In cross-examination by Mr West, Mr Hartrup accepted that NCS had not been able to produce any evidence as to the views taken by these exporters. Mr Pinder, in his closing submissions, referred to the decision taken by NCS not to supply evidence relating to the companies in question. I note from the correspondence between NCS and HMCTS that reference was made to "NDAs" (non-disclosure agreements). I appreciate that commercial considerations were a factor in the decision taken by NCS. The result of that decision is that I can take no account of the exporters' views as to the classification which they consider to be applicable.

23. Subject to this, I accept the parts of Mr Hartrup's witness statement to which I have referred above.

24. The question in classification cases is whether HMRC have applied the relevant principles under the Code in a manner consistent with its application by all other Member States. Although I accept Mr Hartrup's evidence as to the belief of NCS that

it had applied the correct code, I am not persuaded that the state of mind of the importer is a factor relevant in deciding the appropriate classification. Mr West referred to the judgment of the CJEU in *Case C-396-02 DFDS BV v Inspecteur der Belastingdienst – Douanedistrict Rotterdam* [2004] ECR I-8439, which held that the decisive criterion for the classification of goods for customs purposes is in general to be found in their objective characteristics and properties. This appears to me to exclude the possibility of taking into account the state of mind of the party importing the goods. Further, the judgment of the CJEU in Case C-467-03 *Ikegami Electronics (Europe) GmbH v Oberfinanzdirektion Nürnberg* [2005] ECR I-8151 shows that the intended use of a product may constitute an objective criterion in relation to tariff classification if it is inherent in the product, and such inherent character must be capable of being assessed on the basis of the objective characteristics and properties of the product. Again, the question of the state of mind of the party involved is not part of that objective evaluation.

25. In HMRC's submission, there are three potentially applicable codes in relation to the classification of the splitters. The headings in question are 8544, 9001 and 9013.

26. Heading 8544 is in the following terms:

> "8544 Insulated (including enamelled or anodised) wire, cable (including coaxial cable) and other insulated electric conductors, whether or not fitted with connectors; optical fibre cables, made up of individually sheathed fibres, whether or not assembled with electric conductors or fitted with connectors"

27. The sub-heading which NCS contends to be appropriate is 8544 70 00, "Optical fibre cables".

28. Heading 9001 is as follows:

> "9001 Optical fibres and optical fibre bundles; optical fibre cables other than those of heading 8544; sheets and plates of polarising material; lenses (including contact lenses), prisms, mirrors and other optical elements, of any material, unmounted, other than such elements of glass not optically worked"

29. The relevant sub-heading is 9001 10:

> "Optical fibres, optical fibre bundles and cables"

30. Heading 9013 refers to:

> "Liquid crystal devices not constituting articles provided for more specifically in other headings; lasers, other than laser diodes; other optical appliances and instruments, not specified or included elsewhere in this chapter"

31. Within this, 9013 80 lists:

> "Other devices, appliances and instruments";

then sub-heading 9013 80 90 is:

"Other"

32. The submission for NCS is that the classification under sub-heading 8544 700000 adopted by them was correct.

*Mr Hartrup's oral evidence*

33. In his oral evidence, Mr Hartrup described the splitter as a fused coupler. Its purpose was to give a method of access, for the benefit of the large corporations and other similar entities using it. The product was one in which two fibre optic cables were fused. Inside the product the two glass cables were twisted, and heat applied to fuse them. The extent of the process (known as the "Fused Biconical Taper process") determined what proportion of the signal would be taken by the second cable, ie 30 per cent in one version of the splitters. The mechanical process involved in the use of the product was a degradation to light. He likened the effect to that of putting a "t-piece" into a hosepipe. The purpose was to enable the user to monitor without interference.

34. All the fibres were within a sheath mandrel. Some degradation of the signal was caused by taking the monitoring signal. The extent depended on how far away the monitoring device was. The customer would choose what level of signal was required.

35. If one could take the metal sleeving off the product, it would be possible to see one cable fused together with another. One fibre entered the product from one side. In layman's terms the device was cut in two. The product could work in both ways, ie to split or combine signals. No power was involved; the process was completely "dumb". Mr Hartrup described the product's function as "passive".

36. In the course of his oral evidence, Mr Hartrup showed two opened examples of sample component boxes in which the splitters formed part of a completed combined unit. One sample was in the form in which the unit would be supplied to customers, and the other was partly disassembled. His description in giving evidence was by reference to the units which were placed before me.

37. He further explained that the form of the cable inside the splitters could not actually be seen, but was as shown in the diagrams provided as part of the evidence. It was similar to a twisted rope.

38. He did not consider that the splitter was anything more than a cable. From the physical point of view, it became two. He referred to his hosepipe analogy. It was a fibre optic cable split in two and sheathed.

39. He accepted that it would have been possible for NCS to ask for a BTI ruling. However, it had been firmly of the view that its chosen classification was correct.

40. The three BTIs referred to by HMRC related to "wave division multiplexers" ("WDMs"), which were completely different products. Mr Hartrup explained that he

did not fully understand WDMs; they were not used in the industry in which NCS was involved. It had felt that heading 844 was very much the appropriate one.

41. In advance of the hearing, HMRC had referred to a further BTI issued by the relevant German authority. This had been registered in June 2015, twelve months after the HMRC assurance visit. NCS had since examined this BTI, which again was for a different product. That product was described as a "Signal Path Power Combiner". Its view was that this product had a different function, performance and application.

42. In his witness statement, Mr Hartrup expressed the view that the review had been inadequate. He was convinced that the HMRC Review Officer had not even considered the points raised in the request for review made by Mr Pinder on behalf of NCS. NCS had referred to the three BTIs, which all related to WDMs, and had argued on technical grounds that these were for completely different products.

*Mr Harris's oral evidence*

43. Mr Harris stated that he was a Higher Officer of HMRC employed at TCS. He explained that having had the benefit of seeing the products and hearing Mr Hartrup's explanation, this had not changed his view. He maintained his decision. He believed that the explanation confirmed his view that the product split the signal and took the separate parts to different destinations.

44. In cross-examination, Mr Harris explained the TCS view that heading 8544 related purely to optical fibre cable. Splitting was seen as a different function covered by a different heading. It was his interpretation that in order to fall within heading 8544, the fibre had to be individually sheathed.

45. He had considered it appropriate to refer to the 2015 BTI decision taken by the German authorities. Although this had been reached after the date of the import by NCS, he had no reason to believe that the German authorities would have reached a different decision had they been considering the question at an earlier date. They had arrived at their view that heading 8544 was not appropriate because of the splitting and combining function.

46. He considered it appropriate to consider a heading other than 8544 because of the fusing process, which led him to the view that the product was not an optical fibre cable. Even before the German BTI, he had arrived at the view that the splitters were excluded from heading 8544. The German BTI had been a useful clarification.

47. He appreciated that the original three BTIs referred to in the correspondence related to different technologies, but in the light of their function, they provided more support.

48. He emphasised that the classification of the product had been arrived at by working out its objective characteristics. It had been the TCS view that all the BTIs to various degrees supported its position. The product carried out the function of

splitting. That function, as viewed by TCS, moved the product into Chapter 90. The TCS interpretation of the Tariff was that splitting was a function that took the product out of heading 8544.

*My conclusions*

49. The task for the Tribunal was described by Henderson J in a case not referred to by Mr West, namely *HMRC v Flir Systems AB* [2009] EWHC 82 (Ch). (This was referred to in an earlier Tribunal decision with which I was involved, *Furukawa Electric Europe Limited v Revenue and Customs Commissioners* [2012] UKFTT 129 (TC), TC01824.) In *Flir*, HMRC had submitted to Henderson J that the Tribunal had erred in adopting a layman's, non-technical approach to the interpretation of language that was essentially technical and scientific in nature. At [28] Henderson J indicated that he found himself unable to accept this submission, and continued—

> "I was shown no authority which supports the proposition that the language of the relevant headings should be interpreted with scientific precision, and it seems to me inherently improbable that such an approach should have been intended for a tariff code which has to be applied by businessmen and customs authorities worldwide. The appropriate linguistic register is in my view that of the intelligent businessman, not that of a GCSE physics student."

50. The effect of the appeal process is to place on the Tribunal the task of arriving at the classification. As Henderson J indicated, the basis on which the Tribunal is to approach that task is to carry out the evaluation of the relevant factors by reference to the view of an intelligent businessman.

51. The argument for NCS is that each of these two products constitutes an optical fibre cable falling within heading 8544. I have already set out the wording of this heading. The part of it which deals with optical fibre cables is specific:

> "optical fibre cables, made up of individually sheathed fibres, whether or not assembled with electric conductors or fitted with connectors"

The sub-heading makes no reference to insulation, but the reason for this is that the items covered by the sub-heading are limited by the terms of the heading. For a cable to come within heading 8544, my reading is that it must consist of individually sheathed fibres.

52. The process of manufacture of the splitters was explained to me in Mr Hartrup's oral evidence. I was also provided with a diagram showing the Fused Biconical Taper Process, as it would not be possible to see the fused element even if the splitter could be fully disassembled. As I understand that evidence and that diagram, the individual fibres are subjected to heat and brought into close proximity to each other in a manner which controls the extent to which the optical signal will be split by the product. There is no evidence to suggest that the fibres are individually sheathed, and in any event it is clear that in order for the splitters to function, the fibres cannot be sheathed in the "coupling region". There was no evidence to suggest that there was any individual sheathing within the splitters.

53. In my view, the absence of individual sheathing takes the splitters out of heading 8544. As a further factor, it is also necessary to consider the function of the splitters. A cable or fibre carries the signal and has no additional function. In contrast, even if the splitters could be regarded as within heading 8544, their function is both to carry the signal and to divide it. The latter is clearly an additional function, even though, as Mr Hartrup stated, the process by which the splitters carry this out is passive in nature. The fusion process which I have described enables the splitters to separate out a defined portion of the signal for monitoring purposes.

54. I have looked in detail at the three BTIs referred to by HMRC in correspondence, as well as the 2015 German BTI. I do not propose to set out here the technical specifications of the products in question in those BTIs, as I do not consider that this would be appropriate or helpful in the present context. The technologies differ from that used in the splitters under consideration in this appeal, but the common factor in all these cases is the carrying out of a division or combination of an optical fibre signal. That factor in itself is sufficient to take the splitters out of heading 8544 even disregarding the absence of individual sheathing of the constituent optical fibre cable parts of the splitters.

55. For these reasons, I do not consider it appropriate for the splitters to be classified under heading 8544 as contended by NCS. It follows that the sub-heading used by NCS, 85444700000, was not the correct one for the classification and import of the splitters.

56. As a result, it is necessary to consider which other headings may be appropriate.

57. Heading 9001 deals with—

> "Optical fibres and optical fibre bundles; optical fibre cables other than those of heading 8544 . . ."

58. The difficulty with this heading is that the same issue of function arises as I have already considered in relation to heading 8544. I accept that there is no requirement under heading 9001 for the fibres to be individually sheathed. However, the splitters perform a function additional to that of optical fibre cables, and in principle that is sufficient to take them outside this heading if a more suitable heading can be found.

59. The remaining heading for consideration is 9013, which I have set out above. Is it appropriate to classify the splitters under this "optical instruments" heading? Objective evaluation of their function indicates that this is to split the light forming the signal, the purpose in the case of the equipment supplied by NCS being to enable its customers to monitor the signal for commercial or other purposes. This is an optical function.

60. Although at first sight it may not appear to be the most obvious heading to consider in relation to the splitters, I have come to the conclusion that heading 9013 is the appropriate one for the classification of these products. The appropriate sub-heading is 90138090, "Other", as set out in HMRC's decision dated 18 August 2014

and as confirmed by HMRC's review decision dated 9 January 2015. I note that, as Mr Harris stated in evidence, German Customs support HMRC's view that the splitters are optical appliances within heading 9013. I also note the conclusion of German Customs in their 2015 BTI reference DE970/15-1 that the appliance under consideration in that BTI falls within code 9013809090. This reinforces my conclusion as to the appropriate classification of the splitters. (I acknowledge the submission by NCS that this BTI post-dates the importation, but I accept Mr Harris's conclusion that this merely confirms the view which would have been taken had the BTI been under consideration at an earlier point.)

61. Accordingly, I have to dismiss NCS's appeal. In doing so, I must emphasise a point which Mr West made in argument. There is no suggestion on HMRC's part that NCS was in any way acting improperly in choosing to apply commodity code 85444700000. HMRC are under a duty to ensure that the correct code is applied, as this is a question of relevance throughout the EU.

62. NCS also argued that the practical effect of the C18 Post Clearance Demand was to apply the classification retrospectively. Mr West pointed out that in legal terms this might not amount to retrospectivity, although agreed that in practical terms it did so. Questions of retrospectivity and of the conduct of HMRC fall outside the jurisdiction of the First-tier Tribunal, and therefore I can do no more than add my comments. Despite the commercial difficulties which I accept may ensue after importation under what proves to be an incorrect classification, I accept Mr West's argument that this is a necessary consequence of the legislative scheme for the classification of goods under the present regime.

## Outcome of the appeal

63. In the light of my decision on the classification of the splitters, NCS's appeal is dismissed.

## Right to apply for permission to appeal

64. 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.

**JOHN CLARK**
**TRIBUNAL JUDGE**

**RELEASE DATE: 31 AUGUST 2016**