Neutral Citation Number: [2018] EWCA Civ 1515

Case No: A3/2017/0184

IN THE COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)
[2016] UKUT 294 (TCC)

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 29/06/2018

Before :

LORD JUSTICE HENDERSON
LADY JUSTICE ASPLIN
and
DAME ELIZABETH GLOSTER, DBE

- -

Between :

ZIPVIT LIMITED	**Appellant**
- and -	
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS	**Respondents**

- -

Mr Roger Thomas QC (instructed by **Mishcon de Reya LLP**) for the **Appellant**
Mr Sam Grodzinski QC and Ms Eleni Mitrophanous (instructed by the **General Counsel and Solicitor to HMRC**) for the **Respondents**

Hearing dates: 28 and 29 November 2017
Further written submissions: 27 April, 16 May and 17 May 2018

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Approved Judgment

Lord Justice Henderson:

Introduction

1. This appeal raises some important questions of principle in the law of value added tax ("VAT"). They arise when supplies of goods or services, which were wrongly assumed by the parties to the relevant transactions and by the Commissioners for Her Majesty's Revenue and Customs ("HMRC") to be exempt from VAT at the time of supply, are later discovered to have been subject to the standard rate of tax when they were made, following a decision to that effect by the Court of Justice of the European Union ("the CJEU"). Where the recipient of those goods or services was itself a registered trader which made taxable supplies on which it accounted for output tax, the basic question is whether, once the true position has become known, the recipient is in principle entitled to recover as an input tax credit the tax element of the consideration which it paid for the original supplies. If so, does it make any difference if the supplier has failed to pay the tax which should have been paid on the original supplies, and if the recipient is in consequence unable to produce a tax invoice from the supplier showing the amount of the input tax which it seeks to recover?

2. The matter comes before us on an appeal from Proudman J, sitting alone as a judge of the Tax and Chancery Chamber of the Upper Tribunal, in a lead case which was selected as suitable for obtaining a decision in principle from the Tax Chamber of the First-tier Tribunal ("the FTT", Judge Mosedale, who also sat alone) on a preliminary issue. The preliminary issue was formulated as follows:

> "Whether a taxable person, who has received supplies of services which were at the material time treated by Royal Mail [*the original supplier*] as exempt under Value Added Tax Act 1994, but which were properly chargeable to VAT under the Sixth VAT Directive or Principal VAT Directive, is entitled to an input tax credit in respect of those supplies."

3. The appellant is a company called Zipvit Limited ("Zipvit"), which carries on the business of supplying vitamins and minerals by mail order. Zipvit is a registered trader for VAT purposes, and its business has at all material times been fully taxable. All of the supplies which it makes to its customers are standard-rated.

4. On 15 September 2009, Zipvit made a claim under regulation 29 of the VAT Regulations 1995 for input tax which it claimed it had incurred in the period from 31 March 2006 to 30 June 2009 in the sum of £383,599. It made a further claim on 8 April 2010 for £31,164 in respect of the next two accounting periods. HMRC rejected the claims on 7 May 2010, and upheld this decision in a review letter dated 2 July 2010. Zipvit then appealed from the review decision to the FTT, which heard its appeal in May 2014.

5. Zipvit used the services of Royal Mail to despatch its mail orders and also to distribute advertisements. The Royal Mail services used by Zipvit included

Packetpost, Parcelforce and Mailmedia, but only the Mailmedia supplies were taken as specimen supplies for the purpose of the FTT hearing, because it was common ground that they were all taxable transactions under EU law, and none of them was exempt.

6. It is common ground that, at the time when Royal Mail supplied the Mailmedia services, those supplies were considered to be exempt from VAT both by Royal Mail and by HMRC. This view was also shared by Zipvit, as the FTT expressly found in paragraph 13 of its decision in principle released on 3 July 2014 ("the FTT Decision").

7. This consensus is not surprising, given that the domestic VAT legislation then in force provided exemptions for:

> "1. The conveyance of postal packets by the Post Office company.
>
> 2. The supply by the Post Office company of any services in connection with the conveyance of postal packets."

See Group 3 of Schedule 9 to the Value Added Tax Act 1994 ("VATA 1994"). There is no dispute that Royal Mail was "the Post Office company" within the meaning of those provisions.

8. The exemptions which I have quoted gave effect to Article 132 of the Principal VAT Directive 2006/112/EC ("the Principal Directive"), and its precursor in the Sixth VAT Directive, which provided that:

> "1. Member States shall exempt the following transactions:
>
> (a) the supply by the public postal services of services other than passenger transport and telecommunications services, and the supply of goods incidental thereto."

9. This common understanding of the law was, however, shown to be wrong by the decision of the CJEU in 2009 in Case C-357/07, R (on the application of TNT Post UK Limited) v Revenue and Customs Commissioners [2009] ECR I-3025, [2009] STC 1438, which held (in short) that postal services provided by the universal postal provider (i.e. Royal Mail in the UK) were not exempt if they were "individually negotiated": see the judgment of the Court at paragraphs 41 to 49. The principle of fiscal neutrality required that the scope of the exemption should be confined to services provided by the universal service provider in its capacity as such, and did not include "specific services dissociable from the service of public interest, including services which meet special needs of economic operators" (see paragraph 46).

10. As the FTT explained at [6] of the FTT Decision, Zipvit's claim to recover input tax was made on the basis that Royal Mail had wrongly treated supplies it made to Zipvit as exempt when they were in law standard rated. There was an outstanding dispute between the parties about the extent of the CJEU's ruling in the TNT case, and precisely which services supplied by Royal Mail to Zipvit were "individually

negotiated" and therefore not exempt. The FTT had not been asked to rule on that dispute, as the tax status of the various supplies made by Royal Mail was already before the High Court in different proceedings. It was agreed, however, that the Mailmedia supplies were all standard rated as a matter of EU law. Hence the decision to concentrate on those supplies for the purpose of the FTT hearing, leaving issues of quantum for subsequent determination if they could not be agreed.

11. It is convenient to note at this point that Judge Mosedale went on to hold that the Mailmedia supplies to Zipvit were also to be treated as standard rated under domestic UK law, on two alternative grounds. First, as a matter of conforming interpretation under the Marleasing principle, the exemption in Group 3 of Schedule 9 to VATA 1994 should be construed in accordance with the CJEU's judgment in TNT. Secondly, even if such a conforming construction were not possible, it would be open to Zipvit to invoke the direct effect of the postal exemption against HMRC, who were refusing Zipvit's claim for input tax. No appeal was brought by HMRC against either of those conclusions, so the case has proceeded before the Upper Tribunal and before us on the footing that the Mailmedia supplies to Zipvit were standard rated under both EU and UK domestic law.

12. The basic entitlement of a taxable person to deduct input tax from the output tax for which he is liable to account to HMRC is conferred by Articles 167 and 168 of the Principal Directive, which provide as follows:

> "*Article 167*
>
> A right of deduction shall arise at the time the deductible tax becomes chargeable.
>
> *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 taxable person;
>
> …"

13. The FTT dismissed Zipvit's appeal, holding that the words "the VAT due or paid" in Article 168(a) referred to the payment of the relevant VAT by Royal Mail to HMRC, and that this condition had not been satisfied, for reasons given in the FTT Decision at [134] to [148]. This conclusion, if correct, was alone enough to determine the appeal in HMRC's favour, but the FTT went on to consider the absence of a VAT invoice from Royal Mail to Zipvit, finding that HMRC were entitled to exercise their discretion under regulation 29 of the VAT Regulations 1995 to reject the alternative evidence provided by Zipvit of its having received taxable supplies for the purposes

of its trade. The FTT accepted that HMRC's approach to the exercise of their discretion had been flawed, but decided that, even if they were to remake the decision, their conclusion would inevitably have been the same, essentially because Zipvit "never suffered the economic burden of VAT on the supply to it of Mailmedia services by Royal Mail": see the FTT Decision at [198].

14. The neutral citation of the FTT Decision is [2014] UKFTT 649 (TC), and it is reported at [2014] SFTD 1309.

15. Zipvit's appeal to the Upper Tribunal was heard by Proudman J, over three days in March 2016. By her decision ("the UT Decision") released on 27 June 2016, she dismissed the appeal. On the "due or paid" issue, it was common ground, and Proudman J agreed, that the FTT had been wrong to hold that the relevant question was whether the VAT had been paid by, or was due from, the supplier (Royal Mail) to HMRC. Neither side had advanced that contention to the FTT, and Judge Mosedale had taken an independent line of her own in so holding, as she frankly recognised in the FTT Decision at [108] to [110]. The correct question was, rather, whether the relevant tax had been paid by, or was due from, the customer who sought to deduct it as input tax to the supplier, i.e. by or from Zipvit to Royal Mail. On that footing, Proudman J appears to have accepted the submission advanced by Mr Roger Thomas QC on behalf of Zipvit that the sums paid by Zipvit to Royal Mail had to be treated as inclusive of VAT at the standard rate by virtue of section 19(2) of VATA 1994, which provides that:

> "If the supply is for a consideration in money its value shall be taken to be such amount as, with the addition of the VAT chargeable, is equal to the consideration."

16. I say that Proudman J "appears" to have accepted this submission because, with the greatest respect, I confess that I do not find all of her reasoning in this part of the UT Decision entirely easy to follow. Nevertheless, I think it is reasonably clear, in particular from [43], [54] and [56], that this was indeed her view, although she described the issue as "academic only" in the light of her conclusion on the VAT invoice question: see the concluding sentence of [56]. In relation to the latter question, Proudman J took much the same approach as the FTT, agreeing with Judge Mosedale that HMRC had failed to consider all the matters which were relevant to the exercise of their discretion under regulation 29, but that even if the reviewing officer had taken the correct matters into account, her conclusion would necessarily have been the same: see the UT Decision at [57] to [69]. Accordingly, Zipvit's appeal was dismissed.

17. Zipvit now appeals to this court, with permission granted by the Upper Tribunal on 15 December 2016. In granting permission, Proudman J observed that the case raises important points of principle, that this is a lead case with a large number of other cases standing behind it, and that the total amount of tax at stake is thought to be of the order of £1 billion.

18. The case has been argued before us by the same counsel who appeared before both Tribunals, namely Mr Thomas QC for Zipvit and Mr Sam Grodzinski QC leading Ms

Eleni Mitrophanous for HMRC. I am grateful to them for their clear and helpful submissions, both written and oral.

19. Although we heard the appeal over two days at the end of November 2017, our judgment has regrettably been delayed for a number of months. There are two main reasons for this. The first is that, at the conclusion of the hearing, we asked HMRC to make further enquiries of Royal Mail's solicitors about the contractual documentation which governed the Mailmedia supplies to Zipvit, including certain standard terms and conditions to which reference was made in some of the documents, but which had apparently not been obtained before the FTT hearing. These enquiries, and ensuing correspondence between the parties' solicitors, continued until March 2018, when we made it clear that we were not prepared to receive any further material, and that we would in due course rule in our judgment on the admissibility of the material which had been obtained.

20. The second reason is that there have been some significant recent developments in the European case law, upon which it soon became apparent that it would be helpful for us to receive written submissions from the parties. In one of those cases, Case C-533/16, Volkswagen AG v Finančné riaditeľstvo Slovenskej republiky, EU:C:2017:823, the opinion of Advocate General Campos Sánchez-Bordona had been delivered on 26 October 2017, about a month before the hearing in this court, so the parties had been able to make submissions on it, but the judgment of the CJEU was pending, and in the event was delivered on 21 March 2018. The other case was one to which no reference had been made at the hearing, no doubt because it was not expected by either side to be of particular significance and no Advocate General's opinion had yet been delivered. On 30 November 2017, however, Advocate General Kokott delivered her opinion in Case C-8/17, Biosafe-Indústria de Reciclagens SA v Flexipiso-Pavimentos SA, EU:C:2017:927. Her opinion was at that stage available only in the original French, but it was apparent that it might be material to some of the issues debated before us, and it was duly drawn to our attention by junior counsel for HMRC, coupled with an optimistic forecast that the opinion was likely to be published in English within the next two weeks. For reasons which are obscure to us, production of an official English version of Advocate General Kokott's opinion remained outstanding for a period of several months, although it was rapidly translated into virtually every other official language of the EU. In the end, the official English version did not materialise until early April 2018, by when it had also become apparent that the judgments of the Court in both Volkswagen and Biosafe were soon due to be delivered. The judgment in Biosafe, EU:C:2018:249, was in fact delivered on 12 April 2018.

21. In the light of these developments, we directed the parties to agree a timetable for the provision of written submissions dealing with these two cases. This was duly done, and we received written submissions from Zipvit on 27 April 2018, to which HMRC replied on 16 May, with a final response from Zipvit on 17 May.

The facts

22. The basic facts were found as follows by the FTT:

> "9. It is agreed by the parties that Royal Mail treated the supplies of "Mailmedia" to Zipvit as exempt. It did not account

> to HMRC for VAT on the supplies and it did not issue VAT invoices to Zipvit in respect of these supplies.
>
> 10. I was shown the Royal Mail's user guide for Mailmedia services. As it is not in dispute that under *TNT* the Mailmedia service provided by Royal Mail was standard rated under the VAT Directives, little needs to be said about it. In brief, it was a contract by Royal Mail with its customer to mail out identical advertisements to very large numbers of addressees, and include with each mailing a reply paid envelope. The cost of the service depended on quantity, weight and whether the customer pre-sorted the mailings.
>
> 11. There was absolutely nothing in the information provided by Royal Mail about their Mailmedia service which mentioned VAT. A customer wanting the Mailmedia service would complete an online contract application, and Mr Bailey, the principal shareholder and managing director of Zipvit, regularly did so. Similarly, this application did not mention VAT. The Royal Mail's acceptance form also had nothing about VAT in it.
>
> 12. Each time Zipvit contracted for the Mailmedia service, Royal Mail provided Zipvit with an invoice for its services. The invoices show that Royal Mail treated the supply of Mailmedia services as exempt from VAT.
>
> 13. [*Zipvit's*] position is that the invoices did not properly reflect the agreement between the parties. Mr Bailey in oral evidence accepted that when first having used the Mailmedia service and received Royal Mail's invoice showing it treated the supply as exempt, he knew that Royal Mail treated the supply as exempt when Zipvit entered into subsequent Mailmedia contracts. He agreed in oral evidence, if not in his witness statement, and I find that at the time of the supplies at issue in this appeal, both Royal Mail and Zipvit considered the Mailmedia services to be exempt from VAT.
>
> 14. I also admitted into evidence a recently dated email in which Royal Mail refused to provide a VAT invoice to another customer (not Zipvit) in respect of supplies to that person similar to the supplies made to Zipvit. The facts were that no VAT invoices had been issued by Royal Mail to Zipvit for Mailmedia supplies and Zipvit had not asked for VAT invoices to be issued to it."

23. The documentary evidence before the FTT included some sample invoices from Royal Mail to Zipvit which designated with a capital "E" the assumed exempt status

of the Mailmedia services. The invoices would typically include other services which were zero-rated, designated with a "Z".

24. Zipvit's initial claim to recover overpaid input VAT was made on 15 September 2009, in respect of quarterly periods dating back to 1 January 2006. By a letter dated 27 April 2010, the compliance officer dealing with the matter for HMRC informed Zipvit's then agents that before making a decision he would require evidence of the contractual arrangements between Zipvit and Royal Mail over the period of the claim, together with evidence that input tax had been incurred, i.e. copies of the invoices. It was in response to this request that the sample invoices which we have seen were provided, under cover of a letter dated 7 May 2010 from Dains LLP which said:

> "I am unable to provide you with any written agreement between my client and Royal Mail as there is only really the invoices that reflect the agreement. However, the services that have been negotiated between Royal Mail and my client are clearly listed in the copy invoices provided."

25. HMRC replied on 12 May 2010. The officer said he was now in a position to consider Zipvit's claim, following a recent announcement of detailed policy changes resulting from the TNT ruling as set out in a Technical Note issued on 24 March 2010. The letter continued:

> "It is HMRC's understanding that Royal Mail's (including Parcelforce's) contract terms explicitly provide that charges made for supplies of postal services are exclusive of VAT and that any VAT, if due, is to be paid on top of the price quoted in the contract. In such cases, HMRC do not consider that customers can have valid claims that sums charged to them in the past by Royal Mail for supplies of postal services included VAT.
>
> …
>
> From the information that you have provided me with, I am of the opinion that there is no reason to believe that your client's contractual arrangements with Royal Mail differed in some respect from the norm. Furthermore, you have not been able to provide me with evidence that the price which your client was charged by Royal Mail included VAT."

26. Despite the focus in this letter on the precise contractual position as between Zipvit and Royal Mail, and in particular the question whether the relevant supplies were explicitly agreed to be exclusive of VAT (if any), it is unfortunate that this aspect of the underlying facts does not appear to have been followed up with much enthusiasm on either side. Rather, Dains LLP responded on 4 June 2010 by seeking an internal review of HMRC's decision, and advancing an argument of law based on section 19

of VATA 1994 to the effect that the consideration paid by Zipvit for the relevant services had to be treated as a taxable amount which included VAT. As I have already mentioned, the internal review upheld the officer's original decision on 2 July 2010.

27. In any event, the result seems to have been to divert attention away from further investigation of the precise contractual position between Zipvit and Royal Mail in relation to the Mailmedia services, nor had the omission been rectified by the time of the FTT hearing. The relatively few contractual documents placed before the FTT were incomplete, and in some respects difficult to follow. A further problem was that the relevant documents evidently went through various iterations, and the system was designed to be operated online (as the FTT recorded at [11] of the FTT Decision). It is therefore unsurprising, and involves no criticism of Judge Mosedale, that the FTT was unable to analyse the contractual position in any depth. On the limited material available to her, she was in my view plainly right to say that there was nothing in the information provided by Royal Mail about the Mailmedia service which mentioned VAT, and to find that at the relevant time both Royal Mail and Zipvit considered the Mailmedia services to be exempt from VAT: see the FTT Decision at [11] and [13], quoted above. Nevertheless, in a case of such importance, which had been selected as a lead case, it was, and is, unsatisfactory that analysis of the true contractual position should have been allowed in this way to go almost by default.

28. In principle, there were at least three possibilities which needed to be considered. The first possibility was that the price charged by Royal Mail to Zipvit for the Mailmedia services was agreed, either expressly or by necessary implication, to be exclusive of the VAT, if any, which might prove to be chargeable in respect of those services, regardless of the common assumption of the parties that they were exempt from VAT. The second possibility was that the price was agreed, either expressly or by necessary implication, to be inclusive of any VAT which might prove to be chargeable. The third possibility is that the contract, properly construed, was simply silent on the question. It also needs to be said that the position would not necessarily have been the same for each supply of Mailmedia services, over a period of some four and a half years. It is common ground that a separate contract was entered into on each occasion when Zipvit completed an online application for the Mailmedia service, and that there was no overarching "umbrella" contract under which the applications, or any groups of them, were made.

29. It is, I think, reasonable to infer that, had she directed her mind to the question, Judge Mosedale would have considered the third possibility to be correct. On the material before her, there was nothing to indicate that the incidence of VAT on the relevant supplies formed any part of the contracts made between the parties. We felt some concern, however, about proceeding on that basis without any consideration being given to the other two possibilities, particularly as it was apparent from at least one document in the bundle that the agreements were subject (inter alia) to "General Terms and Conditions" which neither side had taken steps to obtain and place before the FTT. Nor were we able to allay our concerns during the course of the hearing in this court, because the transactions had taken place before Zipvit's present solicitors (Mishcon de Reya LLP) had been instructed, and HMRC, for their part, had taken no steps to compel production of the missing documents from Royal Mail.

30. It was for these reasons that, at the conclusion of the hearing, we asked HMRC to make further enquiries of Royal Mail's solicitors to see if further light could be

thrown on the true contractual position, and (in particular) if the missing general terms and conditions could be supplied.

The new contractual material

31. On 15 January 2018, HMRC wrote to the Court with the results of the enquiries they had made since the hearing with Royal Mail's solicitors, Macfarlanes. Two sets of contractual terms and conditions had been supplied:

(1) a "mailmedia Schedule", which stated at clause 1.1 that it set out "the obligations of the Customer and Royal Mail in relation to mailmedia Mailings and must be read with and subject to the Royal Mail Bulk Mail General Terms and Conditions" ("the mailmedia Schedule"); and

(2) an undated set of "Bulk Mail General Terms and Conditions" ("the General Terms").

As to the dates of these documents, HMRC had been informed that Royal Mail believed the mailmedia Schedule to have been created in 2006, a date which was consistent with the metadata "properties" of the document which showed it to have been created on "10/5/2006" and modified on the same date. HMRC had also been informed by Macfarlanes that the General Terms were served on Royal Mail by the claimants in the pending litigation against Royal Mail in the Chancery Division of the High Court, who identified the document as dating from September 2005.

32. Clause 3.1 of the General Terms reads as follows:

> "3 **Postage**
>
> 3.1 The Customer or Royal Mail shall calculate the Postage in accordance with the relevant Schedule on the occasion of each posting on the basis of details submitted by the Customer on the appropriate posting docket (also known as the "posting cheque") to an authorised Royal Mail representative at the time of posting. Such details must be full and accurate. *Unless expressly stated otherwise in a Schedule, all Postage and other charges specified in each Schedule as payable by the Customer are exclusive of VAT*. The Customer shall pay any VAT due on Postage and other charges at the appropriate rate in accordance with the payment provisions set out in the relevant Appendix to these terms and conditions. VAT shall be calculated and paid on the net amount of the Postage (that is after deduction of any Discount to which the Customer is entitled". (Emphasis added.)

"Postage" is defined as meaning "the amount payable by the Customer to Royal Mail in respect of each Posting", while "Schedule" is defined as meaning "the schedule(s) for the Services which describe the services." There is nothing in the mailmedia Schedule itself which qualifies the position set out in clause 3.1 of the General Terms.

33. On the strength of this material, HMRC submitted that clause 3.1 shows that Zipvit and Royal Mail agreed that the charges for Mailmedia services were to be "exclusive

of VAT". On that basis, it was said, it was no longer possible for Zipvit to argue that the charges made for the relevant services could be deemed to have included VAT. HMRC also drew our attention to certain further documents which, they said, indicated that the same position had continued after 2006, including Royal Mail's current General Terms and Conditions dated 3 July 2017, which provide at clause 5.6:

> "Unless otherwise stated, the charges set out in the rate card do not include VAT. You must pay any VAT due on the charges, which will be added to your invoice at the then current rate."

34. On 19 January 2018 Mishcon de Reya also wrote to the court, expressing a number of concerns about the material supplied by HMRC on 15 January. First, they observed that Royal Mail could not guarantee the exact date of the General Terms, even though it was a Royal Mail document. Our attention was drawn to some minor points of detail which might be thought to cast some doubt on whether the General Terms were indeed those applicable at the relevant time. Secondly, even if the General Terms were on the balance of probabilities those in force at the relevant time, we were invited "to exercise a degree of caution" in relation to their application. The documents supplied by HMRC had not been produced at the FTT hearing, and if HMRC had wished to advance a case that all the relevant supplies were exclusive of VAT, if chargeable, they should have done so. In this context, Mishcon de Reya were able to produce an undated copy of another set of Royal Mail Terms and Conditions which were entirely silent on the issue of VAT. It would be most unsatisfactory, they said, "if, at this stage, this case were to be decided on the strength of documents whose relevance had not been tested under conditions of close scrutiny of the kind which would have been possible at first instance." Finally, we were reminded that this is a lead case in respect of VAT claims on postal services under Rule 18 of The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009, and that even if the General Terms provided by HMRC were those which applied to the Mailmedia supplies made to Zipvit, this would not be the case for all the supplies made to the wider class of claimants, or indeed all the supplies made to Zipvit itself.

35. Mishcon de Reya therefore submitted that it would be of most assistance to the general class of Rule 18 claimants if, rather than deciding the appeal on the uncertain basis that the General Terms were those in force at the relevant time, we were instead to consider the matter "first, on the assumption that the FTT was right to find that these supplies were inclusive of VAT; and secondly, on the alternative that the Royal Mail's charges at the relevant time were exclusive of VAT."

36. On 12 February 2018 we gave directions to the parties, which were mainly concerned with obtaining an official English translation of the Advocate General's opinion in Biosafe, but which also said that we proposed to consider the contractual position on the basis of the alternative hypotheses suggested by Mishcon de Reya in their letter of 19 January. Over a month later, on 14 March 2018, HMRC returned to the fray, claiming to have located further documents which supported their earlier submissions on the contractual position. First, however, they pointed out that Mishcon de Reya had been wrong to assert that the FTT found that the supplies made by Royal Mail to Zipvit were "inclusive of VAT", if by that they meant that the FTT had made a finding of fact to this effect. As I have already indicated, I consider that this point was

well taken. If anything, the FTT had implicitly found that the contract was silent on the issue of liability to VAT: see [29] above. Next, HMRC said that they had now located an electronic copy of the General Conditions provided to HMRC by Royal Mail, which had a final page, apparently omitted from the hard copy, which showed the date of the document to be September 2005. Further confirmation of that date was provided by the "properties" of the document, which showed it to have been created on 21 September 2005. A footnote stated that this electronic document had been sent to HMRC Solicitor's Office on 29 February 2012, but its significance had not been appreciated until the mailmedia Schedule recently provided by Royal Mail was considered. Furthermore, another set of General Terms and Conditions dated May 2011 had also been located, which defined "services" as including Mailmedia services, and which stated in clause 6.6 that the charges set out in the rate card "do not include VAT". Accordingly, submitted HMRC, it was now "entirely clear that Mailmedia supplies were made on the basis that charges were exclusive of VAT from at least September 2005 up to 2011", i.e. throughout the claim period.

37. In relation to Zipvit's proposal that the Court should consider the matter on alternative hypotheses, HMRC said that they would have no objection to our doing so, particularly as this is a lead case, but submitted that we should determine Zipvit's own appeal in the present case on the footing that the relevant supplies were exclusive of VAT as a matter of contract.

38. Mishcon de Reya responded on 16 March 2018. They observed that HMRC, on their own admission, had been in possession of both the (2005) General Terms and the 2011 Terms and Conditions since 29 February 2012, which was over two years before the FTT hearing on 14 and 15 May 2014. They submitted that a deliberate decision must therefore have been taken not to produce these documents before the FTT, and that the documents should not be admitted in evidence for the purposes of the present appeal pursuant to CPR Rule 52.21(2) because the well-known conditions in Ladd v Marshall [1954] 1 WLR 1489, 1491 were clearly not satisfied, and there was no overriding reason why HMRC should at this late stage be allowed to rely on evidence which was available and known to them before the FTT hearing. Mishcon de Reya also argued that HMRC had chosen to run their case below on a different basis from that which they now advanced. Their argument before the FTT had not been that the contracts were exclusive of VAT, but rather that Zipvit had never borne the VAT liability because VAT was not in fact charged at the time, nor was there anything which rendered Zipvit liable to pay it: see the FTT Decision at [29].

39. Shortly thereafter, on 21 March 2018, we issued some further directions, which included the following:

> "With regard to the contractual position, we will not rule at this stage on the admissibility and relevance of the further material which HMRC wish to adduce, but will do so in due course in our judgment. HMRC may reply briefly to Mishcon de Reya's letter of 16 March 2018, if they have not already done so, but subject thereto the Court will not receive any further material or submissions on the contractual position."

HMRC had not previously replied to Mishcon de Reya's letter of 16 March, and they belatedly took up the permission which we gave them to do so in the written

submissions which they filed on 16 May 2018. HMRC now submitted that the Ladd v Marshall criteria were satisfied, and that admitting the material would further the overriding objective of enabling this court to deal with the case justly. Although HMRC had asked Royal Mail to provide relevant documentation before the FTT hearing, Royal Mail had not disclosed the mailmedia Schedule; and it was only when this schedule was eventually produced on 7 December 2017, after the hearing of the present appeal, that the relevance of the General Terms had become apparent. The new contractual documentation was clearly relevant and important, and there were no grounds for questioning its credibility. Further, HMRC were not now seeking to advance an entirely new argument. HMRC's position had always been that Zipvit's case must fail because Zipvit was not charged VAT, and did not pay any VAT, in a situation where both parties considered that VAT was not payable. The contract was therefore akin to one which was stated to be exclusive of VAT, and the new material confirmed that the effect of the agreement was precisely as HMRC had argued: the parties agreed that no part of the price included VAT.

40. Finally, Zipvit provided a brief rejoinder in their written submissions dated 17 May 2018. Apart from expressing surprise that HMRC had taken so long to make further submissions on the question, Zipvit argued that the Ladd v Marshall conditions were not satisfied, because there were two reasons why the documents could with reasonable diligence have been obtained for the FTT hearing. First, it appears from an email sent by HMRC to Macfarlanes on 21 December 2017 that some or all of the relevant documents which have now been produced were available online; and, secondly, HMRC at all times had the statutory power to demand the documents from Royal Mail under Schedule 36 to the Finance Act 2008, but had failed to do so.

Should we admit the new contractual material?

41. CPR rule 52.21(2) states that:

> "(2) Unless it orders otherwise, the appeal court will not receive -
>
> (a) oral evidence; or
>
> (b) evidence which was not before the lower court."

An appellate court therefore has a discretion whether or not to receive fresh evidence which was not before the lower court. No guidance is given in the Rules about how this discretion is to be exercised, save that by virtue of rule 1.2 the court must, when it exercises the discretion, seek to give effect to the overriding objective of "enabling the court to deal with cases justly and at proportionate cost": see rule 1.1(1). The jurisprudence on the principles which an appellate court should follow in this context is helpfully summarised in the White Book (2018 edition), volume 1, at paragraph 52.21.3. In short, the old Ladd v Marshall conditions, although no longer primary rules, have been said to still occupy the whole field of relevant considerations to which the appeal court must have regard; but they do not place the court in a straitjacket, and the court must always seek to give effect to the overriding objective of doing justice in the individual case. It is also necessary to bear in mind, in the present context, that the appeal to us from the Upper Tribunal lies only on questions of law: see section 13(1) of the Tribunals, Courts and Enforcement Act 2007.

42. With these considerations in mind, I have concluded, although not without some hesitation, that we should receive in evidence the mailmedia Schedule and the General Terms enclosed with HMRC's letter to the Court dated 15 January 2018, even though this material could with reasonable diligence have been obtained for the FTT hearing. I reach this conclusion for a number of reasons. First, it is clear from the documents which were before the FTT that the agreements for Mailmedia services were contained in a number of separate documents, comprising a Preface, attached General Terms and Conditions, a relevant Schedule, and a User Guide for the relevant service. So much is apparent from the Preface at page 150 of our second supplementary bundle. Secondly, therefore, it is evident from the material before the FTT that the parties were arguing the case before it on the basis of contractual documentation which was incomplete, and which moreover omitted the part of the contract (the General Terms) where any general provision relating to VAT was most likely to be found. Thirdly, in a lead case in wider litigation where tax of around £1 billion is likely to be at stake, it is of particular importance that the facts should be investigated as fully as possible in relation to the sample transactions on which the FTT was asked to rule. The utility of the FTT's ruling will be significantly diminished if it rests on a factual foundation which is incomplete or misleading. Fourthly, it seems to me overwhelmingly probable that the General Terms were indeed in force throughout the period of Zipvit's Mailmedia claims, and that they were incorporated in each Mailmedia contract into which Zipvit entered with Royal Mail during that period. No serious suggestion to the contrary is made in the correspondence from Mishcon de Reya which I have summarised.

43. In these circumstances, the interests of justice seem to me to require the admission of the material in question. Only in this way can the full contractual picture be understood and analysed. Further, I agree with HMRC that the new material clearly satisfies the second and third Ladd v Marshall conditions: the evidence would probably have had an important influence on the result of the case, and it is apparently credible. The difficulty lies with the first condition, namely that the evidence could not have been obtained with reasonable diligence for use at the trial. It seems to me tolerably clear that, with reasonable diligence, it both could and should have been obtained, not least because the material already supplied was self-evidently incomplete. On the other hand, in a lead case of this nature, I think there was a responsibility on both sides to ensure that the contractual position was fully placed before the FTT, and (as I have explained) the question was instead allowed to go virtually by default. In any event, whichever side was mainly to blame – and I stress that we are in no position, having barely scratched the surface, to get to the bottom of that question – it seems to me that this is a case where the interests of justice must prevail over any failure by HMRC to exercise reasonable diligence in obtaining the new material before the FTT hearing.

44. I do, however, accept that, if we admit the new material, we should also do our best to consider the position on the alternative hypotheses (a) that the contract was silent on the issue, and (b) that the contract provided, either expressly or by implication, for the price paid to be inclusive of VAT, if any.

The right to deduct input tax: general principles

45. It is a cardinal feature of the common system of VAT under EU law that a trader who makes taxable supplies is entitled to deduct from the output tax for which he is

accountable in respect of those supplies any input tax due or paid by him on supplies of goods or services to him which are properly attributable to his own taxable supplies. As Article 1(2) of the Principal Directive states:

> "The principle of the common system of VAT entails the application to goods and services of a general tax on consumption exactly proportional to the price of the goods and services, however many transactions take place in the production and distribution process before the stage at which the tax is charged.
>
> On each transaction, VAT, calculated on the price of the goods or services at the rate applicable to such goods or services, shall be chargeable after deduction of the amount of VAT borne directly by the various cost components.
>
> The common system of VAT shall be applied up to and including the retail trade stage."

46. It follows from this basic principle that, leaving aside the case of exempt supplies, it is only the final consumer at the end of a chain of supply who bears the burden of the tax, which is designed to operate with complete neutrality at each intermediate stage in the chain. This was explained by the CJEU in a frequently cited passage from its judgment in Case C-317/94, Elida Gibbs Limited v Customs and Excise Commissioners, [1997] QB 499, [1996] STC 1387, as follows:

> "**General considerations**
>
> 18. Before replying to these questions, it is appropriate to describe briefly the basic principle of the VAT system and how it operates.
>
> 19. The basic principle of the VAT system is that it is intended to tax only the final consumer. Consequently, the taxable amount serving as a basis for the VAT to be collected by the tax authorities cannot exceed the consideration actually paid by the final consumer which is the basis for calculating the VAT ultimately borne by him.
>
> …
>
> 22. It is not, in fact, the taxable persons who themselves bear the burden of VAT. The sole requirement imposed on them, when they take part in the production and distribution process prior to the stage of final taxation, regardless of the number of transactions involved, is that, at each stage of the process, they collect the tax on behalf of the tax authorities and account for it to them.

> 23. In order to guarantee complete neutrality of the machinery as far as taxable persons are concerned, the Sixth Directive provides, in Title XI, for a system of deductions designed to ensure that the taxable person is not improperly charged VAT… a basic feature of the VAT system is that VAT is chargeable on each transaction only after deduction of the amount of VAT borne directly by the cost of the various price components of the goods and services. The procedure for deduction is so arranged that only taxable persons are authorised to deduct from the VAT for which they are liable the VAT which the goods and services have already borne.
>
> 24. It follows that, having regard in each case to the machinery of the VAT system, its operation and the role of the intermediaries, the tax authorities may not in any circumstances charge an amount exceeding the tax paid by the final consumer."

47. By contrast, where a trader makes exempt supplies, he is in respect of those supplies in the same position as a final consumer, and must therefore bear the burden of input tax attributable to those supplies. This burden of irrecoverable input tax is an exception to the general principle of fiscal neutrality in the field of VAT, and this was of course the situation which the parties wrongly thought applied when Zipvit entered into the relevant Mailmedia contracts with Royal Mail. The FTT had some indirect evidence before it about the level of irrecoverable VAT which was borne by Royal Mail on the assumption that the Mailmedia supplies to Zipvit were exempt. At [29] of the FTT Decision, the FTT recorded Zipvit's acceptance "that at most the irrecoverable VAT incurred by the Post Office in making the supplies would only have increased the net price by a maximum of 2.5%". See too [183], where it appears that Zipvit had suggested this was the right figure because of what the postal services regulator, Postcomm, said in a consultation document in 2004:

> "3.7 As Royal Mail cannot reclaim VAT charged to it, this irrecoverable VAT forms part of the costs to Royal Mail and is taken into account in setting the price of its services. Postcomm estimates that irrecoverable VAT leads to Royal Mail's prices being on average around 2.5% higher than they would be if Royal Mail did not incur this cost."

48. A further important principle, to which Mr Thomas QC drew our attention, is that the right to deduct does not depend on showing that the input tax in question has been paid or accounted for by the supplier as output tax to the revenue authorities. As the Third Chamber of the CJEU said in the case of Bonik EOOD (Case C-285/11, [2013] STC 773), at paragraph 28 of its judgment:

> "The question whether the VAT payable on the prior or subsequent sales of the goods concerned has or has not been

> paid to the public purse is irrelevant to the right of the taxable person to deduct input VAT. VAT applies to each transaction by way of production or distribution after deduction of the VAT directly borne by the various cost components…"

Similar statements may be found in other cases which we were shown, including Joined Cases C-80/11 and C-142/11, Mahagében, [2012] STC 1934, at paragraph 40, cited in the UT Decision at [37].

49. Nevertheless, this principle cannot be applied in isolation, and in particular does not in my judgment override the requirement for a person exercising the right of deduction to produce a VAT invoice evidencing payment of the relevant VAT by the supplier. I will return to this point in my consideration of the second main issue on the appeal.

The "due or paid" issue

50. Against this background, I can now turn to the first main issue in the case. If Zipvit's claim is to succeed, Zipvit must first establish that there is "VAT due or paid" in the UK in respect of the Mailmedia services supplied to it by Royal Mail. The wording of Article 168 of the Principal Directive (set out in [12] above) expressly confines the right of deduction to VAT which has been so due or paid, and if no such VAT can be identified it follows that the claim must fall at the first hurdle.

51. As I have already said, it is common ground that the VAT in question must have been paid by, or due from, Zipvit in respect of the Mailmedia services: see [15] above. The question is *not* whether the supplier, Royal Mail, has paid or become liable to pay the corresponding output tax to HMRC. That was the view independently taken by the FTT of its own initiative, but was rightly rejected by the Upper Tribunal: see the UT Decision at [20] to [25] and the authorities there cited, which include Bonik EOOD (see [48] above) and the later judgment of the CJEU to similar effect in Case C-277/14, PPUH Stehcemp sp. J. Florian Stefanek, Janina Stefanek, Jaroslaw Stefanek v Dyrektor Izby Skarbowej w Lodzi, EU:C:2015:719, at paragraph 45.

52. In considering whether, and if so when, VAT was due or paid, the main provisions of the Principal Directive which need to be taken into account are the following.

53. In Title VI, headed "Chargeable Event and Chargeability of VAT", Article 62(1) defines "chargeable event" for the purposes of the Principal Directive as meaning "the occurrence by virtue of which the legal conditions necessary for VAT to become chargeable are fulfilled". Article 63 then states that:

> "The chargeable event shall occur and VAT shall become chargeable when the goods or the services are supplied."

Accordingly, the chargeable event upon which VAT became chargeable in respect of the Mailmedia services supplied to Zipvit was the date when the services were supplied.

54. In Title VII, headed "Taxable Amount", Article 73 provides that:

> "In respect of the supply of goods or services… the taxable amount shall include everything which constitutes consideration obtained or to be obtained by the supplier, in return for the supply, from the customer or a third party, including subsidies directly linked to the price of the supply."

And by virtue of Article 78:

> "The taxable amount shall include the following factors:
>
> (a) taxes, duties, levies and charges excluding the VAT itself;
>
> …"

It follows from these provisions that the taxable amount includes the entire consideration obtained or to be obtained by the supplier in return for the supply, and that VAT is then chargeable on that amount. The taxable amount does not have to be grossed up so that it includes the VAT chargeable on the supply. This is achieved by excluding "the VAT itself" from the taxable amount.

55. As a matter of domestic law, the relevant provisions of the Principal Directive are implemented and given effect by VATA 1994. The basic charge to VAT on taxable supplies is imposed by section 4:

> "(1) VAT shall be charged on any supply of goods or services made in the United Kingdom, where it is a taxable supply made by a taxable person in the course or furtherance of any business carried on by him.
>
> (2) A taxable supply is a supply of goods or services made in the United Kingdom other than an exempt supply."

By virtue of section 6(3), "a supply of services shall be treated as taking place at the time when the services are performed."

56. The value of a supply of goods or services is determined in accordance with section 19. I have already quoted the wording of subsection (2), which plays a crucial role in Zipvit's submissions: see [15] above. It is, however, helpful to place the subsection in its immediate context:

> "19(1) For the purposes of this Act the value of any supply of goods or services shall, except as otherwise provided by or under this Act, be determined in accordance with this section…
>
> (2) If the supply is for a consideration in money its value shall be taken to be such amount as with the addition of the VAT chargeable, is equal to the consideration.
>
> (3) If the supply is for a consideration not consisting or not wholly consisting of money, its value shall be taken to be such

> amount in money as, with the addition of the VAT chargeable, is equivalent to the consideration.
>
> (4) Where a supply of any goods or services is not the only matter to which a consideration in money relates, the supply shall be deemed to be for such part of the consideration as is properly attributable to it.
>
> …"

57. Sections 24 to 26 deal with the payment of VAT by taxable persons, and provide for the familiar machinery by which input tax may be deducted from output tax. By virtue of section 25(2), a taxable person:

> "… is entitled at the end of each prescribed accounting period to credit for so much of his input tax as is allowable under section 26, and then to deduct that amount from any output tax that is due from him."

Subsection (3) then provides that if either no output tax is due at the end of the period, or the amount of the credit exceeds that of the output tax, then (subject to certain exceptions) the amount of the credit or the excess "shall be paid to the taxable person by the Commissioners", and the amount so due is referred to in the Act as a "VAT credit".

What is the effect of section 19(2) of VATA 1994?

58. Section 19(2) has the potential to cause confusion, because at first glance it may look like a grossing-up provision of some kind. But that is not what it says, and (if it did) it would be incompatible with Article 78(a) of the Principal Directive which tells us that the taxable amount excludes the VAT on the supply. Rather, the effect of section 19(2) is that the (taxable) value of a supply made for a consideration in money is "such amount as, with the addition of the VAT chargeable, is equal to the consideration." So, if the rate of VAT is taken to be 20%, the taxable value of a supply made for a total consideration of £120 is £100. The consideration does not itself have to be grossed up with tax at 20% on £120, producing a taxable value of £144.

59. There is no difficulty in principle with this analysis if the consideration for a taxable supply is agreed to be £100 plus VAT, or if the agreement says nothing about VAT, with the consequence that the agreed consideration of £120 must be treated as inclusive of VAT. But what if the parties agree a price which is *exclusive* of VAT, perhaps because it is unclear whether VAT is properly chargeable on the supply? In that kind of case, it will be a matter of construction of the agreement between the parties to determine whether the customer is contractually liable to pay an amount equal to the VAT, if and when it turns out to be properly chargeable. Assuming that to be the correct construction, and if it emerges that VAT is chargeable on the supply, the supplier will probably then send a VAT-only invoice to the customer (which would be for £24, if the agreed VAT-exclusive price were £120).

60. Does section 19(2) then have the effect that the original payment of £120, made on a VAT-exclusive basis, must be retrospectively split into a taxable amount of £100 plus VAT of £20, and that the subsequent payment of £24 (assuming that the customer honours his contractual obligation) must likewise be split into a further taxable amount of £20 and VAT of £4? As a matter of first impression, there is much to be said in favour of an affirmative answer to this question. There is still only one supply, and a single overall consideration for it, albeit paid in two instalments; and since the supply is (on this hypothesis) taxable, each of the sums paid on account of the total price should be regarded as including VAT at the appropriate rate. The function of section 19(2) is to ensure that the total consideration is split into a taxable value of £120 and tax of £24, not to treat the first payment of £120 as exclusive of VAT and the second payment of £24 as consisting entirely of VAT. That may be how the supplier and the customer view the matter in commercial terms, but the correct analysis for VAT purposes could well be that there has been a single taxable supply for a total consideration for £144, comprising a taxable amount of £120 and VAT of £24, paid in two instalments

61. Furthermore, if this is in principle the correct analysis, it should not make any difference if, for whatever reason, the supplier fails to invoice the customer for the £24 when it becomes clear that the supply is indeed taxable. The original consideration of £120 may have been agreed to be exclusive of VAT, but if the true position is that the supply was always taxable, the parties cannot by agreement between themselves turn it into a supply which must be regarded as free from VAT unless and until an additional payment of the VAT element is made by the customer to the supplier. Once the taxable status of the supply has been established, there is no statutory warrant for treating one part of the consideration for the supply differently from the other parts.

62. These are, I think, in substance the arguments advanced by Mr Thomas on behalf of Zipvit for treating the sums paid by Zipvit to Royal Mail for the Mailmedia supplies as comprising VAT at the then standard rate, once it had become clear from the decision of the CJEU in TNT that the supplies were chargeable. Further, although there are no cases directly in point which look at the question from the point of view of a customer such as Zipvit, Mr Thomas submits that support for his analysis can be found in both UK and European case law.

63. The first of the UK cases to which we were referred is the decision of Lewison J (as he then was) in Mason v Boscawen [2008] EWHC 3100 (Ch), [2009] 1 WLR 2139. The facts were far removed from those of the present case, but the relevant issue for present purposes was whether the element of VAT formed part of the rent paid by a tenant of an agricultural holding, in circumstances where the landlord had notified the tenant that he had elected to waive the exemption from VAT (pursuant to paragraph 2 of Schedule 10 to VATA 1994) and to charge VAT on his agricultural rents. When the tenant subsequently failed to pay the amount shown in a quarterly VAT-inclusive rent invoice, and the landlord, relying on this failure, served a notice to quit under the Agricultural Holdings Act 1986, the question arose whether the notice was invalid because it sought to include as rent due the amount payable in respect of VAT.

64. Lewison J decided this issue in the landlord's favour, and at [50] said this:

> "If… the VAT element is not part of the rent, how is the landlord to recover it from the tenant if the tenant refuses to pay? In some tenancy agreements there may be a separate covenant to pay VAT; but many agreements (of which, in my judgment, this is one) contain no such obligation. In the case of a tenancy granted orally, an arbitration on terms would not result in the inclusion of such an obligation. Mr Rodger said that the VAT would be payable by the tenant as an obligation of his tenancy. But I was unable to discern which obligation had that effect unless it was the obligation to pay rent. Mr Rodger also submitted that VATA gave the landlord a freestanding right to recover the VAT. However, I do not think that it does. As I have said the rule is that the consideration for the supply is inclusive of VAT. Thus the VAT element is recoverable by the supplier simply because it is part of the consideration for the supply; and if the rate of VAT changes, VATA does no more than to provide for a change in the consideration."

65. In my view, this decision does not take matters much further, although it does show reliance by the judge on section 19(2) of VATA 1994 as showing "that the consideration for the supply is inclusive of VAT". Lewison J went on, in [52], to set out "a number of strong pointers towards the conclusion that the VAT element is part of the rent", the second of which was:

> "The prima facie rule under VATA is that the sum agreed for the supply is inclusive of VAT."

This must again be a reference to section 19(2), but as Mr Grodzinski emphasised for HMRC the judge only describes it as "the prima facie rule", thus leaving it open to the parties to agree a price which is exclusive of VAT.

66. Much more to the point, in my judgment, is the decision of the Third Chamber of the CJEU in the case of Tulică (Joined Cases C-249/12 and C-250/12), EU:C:2013:722, where the taxpayers had entered into numerous contracts for the sale of land over a period of three years, but had made no provision for VAT. Following a subsequent tax inspection, the tax authorities found that the activities of the taxpayers had the hallmarks of economic activity, with the consequence that they were taxable persons subject to VAT. They were then assessed to tax on the basis that VAT should be added to the agreed prices which had been paid by the contracting parties. The issue was whether this treatment was correct, or whether the prices actually paid should be regarded as inclusive of VAT. Relying on Articles 73 and 78 of the Principal Directive, the CJEU held that the price agreed must be regarded as already including the VAT which was chargeable, unless the supplier was able to recover from the purchaser the VAT claimed by the tax authorities.

67. The core reasoning of the Court is contained in paragraphs 33 to 37 of its judgment, as follows:

> "33. In accordance with the general rule set out in Article 73 of the VAT Directive, the taxable amount for the supply of goods or services for consideration is the consideration actually received for them by the taxable person. That consideration is thus the subjective value, that is to say, the value actually received, and not a value estimated according to objective criteria…
>
> 34. This rule must be applied in accordance with the basic principle of that directive: that the VAT system is aimed at taxing only the end consumer (see, inter alia, *Elida Gibbs*, paragraph 19, and order of 9 December 2011 in Case C-69/11 *Connoisseur Belgium*, paragraph 21).
>
> 35. When a contract of sale has been concluded without reference to VAT, in a situation where the supplier has no means under national law of recovering from the purchaser the VAT claimed subsequently by the tax authorities, taking the total price, without deducting the VAT, as the taxable amount on which the VAT is to be levied, leads to a situation where it is the supplier which bears the VAT burden, thereby conflicting with the principle that VAT is a tax on consumption to be borne by the end consumer.
>
> 36. Taking that amount as the taxable amount also conflicts with the rule that the tax authorities may not charge a VAT amount exceeding the amount paid by the taxable person (see, inter alia *Elida Gibbs*, paragraph 24; Case C-330/95 *Goldsmiths* [1997] ECR I-3801, paragraph 15; and *Balkan and Sea Properties and Provadinvest*, paragraph 44).
>
> 37. The situation is otherwise when the supplier has the possibility under national law of adding to the agreed price a supplement equal to the tax applicable to the transaction and recovering it from the purchaser of the good."

(Although paragraph 36 refers to "the amount paid by the taxable person", it is common ground that the context and the authorities cited make it clear that the reference should have been to "the amount paid by the end consumer".)

68. The significance of this case is that it shows the CJEU relying on Articles 73 and 78(a) of the Principal Directive so as to treat the contractually agreed consideration paid for supplies which were subsequently established to be taxable as inclusive of the VAT which ought to have been charged, even though the agreements were entirely silent on the question of VAT. The Court rejected the argument of the revenue authorities that VAT should be charged on a net amount equivalent to the original purchase price, because that would conflict with the principle that VAT is a tax borne by the end consumer. The only exception to this would be if, as a matter of contract, the vendors were able to pass on to the purchasers the amount of the VAT and to recover it from them, because in those circumstances the tax would still end up being paid by the end consumer.

69. Where the exception applies, the question then arises whether the original price should still be treated as partly composed of VAT, and whether the "supplement equal to the tax applicable to the transaction" which is recovered from the purchaser should be treated in the same way, or whether the transaction should now be analysed as consisting of an original payment exclusive of VAT, followed by a payment which in its entirety represents the tax. That question was not considered by the Court, but in my view it is at least arguably implicit in its reasoning that the treatment of the original price as VAT-inclusive is only necessary if VAT on the whole of the original price cannot subsequently be recovered from the purchaser. It is a matter for national law to determine whether the supplier can recover the VAT from the purchaser in this way, but, if he can, there is no explicit support in the Court's judgment for the proposition that it remains necessary to treat the original price as having included an element of VAT at the rate applicable to the transaction as a whole. Furthermore, if the tax can be recovered in this way, the taxable amount will be larger than if the original price has to be treated as VAT-inclusive, because the recoverable supplement will represent VAT on the whole of the original purchase price. That is the VAT which should have been added to the purchase price in the first place, and which was consequently claimed by the tax authorities. It is only if that tax cannot be recovered by the supplier from the purchaser that it becomes necessary to treat the original price as VAT-inclusive, in order to preserve the principle that the VAT on a transaction cannot exceed the amount actually paid by or due from the end customer.

70. In summary, therefore, Tulică provides solid support for Zipvit's case to the extent that it recognises the need for a retrospective dissection of the price paid for a supply which subsequently turns out to be taxable, but only in a situation where the supplier is unable to recover the tax from the customer as a matter of national law. The case provides no explicit guidance on the correct analysis in cases where recovery of the tax is possible, but arguably proceeds on the assumption that no retrospective dissection is then called for, and that the transaction should then be analysed as a single one, based on a taxable amount equal to the original purchase price, with the VAT being invoiced and paid separately.

71. Nor does the case give any separate consideration to the position of the purchaser, or to the question whether it is open to the purchaser to claim an input tax deduction for the notional VAT component of the original purchase price. As a matter of general principle, however, one would expect the purchaser's right of deduction to mirror the tax treatment of the transaction for the supplier, once the true taxable amount has been ascertained. If, therefore, the original purchase price has to be treated as VAT-inclusive, the purchaser should in principle be entitled to deduct the VAT component of the price which he has paid. If, on the other hand, the original price is treated as the taxable amount, and the VAT on it is subsequently paid by the purchaser, no right to deduct will arise until that stage.

72. I now turn to the second of the domestic authorities on which Zipvit principally relies, the decision of the Inner House of the Court of Session in Simpson & Marwick v Revenue and Customs Commissioners [2013] CSIH 29, [2013] STC 2275. The relevant facts, in outline, were as follows. The taxpayers ("S&M") were a firm of Scottish solicitors, who provided legal services to insurance companies. Pursuant to an agreement made in 1985 between HMRC and the British Insurance Association and other insurers, it was agreed that the relevant legal services could be treated as

supplied to the policyholders, who (if registered for VAT) could deduct as input tax VAT incurred on legal services supplied to them in connection with insurance claims relating to their business. In such cases, solicitors supplying services to insurance companies were obliged to address a tax invoice to the policyholder, requesting payment of an amount equal to the VAT on the relevant supply, and stating that the balance of the account would be settled by the insurance company, to which a copy of the invoice would be sent endorsed to indicate that the policyholder had been asked to pay the VAT. What happened, in practice, was that S&M would send a VAT-only invoice to the policyholder, and issue a different invoice to the insurance company client which was described as a "fee note" and expressly stated to be "not a VAT invoice": see the opinion of the court, delivered by Lord Eassie, at [6].

73. Following the insolvency of various policyholder clients, S&M claimed bad debt relief for the whole amount invoiced to the policyholder, representing the entirety of the VAT for which the firm had accounted on the making of the supply, even though their net fees had been paid in full by the insurance company. When this came to light, HMRC challenged the treatment adopted by S&M on the basis that the amount invoiced to the policyholder had to be treated as a part payment of the entire consideration for the supply, and the bad debt relief was therefore confined to the relevant VAT fraction (which was then 7/47, reflecting a standard rate of VAT of 17.5%) of the amount invoiced.

74. Under section 36 of VATA 1994, bad debt relief was available where a supplier of goods or services had accounted for and paid VAT on the supply, and "(b) the whole or any part of the consideration for the supply has been written off in his accounts as a bad debt". Subject to satisfying various conditions, the supplier was then entitled "to a refund of the amount of VAT chargeable by reference to the outstanding amount", and "outstanding amount" was defined in subsection (3) by reference to the amount of the consideration which had been written off.

75. S&M's claim succeeded before the Upper Tribunal, but the Inner House allowed HMRC's appeal. As Lord Eassie explained, at [26]:

> "On the assumption that one can identify the unpaid debt as being wholly or partially the amount of the VAT in the consideration the issue then arises whether s 36 VATA allows for the possibility of that being wholly available as relief. In our opinion the proper construction of s 36 VATA is the construction for which HMRC contend. The refund to which the taxpayer is entitled is stipulated in s 36(2) as the "amount of VAT chargeable by reference to the outstanding amount". The words "outstanding amount" are defined in sub-s (3) by reference to the amount of the "consideration" or the extent to which the "consideration" has been written off. But as s 19 VATA makes plain, the "consideration" is an amount inclusive of VAT. There is nothing in the text which gives any warrant for an exercise of seeking to identify the extent to which the amount is "demonstrably all VAT". While counsel for S&M submitted that the construction of s 36 for which he contended did not involve the reading in of qualifying words, or words of exception, we are unable to agree with that submission."

76. The court went on to say, at [27]:

> "Put shortly, S&M provided a taxable service for which they received partial payment of the consideration and we have to say we cannot see any real basis whereon it is inequitable, or contrary to elementary fairness, that they should not be responsible, in the normal way, for the proportionate amount of VAT on the part-consideration which they received."

77. On the rather unusual facts of the case, this was in my view clearly the correct conclusion. S&M had been paid by the insurance companies the full net amount of the consideration for the supplies, and although the full amount of the VAT was separately invoiced to the policyholder, with the intention that the policyholder should then utilise it as input tax, the position so far as S&M was concerned was simply that it had received a part payment of the consideration for the original supply. Section 19(2) of VATA 1994 applied to the whole of that consideration, and since the only "outstanding amount" for the purposes of bad debt relief was the amount invoiced to the policyholder, relief could only be given for the VAT chargeable by reference to that amount, i.e. the appropriate VAT fraction of it. The decision turns, however, on the construction of the bad debt relief provisions in section 36. It does not deal with the separate question whether it was in law open to the parties to structure the transaction so that the entirety of the VAT element was paid by the policyholder, which would then be entitled to deduct it as input tax, although it is fair to say that HMRC must have had no objection to this being done, because it followed from the agreement which they made with the insurers in 1985. Thus the support which Zipvit is able to draw from the case is in my opinion limited. True, it reflects the fact that section 19(2) of VATA 1994 treats the consideration for a supply as VAT-inclusive, but it leaves open the question whether the parties to a transaction may agree that the entirety of the VAT element of the consideration shall be paid by a person who is then entitled to deduct it as input tax, even though the net taxable amount is paid in full by another person.

The recent decisions of the CJEU in Volkswagen and Biosafe

78. It is convenient at this point to consider whether any light is thrown on the "due or paid" issue by the recent decisions of the CJEU in the Volkswagen (EU:C:2017:823) and Biosafe cases. I will need to return to these cases in the context of the second main issue, which concerns the need for a VAT invoice before the right to deduct input tax may be exercised. HMRC submit, however, that the cases are also relevant to the "due or paid" issue, because in each case the parties to the transactions had been mistaken about the application of VAT. In Volkswagen, the parties considered that the supply was exempt, when it was in fact standard-rated; and in Biosafe, the parties considered that the supply was taxed at a reduced rather than a standard rate. In Volkswagen, the customer (Volkswagen) sought to claim input VAT after it became clear that the supply was not exempt and a new invoice had been obtained charging the VAT due, which Volkswagen then paid. In Biosafe, the supplier (Biosafe) had originally charged VAT at the reduced rate of 5%, and when it was later

assessed to tax on the basis that the standard rate of 21% applied, Biosafe paid the assessment and issued new invoices to its customer, Flexipiso. Flexipiso refused to pay, on the basis that it would be out of time to deduct the additional VAT invoiced under the relevant domestic limitation period. Similarly, the issue in Volkswagen was whether the company could apply for a refund of the relevant VAT after the expiry of the relevant limitation period. In each case, the CJEU decided that the right to deduct the correct amount of input tax charged on the new invoices could not be defeated by the limitation period, because the true position had not been apparent to the claimant company at the time of the original transaction, and neither customer was able to deduct the correct amount until the issue of the new invoices.

79. The point made by HMRC is that in neither case did the CJEU analyse the position on the basis that the price paid for the original supply must be treated as inclusive of VAT at the correct rate, with the consequence that the customer, having paid that price, could have claimed to recover the VAT as input tax even before new invoices showing the correct amount of VAT due were issued. The difficulty with this submission, however, is that no argument to this effect appears to have been raised in the questions referred to the CJEU, nor was it considered by the Court. Indeed, there is no reference to Tulică in the judgment of the Court or the opinion of the Advocate General in either case. In those circumstances, it is in my view impossible to read anything into the Court's omission to analyse the matter in that way.

80. Without going into further detail, therefore, I am satisfied that neither case throws any useful light on the "due or paid" issue.

The contractual position as between Royal Mail and Zipvit

81. The Mailmedia services which Royal Mail supplied to Zipvit were subject to the General Terms, which provided that the charges payable by Zipvit were "exclusive of VAT". If, as I have held, we should take account of the General Terms on this appeal, it seems that they applied to all of the Mailmedia supplies made to Zipvit during the claim periods. At the time of the supplies, and when Zipvit paid the charges invoiced by Royal Mail, it was the common understanding of the parties that the supplies were exempt. What, then, is the effect of the contractual term that the supplies were "exclusive of VAT", when it later became clear that the supplies were subject to VAT at the standard rate? In particular, would it then have been open to Royal Mail to invoice Zipvit for VAT on the original contract price for each supply?

82. There is no provision in the Principal Directive or in the domestic law of VAT in the United Kingdom which would have entitled Royal Mail to raise an invoice for VAT in those circumstances. On the contrary, the effect of the provisions which I have already examined is that, in the absence of a contractual right to recover the VAT, the consideration paid for the original supply has to be treated as VAT-inclusive. Thus the question resolves itself into one of contractual interpretation. On the true construction of the agreement made between Royal Mail and Zipvit in relation to each supply of Mailmedia services, including the General Terms, did Royal Mail have the right to recover VAT on the original contract price from Zipvit?

83. In my judgment, the answer to this question is now clear. According to clause 3.1 of the General Terms, quoted at [32] above, Zipvit is obliged to "pay any VAT due on Postage and other charges at the appropriate rate in accordance with the payment

provisions set out in the relevant Appendix". There are five Appendices to the General Terms. The first four set out various forms of arrangement for payment which may be made (credit account, reducing customer balance, pre-paid account and budget account respectively), while Appendix 5 sets out the permitted methods of settlement. Thus there is a clear obligation on Zipvit to pay any VAT which may be due. Furthermore, since the charges were expressly agreed to be "exclusive of VAT", it is clear that the taxable amount would be the amount actually charged to Zipvit for each supply of Mailmedia services, subject only to deduction of any discount to which Zipvit may have been entitled (see the concluding words of clause 3.1).

84. It follows, in my judgment, that the case may fall within the exception identified by the CJEU in Tulică, and potentially requires decision of an issue which the CJEU left undecided because it did not arise on the facts of that case, namely whether the original purchase price paid by the customer to the supplier should be treated as VAT-inclusive, in circumstances where the supplier has a contractual right to obtain payment of the VAT from the customer, but (for whatever reason) has failed or chosen not to enforce that right. Furthermore, if such treatment were in principle correct, would the customer then have the right to deduct the VAT element of the original price as input tax? In my view, neither the case law of the CJEU, nor the domestic authorities which I have reviewed, provide a clear answer to these questions, and if their resolution were essential to the outcome of the present appeal, I would see no escape from the conclusion that a reference to the CJEU was necessary.

Conclusions on the "due or paid" issue

85. In the light of the above discussion, I can now summarise my conclusions on the "due or paid" issue.

86. In circumstances where (as I have held) the supplier (Royal Mail) had a contractual right to recover from the customer (Zipvit) an amount equivalent to the VAT which should have been charged on the Mailmedia supplies, but took no steps to enforce that right, a reference to the CJEU would be needed in order to determine whether Zipvit is in principle entitled to claim a deduction for the VAT element of the original purchase price on the footing that it must now be treated as inclusive of VAT.

87. The position would, however, be different if Royal Mail had no contractual right to recover from Zipvit an amount equivalent to the VAT which should have been charged. In that situation, the judgment of the CJEU in Tulică is clear authority that the price paid for each supply must be treated as VAT-inclusive. That is the consequence of Articles 73 and 78(a) of the Principal Directive, and (in domestic law) of section 19(2) of VATA 1994. Further, since Zipvit has paid the original invoiced prices of the supplies in full, it would clearly have "paid" the VAT element contained in those prices, and there would be no need to consider whether any further payment was "due" from Zipvit in respect of the tax. Accordingly, if that were the correct contractual analysis, I would hold that the first main condition for recovery of the input tax by Zipvit was satisfied.

88. This conclusion would in my judgment be "acte clair" as a matter of EU law, because although Tulică was concerned with the position of a supplier, I can see no reason of principle why the same treatment should not be accorded to the customer, always assuming the case to be one where the supplier has no right to recover any further

amount from the customer. Nor would it matter, in relation to this issue, that Royal Mail has never accounted for the corresponding output tax to HMRC, because the right of deduction is a fundamental feature of the common system of VAT, and the CJEU has consistently said that it is irrelevant whether the tax in question has been paid to the public purse by the supplier.

89. According to my reading of the UT Decision, this was also the conclusion reached by the Upper Tribunal, albeit without the benefit of the further contractual documentation which we have now seen.

90. The position would in my judgment also be the same if, as a matter of contract, the supplies had expressly been agreed to be VAT-inclusive. The contractual position would then have been even more closely aligned with the basic requirements of VAT law, and no question could have arisen whether Zipvit might be liable to pay an additional amount to Royal Mail on account of VAT.

The invoice issue

91. I can now move on to the second main issue in the case, which is (in short) whether the absence of a VAT invoice showing that VAT was charged to Zipvit by Royal Mail, and giving details of the rate of tax and the amount charged, is fatal to Zipvit's claim to recover input tax. I will begin by setting out the statutory framework in which the issue arises.

(a) The Principal Directive

92. Chapter 4 of Title X of the Principal Directive is headed "Rules governing exercise of the right of deduction". The first Article in the chapter, Article 178, provides as follows:

> "In order to exercise the right of deduction, a taxable person must meet the following conditions:
>
> (a) For the purposes of deductions pursuant to Article 168(a), in respect of the supply of goods or services, he must hold an invoice drawn up in accordance with Articles 220 to 236 and Articles 238, 289 and 240;
>
> …"

The deductions which Zipvit wishes to make are all deductions pursuant to Article 168(a), which sets out the substantive conditions for the right to deduct input tax: see [12] above. It will also be noted that the language of Article 178(a) is mandatory: the taxable person *must* hold an invoice drawn up in accordance with the specified Articles.

93. The relevant Article for present purposes is Article 226, which comes under the heading "Content of invoices" in Section 4 of Chapter 3, which is itself entitled "Invoicing". By virtue of Article 220, every taxable person must ensure that an invoice is issued, either by himself or by his customer, in respect of supplies of goods or services which he has made to another taxable person. Article 226 then provides as follows:

> "Without prejudice to the particular provisions laid down in this Directive, only the following details are required for VAT purposes on invoices issued pursuant to Articles 220 and 221:
>
> (1) the date of issue;
>
> (2) a sequential number, based on one or more series, which uniquely identifies the invoice;
>
> (3) the VAT identification number referred to in Article 214 under which the taxable person supplied the goods or services;
>
> (4) the customer's VAT identification number, as referred to in Article 214, under which the customer received a supply of goods or services in respect of which he is liable for payment of VAT…;
>
> (5) the full name and address of the taxable person and of the customer;
>
> (6) the quantity and nature of the goods supplied or the extent and nature of the services rendered;
>
> (7) the date on which the supply of goods or services was made or completed…;
>
> (8) the taxable amount per rate or exemption, the unit price exclusive of VAT and any discounts or rebates if they are not included in the unit price;
>
> (9) the VAT rate applied;
>
> (10) the VAT amount payable, except where a special arrangement is applied under which, in accordance with this Directive, such a detail is excluded;
>
> …"

94. It is also relevant to note Article 219, which states that:

> "Any document or message that amends and refers specifically and unambiguously to the initial invoice shall be treated as an invoice."

95. Finally, Articles 180 and 182 empower Member States to authorise a taxable person to make a deduction which he has not made in accordance with Article 178, and to determine the conditions and detailed rules for application of that provision.

(b) Domestic law

96. The detailed provisions relating to VAT invoices under domestic law are contained in the VAT Regulations 1995. The basic obligation to provide a VAT invoice is contained in regulation 13(1), which states that:

> "Save as otherwise provided in these Regulations, where a registered person –
>
> a) makes a taxable supply in the United Kingdom to a taxable person, or
>
> …
>
> he shall provide such persons as are mentioned above with a VAT invoice…"

Again, it will be noted that this obligation is expressed in mandatory language.

97. The prescribed contents of a VAT invoice are set out in regulation 14, as follows:

> "(1) Subject to paragraph (2) below and regulation 16 and save as the Commissioners may otherwise allow, a registered person providing a VAT invoice in accordance with regulation 13 shall state thereon the following particulars –
>
> (a) a sequential number based on one or more series which uniquely identifies the document,
>
> (b) the time of the supply,
>
> (c) the date of the issue of the document,
>
> (d) the name, address, and registration number of the supplier,
>
> (e) the name and address of the person to whom the goods or services are supplied,
>
> (f) …
>
> (g) a description sufficient to identify the goods or services supplied,
>
> (h) for each description, the quantity of the goods or the extent of the services, and the rate of VAT and the amount payable, excluding VAT, expressed in any currency,
>
> (i) the gross total amount payable, excluding VAT, expressed in any currency,
>
> (j) the rate of any cash discount offered,
>
> (k) ...

(l) the total amount VAT chargeable, expressed in sterling,

…"

98. Regulation 29 deals specifically with claims for input tax, and so far as material provides as follows:

> "(1)…save as the Commissioners may otherwise allow or direct either generally or specially, a person claiming deduction of input tax under section 25(2) of the Act shall do so on a return made by him for the prescribed accounting period in which the VAT became chargeable save that, where he does not at that time hold the document or invoice required by paragraph (2) below, he shall make his claim on the return for the first prescribed accounting period in which he holds that document or invoice.
>
> …
>
> (2) At the time of claiming deduction of input tax in accordance with paragraph (1) above, a person shall, if the claim is in respect of –
>
> (a) a supply from another taxable person, hold the document which is required to be provided under regulation 13 [*i.e. a VAT invoice*];
>
> …
>
> provided that where the Commissioners so direct, either generally or in relation to particular cases or classes of cases, a claimant shall hold or provide such other…evidence of the charge to VAT as the Commissioners may direct."

99. It is the proviso to regulation 29(2), quoted above, which confers a discretion on HMRC, in relation to particular cases, to accept "other evidence of the charge to VAT". In the view of both the FTT and the Upper Tribunal, the discretion could only have been exercised in the present case by refusing to accept the alternative evidence of the charge to VAT provided by Zipvit.

The invoices supplied by Royal Mail to Zipvit

100. Mr Thomas submits, and I would accept, that the invoices which Royal Mail provided to Zipvit purported to be VAT invoices, in the sense that they contained all the information which Royal Mail considered was required by the terms of regulation 14, and they specified the individual supplies as either zero rated or exempt, as Royal Mail then considered them to be. What the invoices obviously did not contain, however, was details of the charge to VAT which should have been added to the contract price (in accordance with the General Terms) on the footing that the supplies were standard rated.

101. Zipvit's basic submission is that the existing invoices should have been treated by HMRC as defective VAT invoices, and the defects were then remedied when the necessary further information was provided to HMRC following the decision of the CJEU in TNT. This submission requires us to examine some of the European case law relating to the provision of VAT invoices.

The relevant EU case law on VAT invoices

102. I will begin with the decision of the Second Chamber of the CJEU in Case C-271/12, Petroma Transport SA and Others v Belgium, [2013] STC 1466, where deductions of input tax were disallowed by the national tax authority on the ground that the invoices relied upon were incomplete and could not be shown to correspond to actual services. The question was whether the refusal to allow the deduction could be upheld when, after the decision had been made, the necessary supplementary information was provided. The Court, which proceeded without an opinion from the Advocate General, dealt with this question as follows:

> "33. The appellants in the main proceedings argue that the fact that the invoices do not contain certain particulars required by national legislation is not such as to call into question the exercise of the right to deduct VAT when the occurrence, nature and amount of the transactions have been subsequently demonstrated to the tax authority.
>
> 34. It should be noted that the common system of VAT does not prohibit the correction of incorrect invoices. Accordingly, where all of the material conditions required in order to benefit from the right to deduct VAT are satisfied and, before the tax authority concerned has made a decision, the taxable person has submitted a corrected invoice to that tax authority, the benefit of that right cannot, in principle, be refused on the ground that the original invoice contained an error…
>
> 35. However, it must be stated that, with regard to the dispute in the main proceedings, the information necessary to complete and regularise the invoices was submitted after the tax authority had adopted its decision to refuse the right to deduct VAT, with the result that, before that decision was adopted, the invoices provided to that authority had not yet been rectified to enable it to ensure the correct collection of the VAT and to permit supervision thereof."

103. The Court therefore held that the decision of the Belgian tax authority to refuse the deductions could not be impugned, even though the necessary corrective information was supplied after the decision had been made. Nevertheless, the Court clearly recognised that at least some deficiencies in incorrect invoices can be made good *before* a decision is taken. The general nature of the deficiencies which were in issue appears from paragraphs 11 and 12 of the judgment. The invoices were rendered within a corporate group, and related to services provided within the group. The problem was that most of the invoices "included an overall amount, with no indication of the unit price or the number of hours worked by the staff of the service-providing

companies, thereby making it impossible for the tax authority to determine the exact amount of tax collected."

104. I now come to the case which Zipvit places at the forefront of its submissions, and which post-dates the UT Decision: Case C-516/14, Barlis 06 – Investimentos Imobiliários e Turísticos SA v Autoridade Tributária e Aduaneira, EU:C:2016:690. The taxpayer company was a hotel operator, which claimed an input tax deduction for supplies of legal services, relying on invoices which stated the dates between which the invoiced services had been rendered, but gave no particulars of the nature of the services. When the Portuguese tax authority took the point that the information provided in the invoices was insufficient, the necessary information was then provided in annexes giving a more detailed description of the relevant legal services. The authority, however, maintained its view that no deduction could be permitted, because the invoices themselves remained defective, and the annexes were not documents equivalent to invoices.

105. The Court began its discussion of the question by considering the purpose of the requirements in Article 226(6) of the Principal Directive. It said at paragraph 27 of its judgment:

> "As the Advocate General observes in points 30, 32 and 46 of her Opinion, the objective of the details which must be shown in an invoice is to allow the tax authorities to monitor payment of the tax due and, if appropriate, the existence of the right to deduct VAT. It is therefore in the light of that objective that it should be examined whether invoices such as the invoices at issue in the main proceedings comply with the requirements of Article 226(6) of Directive 2006/112."

106. After holding that the invoices in their original form did not satisfy the requirements of Article 226(6) and (7), the Court then considered the consequences of the defects for the exercise of the right to deduct VAT. After referring to the fundamental nature of the right to deduct, and stating that it "is exercisable immediately in respect of all the taxes charged on transactions relating to inputs", the Court continued (omitting the citations of earlier authority):

> "39. The deduction system is intended to relieve the operator entirely of the burden of the VAT due or paid in the course of all his economic activities. The common system of VAT therefore ensures that all economic activities, whatever their purpose or results, provided that they are in principle themselves subject to VAT, are taxed a neutral way…
>
> 40. As regards the substantive conditions which must be met in order for the right to deduct VAT to arise, it is apparent from Article 168(a) of [*the Principal Directive*] that the goods or services relied on to give entitlement to that right must be used by the taxable person for the purposes of his own taxed output

transactions and that those goods or services must be supplied by another taxable person as inputs…

41. As regards the formal conditions for the exercise of that right, it is apparent from Article 178(a) of [*the Principal Directive*] that the exercise of the right is subject to holding an invoice drawn up in accordance with Article 226 of that directive…

42. The Court has held that the fundamental principle of the neutrality of VAT requires deduction of input VAT to be allowed if the substantive requirements are satisfied, even if the taxable persons have failed to comply with some formal conditions. Consequently, where the tax authorities have the information necessary to establish that the substantive requirements have been satisfied, they cannot, in relation to the right of the taxable person to deduct that tax, impose additional conditions which may have the effect of rendering that right ineffective for practical purposes…

43. It follows that the tax authorities cannot refuse the right to deduct VAT on the sole ground that an invoice does not satisfy the conditions required by Article 226(6) and (7) of [*the Principal Directive*] if they have available all the information to ascertain whether the substantive conditions for that right are satisfied.

44. In this respect, the authorities cannot restrict themselves to examining the invoice itself. They must also take account of the additional information provided by the taxable person. That conclusion is confirmed by Article 219 of [*the Principal Directive*], which treats as an invoice any document or message that amends and refers specifically and unambiguously to the initial invoice.

45. In the dispute in the main proceedings, it is therefore for the referring tribunal to take into account all the information included in the invoices at issue and in the annexes provided by Barlis in order to ascertain where the substantive conditions for its right to deduct VAT are satisfied.

46. In this connection, it must be pointed out, first, that it is for the taxable person seeking deduction of VAT to establish that he meets the conditions for eligibility… The tax authorities may thus require the taxable person himself to produce the evidence they consider necessary for determining whether or not the deduction requested should be granted."

107. In reliance on these principles, Zipvit argues that its letter of claim dated 15 September 2009 provided HMRC with all the further information which they needed in order to supplement the details provided in the original invoices. The letter referred to an enclosed schedule, which gave a figure for "gross postage" for each quarter, with a corresponding figure for the VAT claimed (on the basis that the gross postage should be treated as VAT-inclusive, although this was not explicitly stated). The letter said that the figures had been provided by Zipvit from its records of monthly postage charges, and that the records were available for HMRC to inspect if they so required. Accordingly, says Zipvit, it was not open to HMRC to refuse deduction of the input tax claimed.

108. At first sight, the decision in Barlis may appear to provide some support for Zipvit's case. But the facts could hardly have been more different. The only defects in the relevant invoices were that they did not provide a proper description of the legal services which had been supplied, and thus did not comply with Article 226(6) and (7) which required details of "the extent and nature of the services rendered" and the date on which the supply had been made or completed. There was no reason to doubt that the corresponding output tax had been paid by the lawyers, nor was there any doubt about its chargeable rate and amount. In the present case, by contrast, the original invoices issued by Royal Mail to Zipvit described the supplies as exempt, and Zipvit has been wholly unable to provide any evidence that tax on the supplies was paid or accounted for by Royal Mail when it became clear that the supplies were in fact standard rated. Zipvit is therefore claiming to be entitled to exercise its right to deduct without being able to produce either a compliant VAT invoice, or supplementary information which shows that the conditions of Article 226(9) and (10) are satisfied, that is to say details of "the VAT rate applied" and "the VAT amount payable", coupled with evidence of payment of that amount by Royal Mail.

109. In her opinion in Barlis, Advocate General Kokott said at paragraph 30 that the purpose of requiring a specific detail in a VAT invoice depends on the function which an invoice has to fulfil in the scheme of VAT. She then said:

> "As follows from recital 46 of the [*Principal Directive*], issuing invoices allows the tax authorities of the Member States to carry out their monitoring activities."

She added in paragraph 31:

> "In the light of this aim, the purpose of each individual detail in an invoice is directly connected with the question as to what the tax authorities ought to be able to monitor on the basis of an invoice."

110. Under the heading "(i) Monitoring payment of the correct tax", Advocate General Kokott continued:

> "32. An invoice is intended first to enable a check on whether the person issuing the invoice [*i.e. the supplier*] has paid the tax.

> 33. This follows from Article 178(a) of the [*Principal Directive*]. It provides that in order to exercise the right of deduction, the recipient of a supply must hold an invoice. According to the case-law, this requirement is intended to ensure that VAT is levied and supervised. This is because, pursuant to this provision, deduction of input tax is allowed only if, in the form of the invoice, the tax authority can at the time obtain access to a document which, because of the particulars required by Article 226 of the [*Principal Directive*], contains the information necessary to ensure the corresponding payment of VAT by the person who issued the invoice. This access to the person who issued the invoice is supported by Article 203 of the [*Principal Directive*]. According to it, the VAT shown in an invoice is payable by the person who issued it, regardless of whether a liability to tax has actually arisen, and in particular of whether any supply has actually been made. In such cases this saves the tax authority from requiring other evidence.
>
> 34. So the invoice is a type of insurance for the fiscal authority, in that in a certain sense it links the input tax deduction to payment of the tax…"

111. The second monitoring activity described by Advocate General Kokott was "Monitoring the right of deduction", in relation to which she said at paragraph 46:

> "In addition, the invoice and its contents do not merely enable payment of the correct tax by the person who issued it to be monitored. As likewise appears from the legislative history of Article 226 of [*the Principal Directive*], the invoice is intended to fulfil the function of "proving" its recipient's right of deduction."

112. I have referred to these parts of the Advocate General's opinion because they were expressly endorsed by the Court in paragraph 27 of its judgment. I have already quoted that paragraph, but will repeat the critical sentence:

> "As the Advocate General observes in points 30, 32 and 46 of her Opinion, the objective of the details which must be shown in an invoice is to allow the tax authorities to monitor payment of the tax due and, if appropriate, the existence of the right to deduct VAT."

Properly understood, therefore, the decision of the Court in Barlis appears to me to expose a fatal flaw in Zipvit's case. One of the main purposes of the mandatory requirement for a VAT invoice is to enable the taxing authorities to monitor payment by the supplier of the tax for which a deduction is sought, or as the Advocate General

put it "to enable a check on whether the person issuing the invoice has paid the tax." Zipvit remains wholly unable to satisfy this condition, because the only invoices which it can supply show the complete opposite, namely that no tax was paid because the supplies were considered to be exempt. Nor can it be said that the position was remedied by the exiguous further information supplied with the letter of claim in September 2009. All this did was to show the VAT component of the original purchase prices, on the assumption that the supplies were taxable. It provided no evidence that a penny of that tax had been paid by Royal Mail to HMRC, and still less did it do so in the form of an invoice issued by Royal Mail.

113. Mr Thomas argues that none of this matters, because Zipvit was entitled to exercise its right to deduct input tax referable to the supplies which it made to its own customers, on which it accounted for output tax in the usual way. To deny a deduction on the sole basis that Royal Mail cannot be shown to have paid tax on the relevant supplies which it made to Ziptvit is, he submits, to rely on a wholly irrelevant consideration, because it would offend the well-established principle that the right of deduction is unaffected by the question whether VAT due at an earlier stage in the chain of supply has been paid to the public purse. In my view, however, this objection misses the point. Exercise of the right to deduct is subject to a mandatory requirement to produce a VAT invoice, which must contain the specified particulars. Zipvit is unable to produce invoices which satisfy the requirements of Article 226(9) and (10), and it is also unable to produce any supplementary evidence showing payment of the relevant tax by Royal Mail. A necessary precondition for exercise of the right to deduct therefore remains unsatisfied.

114. I also fail to see how Zipvit could hope to circumvent this fundamental difficulty by arguing that the requirement for a compliant VAT invoice is one of form rather than substance, and by invoking the discretion which HMRC have to accept alternative evidence under regulation 29(2) of the 1995 Regulations. It is true that Barlis (at paragraphs 40 and 41), and a number of other cases which we were shown, consistently draw a distinction between the substantive conditions which must be met in order for the right to deduct VAT to arise, and the formal conditions for the exercise of that right. But to describe a requirement as "formal" does not necessarily imply that compliance with it is optional, or that a failure to satisfy it is always capable of being excused. Cases like Barlis show that some of the requirements relating to invoices in Article 226 must be dispensed with, if the tax authorities are supplied with the information necessary to establish that the substantive requirements of the right to deduct are satisfied. But the Court was careful in Barlis to confine its discussion to the requirements in Article 226(6) and (7), and I do not think its reasoning can be extended to cover a failure to comply with the fundamental requirements relating to payment of the relevant tax in Article 226(9) and (10). Provision of an invoice which complies with those requirements is essential to the proper performance by HMRC of their monitoring functions in relation to VAT, and is needed as evidence that the supplier has duly paid or accounted for the tax to HMRC.

115. It needs to be remembered in this context that the amounts for which Zipvit is claiming a deduction have not been paid by Zipvit in response to a request by Royal Mail for payment once the taxable status of the supplies had been established. In that situation, Royal Mail would have rendered an invoice showing the VAT due, and

would then have been liable to account for it to HMRC as output tax in the usual way. In those circumstances, there would have been no difficulty about Zipvit deducting the amount shown on the new invoice as input tax. All that has actually happened, however, is that Zipvit now wishes to treat the payments which it originally made to Royal Mail, on the common understanding that the supplies were exempt, as comprising an element of VAT, and to obtain a deduction for that element on the strength of nothing more than the original payment.

116. Even if it is open to Zipvit to recharacterise the original payment in this way (which at this stage of the argument must be assumed in Zipvit's favour), there would be an obvious detriment to HMRC and the public purse if Zipvit were able to obtain such a deduction without first showing that the tax in question had been paid by Royal Mail. The normal way of fulfilling that obligation is by production of a fully compliant VAT invoice. Since Zipvit is unable to produce such an invoice, I am unable to see any grounds upon which HMRC could properly conclude that Zipvit should nevertheless be allowed the deductions claimed, to the detriment of the general body of taxpayers. In effect, a retrospective recharacterisation of sums originally paid on the footing that the supplies in question were exempt would now yield an uncovenanted bonus to Zipvit, generated by nothing more than Zipvit's unilateral decision to treat the amounts originally paid as VAT-inclusive. It would, I think, be offensive to most people's sense of fiscal justice if a mechanical accounting exercise of this nature were permitted to generate a very substantial input tax credit, in circumstances where (for whatever reason) none of the tax in question has been paid by the supplier.

117. Whether the situation is described as one in which HMRC have no discretion, because the requirements of Article 226(9) and (10) cannot be dispensed with, or as one where there is in law a discretion but on the facts of the present case it can only be exercised in one way, does not seem to me to matter. The important point is that the inability of Zipvit to produce a compliant VAT invoice in support of its claim to deduct input tax is in my judgment fatal. This was rightly recognised by the two Tribunals below, although I would (with respect) not adopt their analysis of the position in terms of the absence of an "economic burden" on Zipvit. That way of looking at the matter seems to me misconceived, because Zipvit did bear the economic burden of paying the original purchase price for the supplies. The real issue, as I see it, is whether Zipvit can claim a deduction for VAT by treating the original price as VAT-inclusive, without producing evidence that the tax in question has been duly paid by the supplier.

118. My conclusion also makes it unnecessary to resolve the question, as a matter of EU law, whether the requirements of Article 226(9) and (10) should be treated as both formal and substantive, in the sense that compliance with them is essential to a valid exercise of the right to deduct input tax. There are passages in the interesting discussion by Advocate General Kokott in Biosafe which would lend support to such a conclusion, and it seems to me that the law may well develop in that direction. As Mr Thomas rightly points out, however, this reasoning was not adopted by the CJEU in its judgment, which was able to decide the case on grounds which did not require a re-examination of the existing law on the right to deduct. The same is true of the Court's decision in Volkswagen, which repeats the now familiar jurisprudence of the Court on the principles which govern the right to deduct: see the judgment at

paragraphs 36 to 42. Put negatively, I am satisfied that no support can be found in either case for the proposition that a right to deduct may be recognised and given effect without production of a VAT invoice showing that the tax in question has been paid by the supplier.

119. Finally, I should make it clear that the need for a VAT invoice which complies with Article 226(9) and (10) is in my judgment fatal to Zipvit's claims, whether or not the new contractual material is admitted, and whether or not the original purchase price was agreed to be inclusive of VAT. It also follows that it is unnecessary to make a reference to the CJEU on the first main issue, because all the claims must anyway fail on the second issue.

Overall conclusion

120. For these reasons, therefore, which differ in some significant respects from those given by the Tribunals below, I would dismiss Zipvit's appeal.

Asplin LJ:

121. I agree.

Dame Elizabeth Gloster, DBE:

122. I also agree.