[2015] UKFTT 0173 (TC)

TC04367

Appeal number: TC/2014/03258

VALUE ADDED TAX – supply – provision of clothing free of charge to store staff – whether business purpose constituted grounds to except transaction from treatment as a supply – no – whether clothing constituted uniform – no – lack of significance of latter question – whether provision of clothing constituted business gifts – question not relevant for goods of more than £50 in value – whether value of supply should take account of conditions on which clothing supplied to staff – no – valuation to be based on cost of buying equivalent goods at time of supply – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

FRENCH CONNECTION LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE JOHN CLARK
SHAMEEM AKTAR

Sitting in public at The Royal Courts of Justice on 26 February 2015

Ian Morgan, Morgan & Co, Chartered Accountants, for the Appellant

Erika Carroll, Appeals and Reviews, HM Revenue and Customs, for the Respondents

DECISION

1. The Appellant ("FCL") appeals against a decision of the Respondents ("HMRC"), confirmed on subsequent review, that the provision of clothing to staff free of charge is a taxable supply for VAT purposes.

The background facts

2. The evidence consisted of a bundle of documents, including witness statements given on behalf of FCL by Stephen Marks and Simon Donoghue. In addition, Mr Marks and Mr Donoghue gave oral evidence.

3. From the evidence we find the following background facts; we consider other factual questions at a later point in this decision.

4. FCL is the representative member of a VAT group consisting of French Connection Group PLC ("FC PLC") and subsidiaries. The principal retailer in the group is French Connection UK Ltd, to which we refer in this decision as "FC". The merchandise is sold under the "French Connection" label.

5. In the course of a VAT audit which began in the latter part of 2013, HMRC raised the question of the treatment of the issue by FC of clothing to staff.

6. The terms on which clothing was provided were, in summary, that staff members were provided with a clothing allowance (referred to in the documentation as "an employee uniform allowance") for the particular season; this enabled them to choose items from FC's stock up to the amount of the allowance. They were required to wear such clothing when working, and had also to wear a magnetic badge identifying the wearer as a FC staff member. If a staff member left within three months of the start of that new season, there was no requirement to return the clothing, but the staff member's pay would be reduced by 30 per cent of the clothing allowance used. (At a later point in this decision we examine in more detail the terms and conditions of these arrangements.)

7. In continuing correspondence, in particular a letter from the HMRC officer, Mr Jemson, dated 10 March 2014, HMRC indicated their view that where clothing was supplied to staff and no consideration was received by FC, this was a supply of goods for VAT purposes and therefore output tax was due in respect of that supply.

8. On 26 March 2014 Mr Castleton, the Finance Director of FC PLC, requested an independent review of the decision in HMRC's letter dated 10 March 2014.

9. At some point in later March 2014, HMRC issued assessments for output tax undeclared on free of charge clothing. These assessments took into account reductions in the quarterly amounts where the amount per person did not exceed £50.

10. Mr Castleton wrote to Mr Jemson on 10 April 2014 to ask why he had not deducted from the amounts assessed the charges actually paid by staff members for clothing that had initially been supplied to them without charge, where they had left employment within three months of the start of the selling season. In an email dated 14 April 2014, HMRC indicated that they would reduce the assessment to take account of the payments made by staff members in the circumstances described.

11. The amount originally assessed in March 2014 was £51,663.00. The revised amount shown in the amended assessment calculated on 25 April 2014 was £35,724.00.

12. On 1 May 2014, Mr Castleton wrote to HMRC to give formal notice of appeal against the assessments.

13. On 13 May 2014, Mrs Champion, the HMRC Review Officer dealing with FCL's case wrote to Mr Castleton with the results of her review. (This letter was in exactly the same terms as a letter from her on the same subject dated 25 April 2014, also contained in the bundle; we assume that the latter was written in response to the request made by Mr Castleton on 26 March 2014, and that it did not constitute a formal review because it was written before FCL had given formal notice of appeal to HMRC.) Her conclusion was that the decision contained in the letter dated 10 March 2014 should be upheld. She set out detailed reasons for her conclusion. (As these matters were considered in the course of the appeal hearing, we do not set them out here; we refer below to the points raised by HMRC in support of their contention that FCL's appeal should be dismissed.)

14. On 12 May 2014, FCL gave Notice of Appeal to HM Courts and Tribunals Service.

The legislation

15. The main UK legislative provisions referred to by the parties were paragraph 5(1) of Schedule 4 to the Value Added Tax Act 1994 ("VATA 1994") and para 6(2)(a) Sch 6 VATA 1994. These are as follows:

> "**Schedule 4**
>
> **Matters to be treated as supply of goods or services**
>
> 5(1) Subject to sub-paragraph (2) below, where goods forming part of the assets of a business are transferred or disposed of by or under the directions of the person carrying on the business so as no longer to form part of those assets, whether or not for a consideration, that is a supply by him of goods."
>
> **Schedule 6**
>
> **Valuation: special cases**
>
> 6(1) Where there is a supply of goods by virtue of—

(a) . . . ; or

(b) paragraph 5(1) or 6 of Schedule 4 but otherwise than for a consideration); or

. . .

then, . . . , the value of the supply shall be determined as follows.

(2) The value of the supply shall be taken to be—

(a) such consideration in money as would be payable by the person making the supply if he were, at the time of the supply, to purchase goods identical in every respect (including age and condition) to the goods concerned; or

. . . "

16. In addition, reference was made to Article 16 of European Council Directive 2006/112/EC, generally cited as the Principal VAT Directive ("PVD"):

"**Article 16**

The application by a taxable person of goods forming part of his business assets for his private use or for that of his staff, or their disposal free of charge or, more generally, their application for purposes other than those of his business, shall be treated as a supply of goods for consideration, where the VAT on those goods or the component parts thereof was wholly or partly deductible.

However, the application of goods for business use as samples or as gifts of small value shall not be treated as a supply of goods for consideration."

Arguments for FCL

17. Mr Morgan referred to the background to the dispute between FCL and HMRC. He accepted that all "uniform clothing" provided by FC had to be treated as supplies of goods on which output tax was required to be paid, unless FCL could demonstrate that the supplies were not to be treated as supplies for consideration.

18. He submitted that HMRC had assessed FCL to output tax on the basis that the supplies of uniform clothing by FC were a series of "business gifts"; this was disputed by FCL.

19. FCL maintained that FC provided uniform clothing to its retail store staff, without charge at the time of supply, for the purposes of its business.

20. On this basis, FCL's submission was that the provision of uniform clothing should not be treated as supplies of goods for consideration on which output tax was payable. In support of this submission, Mr Morgan relied on the terms of Article 16 PVD. We consider this in detail at a later point below.

21. If, contrary to the above submission, the Tribunal found that the provision of uniform clothing should be treated as taxable supplies, then the question that followed

was, what was the value of the consideration for the uniform clothing on which output tax was payable?

22. On the latter question, FCL's submission was that the contractual conditions of use of uniform clothing, and the possible retrospective charge, imposed by FC on its retail store staff at the time of supply meant that at the time of supply the value of the goods supplied was unascertainable or *de minimis*.

23. Mr Morgan produced a flow chart "decision tree", with a series of questions as follows:

> (1) Was uniform clothing supplied by FC free of charge to its retail store staff provided for the purposes of its business? If the answer was "yes", the result would be that no output tax was payable, and the appeal should be allowed. If "no", the following question should be considered.
>
> (2) Should uniform clothing supplied by FC free of charge to its retail store staff be treated as their "uniform"? If the answer was "yes", the outcome should be that no output tax was payable, and the appeal should be allowed. If "no", the following question should be considered.
>
> (3) Should uniform clothing supplied free of charge to its retail store staff be treated as a series of "business gifts? If the answer was "yes", the suggested outcome was that output tax was payable on the equivalent cost of purchasing clothing identical in every respect to that supplied by FC free of charge to its staff, excluding "business gifts" consisting £50 or less (excluding VAT) to the same recipient in the same year. If the answer was "no", this meant considering the following question.
>
> (4) Was the cost of purchasing clothing identical in every respect to that supplied by FC free of charge to its staff ascertainable at the time of supply? If "yes", the suggested outcome was that output tax was payable on the equivalent cost of purchasing clothing identical in every respect to that supplied by FC free of charge to its staff. If the answer was "no", the suggested answer was that no output tax was payable and that the appeal should be allowed.

24. Mr Morgan submitted that the principles enshrined in Article 16 PVD must be applied in interpreting paragraph 5(1) of Schedule 4 to the Value Added Tax Act 1994 ("VATA 1994").

25. In relation to his third question, he referred to the definition of "business gifts" in para 5(2ZA) Sch 4 VATA 1994. On the meaning of "gift", he referred to the following cases: *Howard v Fingall* (1853) 22 LTOS 12, *Roberts v Roberts* (1865) 13 LT 492, and *Leary v Federal Commissioner of Taxation* 91980) 11 ATR 145.

26. In the context of his first question, he referred to HMRC's guidance at paragraph 4.4 of VAT Notice 700, which stated:

> "You do **not** make a supply if you provide goods (such as overalls or tools) to employees solely for the purposes of their employment and make no charge."

27. He submitted that this official guidance mirrored Article 16 PVD, which treated the disposal of goods for non-business purposes as a supply of goods, in the same way that para 5(4) Sch 4 VATA 1994 treated the application of goods for non-business purposes as a supply of services.

28. On the question of valuation, he referred to the application of para 6(2)(a) Sch 6 VATA 1994; did the conditions of use of uniform clothing imposed by FC on its retail store staff mean that, at the time of its supply, such clothing had no ascertainable value?

29. He emphasised the difference between purposes and effects. The purposes were the intentions in the corporate mind of FC. He referred to *Sweet v Parsley* [1969] 1All ER 347 and the consideration of "purpose". Here, the purpose was that of FC and not of its retail store staff.

30. He also referred to *Zoo Clothing Ltd v Customs and Excise Commissioners* (1992) VAT Decision 9161. The guidance from this case was doubtful, as the appellant had not appeared, had not presented any evidence, and had not been represented. He submitted that the income tax cases which had been relied on by HMRC were not relevant; in the present case, the staff did not incur expenditure on clothing. He referred to comments of Lord Reid in *Strick v Regent Oil Co Ltd* (1965) 43 TC 1 at 29 concerning the application of statements to different kinds of case.

31. HMRC had cited a case under the name of *JK Hill*. There were two reports relating to cases with this name: the first, *JK Hill and SJ Mansell (t/a JK Hill and Co) v Commissioners of Customs and Excise* (1987) was a decision of the London VAT Tribunal under the file reference LON/86/472Z, and the second, *Hill and another (trading as JK Hill & Co) v Customs and Excise Commissioners* [1988] STC was the appeal to the High Court. Simon Brown J considered an appeal against only one of the decisions taken by the VAT Tribunal. Thus the question of input tax on clothing was not before him, as no appeal had been made against that decision. In the present case, the question was whether output tax was due.

32. Mr Morgan also referred to *Bridget Jennifer Brown* (1991) VAT Decision 6552. This was another input tax case, and no evidence had been called in support of the appeal.

33. In relation to Article 16 PVD, he made detailed submissions concerning its interpretation and its effect in the context of para 5(1) Sch 4 VATA 1994. As these questions are central to the arguments for FCL, we consider them separately below.

34. Mr Morgan made various submissions in relation to factual matters; we consider these, together with those made by HMRC, in a later section of this decision.

Arguments for HMRC

35. Mrs Carroll stated the point at issue in the appeal. This was whether FCL could demonstrate that clothing given to staff was not a taxable supply for VAT purposes,

or if it was a taxable supply, when the supply was made and what its value was at that time.

36. There was no dispute that—

(1) the clothing was provided to staff free of charge;

(2) title passed when the staff member first took the clothing;

(3) the value should be determined as per para 6(2)(a) Sch 6 VATA 1994.

37. HMRC submitted that the provision of clothing to staff involved a supply as provided for by para 5(1) Sch 4 VATA 1994, whether or not for a consideration. As the title in the goods passed to the staff member when the items were taken, FCL accepted that para 6(2)(a) Sch 6 VATA 1994 applied. In HMRC's submission, this provision effectively valued goods at cost price. This had been the basis of the assessment made on FCL by HMRC.

38. FCL argued that the value of the goods was unascertainable due to the conditions on which they were provided, including the retrospective charge if the staff member were to leave within three months. HMRC's argument was that the conditions of use were irrelevant; the time of supply was when the staff member took the clothing, and at that point it would be brand new. This would enable the clothing to be valued on that basis pursuant to para 6(2)(a) Sch 6 VATA 1994.

39. In relation to the retrospective charge, it could not be right that a supply was deliberately devalued just in case a staff member were to leave in the future.

40. HMRC were not arguing that the provision of clothing to staff amounted to "business gifts"; it just happened that the transactions in question fell under the same heading as that under which business gifts were dealt with. It was irrelevant whether the transaction fell within the "business gift" description; it had to be a taxable supply. The assessment had been reduced; Mrs Carroll believed that HMRC had used their discretion at the time to do so.

41. Mrs Carroll made submissions concerning the effect of Article 16 PVD in the context of FCL's submissions; HMRC did not agree with the arguments on this question being put for FCL. (We deal with both parties' submissions together at a later point in this decision.)

42. One of FCL's main arguments was that the clothing constituted a uniform. Mrs Carroll submitted that there was nothing in VATA 1994 which prevented the supply of a uniform from being a supply of goods. The inference derived by Mr Morgan from *Zoo Clothing* was incorrect and not contained in the decision. In HMRC's submission, whether or not the clothing was a uniform was irrelevant.

43. If clothing passed into the ownership of an employee (so that title passed), it was HMRC's case that this was a taxable supply. If title did not pass, in other words that the clothing was loaned throughout, this might not be a supply of goods. This very much depended on the terms and conditions of the employment.

44. Although the question of a "uniform" was in HMRC's view irrelevant, Mrs Carroll made submissions concerning what might or might not constitute a uniform. As these matters relate to the factual issues, we consider them together with the wider factual questions at the appropriate point below. HMRC had cited the *Zoo Clothing* decision, which was thought to be the only VAT case involving clothing and uniforms; it appeared to be very similar to FCL's case.

45. In summary, in HMRC's submission, the legislation was clear; the transfer of business assets, whether or not for a consideration, was a taxable supply of goods. On the facts of the case, assets of the business were supplied to staff members, and VAT was due accordingly. HMRC submitted that the appeal should be dismissed.

Discussion and conclusions

46. In order to consider the arguments for FCL, and the responses from HMRC to those arguments, we review first the issues of law, to put us in a position to establish the relevance and significance of the facts.

(a) The legal issues

47. The specific UK VAT charging provision in question in this appeal is para 5(1) Sch 4 VATA 1994 (see text above). We did not understand Mr Morgan on behalf of FCL to doubt the application of this sub-paragraph in the context of FC providing clothing to its staff. Before we consider his arguments as to the effect of Article 16 PVD, we examine the language of para 5(1).

48. The first condition for para 5(1) to apply is that the goods in question are "goods forming part of the assets of a business". The second is that goods within that category are transferred or disposed of by (or under the directions of) the person carrying on the business. The third is that, as a result of the transfer or disposal, the goods no longer form part of the assets of the business.

49. If all those conditions are met, then, whether or not the transfer or disposal is for a consideration, the transaction is treated as a supply of goods by the taxable person.

50. There are exceptions within para 5(2), which states that para 5(1) does not apply where the transfer or disposal is a business gift the cost of which when added to that of any other business gifts made to the same person in the same year does not exceed £50. (The other exception, not relevant in the present context) is for the provision of samples of goods to persons otherwise than for a consideration.

51. Thus the concept of "business gifts" is not part of the charging provision; instead, it forms part of a limited exception from the full effect of that charging provision.

52. Mr Morgan's argument for FCL was that FC provides uniform clothing to its retail store staff, without charge at the time of supply, *for the purposes of its business* [his emphasis]. On that premise, he submitted that such provision of clothing should

not be treated as supplies of goods for consideration, on which output tax was payable. The basis for his submission was Article 16 PVD.

53. He argued that the imputation of consideration applied only where the transaction in question was for purposes other than those of FC's business. This proposition was to be derived from the language of Article 16 PVD.

54. Mr Morgan referred to para 5(4) Sch 4 VATA 1994, which made references to "goods held or used for the purposes of the business" and ". . . used, or made available to any person for use, for any purpose other than a purpose of the business." He submitted that this properly reflected the effect of Article 16 in its reference to ". . . purposes other than those of his business", and should be contrasted with para 5(1), which made no similar reference.

55. Mrs Carroll indicated that HMRC did not agree with FCL's arguments as to the effect of Article 16 PVD. In linguistic terms, Article 16 went through a series of "ors", not "ands" as Mr Morgan was seeking to suggest; business was not the only consideration. On HMRC's reading, Article 16 was to be read in the following way: "The application . . . or disposal free of charge shall be treated as a supply of goods for consideration, where the VAT on those goods . . . was wholly or partly deductible." Thus a supply in such circumstances was a supply of goods; Article 16 PVD had been enacted in the UK VAT legislation as para 5 Sch 4 VATA 1994.

56. In interpreting a European provision such as Article 16 PVD, we think that there may be some advantage in first standing back and looking at what appears to be its underlying policy, before engaging in the exercise of examining closely the precise language employed. A broader purposive approach appears more consistent with the general tenor of European legislation.

57. Article 16 is dealing with the subject of goods forming part of a taxable person's business assets, in circumstances where the VAT (ie input tax) on those goods was wholly or partly deductible. It concerns the process of the goods being "taken out" of the business, whether merely by being applied to the private use of the taxable person or that of his staff, being given away, or applied for non-business purposes. In such cases, there is a form of "VAT exit charge" when goods are "taken out" in this way; in effect, this neutralises the input tax recovery on those goods, and prevents or the taxable person from benefiting from the input tax recovery and yet subsequently escaping from the charge to VAT at the point where the goods are taken out of the business. The effect of Article 16 appears therefore to be the achievement of neutrality in such a context.

58. On that basis, is there a reason for different treatment where the goods can be shown to have been dealt with or applied in some way for business purposes? We find it difficult to see any policy basis for different treatment in such circumstances. If goods are "taken out" of the business as described above, they will have had the benefit of input tax recovery, and if they are exempted from any charge to output tax when they "leave" the business, that business will derive some form of benefit by not suffering that charge. We accept that, in circumstances where a business provides

goods free of charge, the business has borne the cost of acquiring or producing those goods, but in our view this does not affect the VAT analysis.

59. Thus, in terms of the apparent policy underlying Article 16 PVD, we do not consider that it is intended to provide any form of exemption from a charge to output tax where goods are provided free of charge to members of staff, even in circumstances where the provision of those goods is clearly established to be for the purposes of the taxable person's business.

60. We turn now to the language of Article 16 (for the full text, see above). On our reading, it provides for three broad eventualities, in cases where there has been complete or partial input tax recovery in respect of the relevant goods:

> (1) The application by a taxable person of goods forming part of his business assets for his private use, or for that of his staff;
>
> (2) The disposal free of charge of goods forming part of the taxable person's business assets;
>
> (3) The application of goods forming part of the taxable person's business assets for purposes other than those of his business.

61. We regard these three elements of Article 16 as separate. The only relevance of business purposes is in relation to the third element. We do not regard it as permissible to read into the second element any qualification concerning the purposes of the taxable person's business. That second element is the one which we consider to be relevant to FCL's appeal.

62. Article 16 also contains exemptions for business samples and business gifts of small value.

63. On our reading of Article 16 PVD, we regard the corresponding UK legislation (para 5 Sch 4 VATA 1994) as entirely consistent with, and therefore (at least in the present context) a full implementation of, Article 16.

64. Mr Morgan referred to the different wording in para 5(4) Sch 4 VATA 1994. As this refers to a supply of services, it is not appropriate to refer to Article 16 PVD. Instead, it derives from Article 26 PVD, paragraph (1)(a) of which relates to the private use of goods forming part of the assets of a business or their use for purposes other than those of the business. In Article 26 and para 5(4) Sch 4 VATA 1994, the circumstances in question are where goods that have qualified for input tax recovery and continue to be owned by the business are permitted to be used for some non-business purpose; in that event, this is treated as a supply of services. Article 26(1)(a) deals with two elements, not three as are to be found in Article 16.

65. Neither Article 26 nor para 5(4) Sch 4 VATA 1994 contain anything corresponding to the second element of Article 16. Thus they provide no assistance in determining whether Article 16 is to be read as subject to a qualification that, as Mr Morgan argues for FCL, a free of charge disposal to a staff member made for the

purposes of the business of the taxable person is not to be treated as a supply of goods for consideration.

66. In our view, there is no basis on which any such qualification can be read into Article 16 PVD, and thus there are no grounds for any suggestion that Article 16 has not been implemented by the enactment in the UK of para 5 Sch 4 VATA 1994.

67. We are satisfied that, whether Article 16 is interpreted on the basis of a purposive construction or by reference to its language, the result is the same; there is no basis for restricting its operation in a case where there has been full or partial recovery of input tax on particular goods and those goods are disposed of free of charge by the taxable person.

68. This explains the need for the final part of Article 16; it provides an exception for the application of goods for business use as samples or as gifts of small value. It takes into account that there may be a commercial need to distribute promotional samples or small gifts. For this reason, the sentence refers to "business use". This recognises that a free of charge disposal can be for business purposes, and that in these limited circumstances it is appropriate for that disposal to be exempted from treatment as a supply of goods for consideration.

69. It follows that the existence of a business purpose (or more than one such purpose) does not of itself remove a free of charge disposal from treatment as a supply of goods for consideration if that disposal does not meet the conditions of the final sentence of Article 16. In other words, if what is provided free of charge is not a sample or a gift of small value, there is no basis for the transaction to be taken out of the main charging provision. It is treated as a supply of goods for consideration, even though it is made for the purposes of the business.

70. Mr Morgan argued that if the Tribunal found as a fact that the provision of clothing by FC free of charge to its staff was for the purposes of FC's business, HMRC should apply its official guidance at paragraph 4.4 of VAT Notice 700 and should not assess FCL to output tax on supplies of uniform clothing provided without charge by FC to its retail store staff for the purposes of its business.

71. We have considered the guidance set out by HMRC at paragraph 4.4 of Notice 700. Mr Morgan referred to the final sentence of that paragraph (see paragraph [26] above) indicating the circumstances in which a trader would not be regarded as making a supply. However, we read this sentence as coming within a particular, limited context.

72. Paragraph 4.4 begins with the following general statement:

> "You supply goods if you pass the exclusive ownership of movable items to another person."

It then refers to other circumstances in which a trader is regarded as supplying goods. The sentence quoted by Mr Morgan follows at the end of the paragraph.

73. In our view, the statement at the beginning reflects the effect of the law, ie Article 16 PVD and the corresponding UK statutory provision, para 5 Sch 4 VATA 1994. If the trader passes the ownership of the goods to another person, that transaction is treated as a supply of the goods.

74. It follows that the final sentence in paragraph 4.4 of Notice 700 cannot be dealing with a situation where the ownership of the goods has passed to another person. What is contemplated is a situation in which the trader owns goods such as overalls or tools, and provides them free of charge to employees solely for the purposes of their employment. This is not regarded as a supply; in other words, no "hire charge" is deemed to be made. This appears to us to reflect Article 26 PVD, and correspondingly para 5(4) Sch 4 VATA 1994. This final sentence provides no assistance in a case where the items in question have been transferred into the ownership of employees, even where it can be established that those items have been provided to the employees solely for the purposes of their employment.

75. FCL's first question as set out at paragraph [23] above is based on the fundamental assumption that the "purposes of the business" qualification forms part of the applicable legislation. We have concluded that this assumption is incorrect. We therefore turn to the legal issues involved in FCL's second question, relating to "uniform".

76. In Mrs Carroll's submission, whether or not the clothing was a uniform was irrelevant; Mr Morgan's argument for FCL is that the clothing was a uniform and not a business gift and was only supplied as specified in the staff members' terms of employment.

77. Mr Morgan commented that there was a dearth of "uniform" cases, and that the cases under consideration were ones where there had been no appearance by the appellant. In *Zoo Clothing*, the trader did not present any evidence and did not explain the purposes of the requirement that the staff should wear as uniform clothes supplied by the company. In that case, Customs had relied on *Mallalieu v Drummond* [1983] STC 665; Mr Morgan submitted that the VAT legislation required examination not of the purposes of the employee but instead the purposes of the trader, here FC.

78. He submitted that in *Zoo Clothing*, there was a clear inference that if the Customs officer had regarded the clothing as uniforms, there would have been no charge to output tax.

79. Mrs Carroll commented that as far as HMRC were aware, this was the only VAT case relating to clothing and uniforms; it was very similar to FC's situation. The Tribunal had said in the penultimate paragraph of its decision:

> "With regard to the issue of uniforms, again the Appellant Company has produced no evidence of the basis on which the clothing alleged to be uniforms was given or supplied to employees Specific questions were asked on it by the Respondent Commissioners on 28th October 1991 but no further evidence was given. Accepting what the Appellant Company says on this subject that there is a contractual obligation on

> employees of the Appellant Company to wear clothes from the stock held for sale by the Appellant Company this information does not allow the tribunal to conclude that there was here a disposal of the stock of the Appellant Company other than by a transaction which should have attracted tax."

80. Mrs Carroll argued that there was nothing in VATA 1994 which prevented the supply of a uniform from being a supply of goods. The inference derived by FCL from *Zoo Clothing* was not correct and not to be found in that decision. In HMRC's submission, whether or not the clothing was a uniform was irrelevant.

81. We consider that the Tribunal in *Zoo Clothing* applied normal principles in reviewing the transaction, and (in the absence of evidence to the contrary) concluded that there was nothing to show that the provision of clothing to the company's staff should not attract tax on the disposal of the stock involved. In our view, the normal principles did not require the Tribunal to examine whether the clothing amounted to uniforms, or on what terms the clothing was provided to the company's employees.

82. In relation to the inference which Mr Morgan said should be drawn from the decision in *Zoo Clothing*, we do not agree with his conclusion. The officer merely said that the items in question could not be considered as articles of uniform as they could be worn for everyday usage. There is no indication in the decision to suggest that passing the exclusive ownership of uniform clothing to staff members should not be treated as a supply of goods.

83. We have reviewed the other cases cited to us in this appeal concerning the provision of clothing to persons working for a trader (*JK Hill*, and *Bridget Jennifer Brown*). These did not concern uniforms, but involved claims for input tax in respect of clothing which the respective appellants claimed was required for the purposes of their businesses. We do not find these cases of assistance in the context of FCL's appeal.

84. Although it was a substantial part of FCL's submissions that the clothing provided to staff constituted uniforms, we hold that the question whether it did so is of little or no relevance in determining whether the provision of clothing free of charge to FC staff members was to be treated as a supply of goods for consideration.

85. FCL's third question is whether the supply of "uniform clothing" free of charge to its retail store staff is to be treated as a series of "business gifts". In our view, this question does not fit either the domestic UK legislation (para 5(1) Sch 4 VATA 1994) or Article 16 PVD. As we have already concluded, the concept of "business gifts" is not part of the charging provision; instead, it forms part of a limited exception from the full effect of that charging provision. Where transactions fulfil the terms of that exception, they are to be excluded from the total of supplies treated as made by the taxable person. The terms of the exception are set out in para 5(2) and 5(2ZA) Sch 4 VATA 1994.

86. The fourth question which Mr Morgan put for FCL was whether the cost of purchasing clothing identical in every respect to that supplied by FC free of charge to

its staff was ascertainable at the time of supply. The relevant UK statutory provision to be applied in arriving at a valuation is para 6(2)(a) Sch 6 VATA 1994 (for text, see above). The valuation hypothesis is that the taxable person is assumed to purchase goods identical in every respect (including age and condition) to the goods subject to the supply treated as made under para 5(1) Sch 4 VATA 1994.

87. FCL's argument is that the conditions imposed on staff members relating to the provision of "uniform clothing" have the effect that the clothing has no readily ascertainable value. We examine below the terms on which the clothing is provided, but without referring to those conditions at this point, it is possible to consider the issue in principle. The terms apply to staff members. The test to be applied in valuing the goods is the cost to FC of acquiring goods identical in every respect to those in question. The contractual terms to which FCL refers are those of the contract between FC and the staff member. Thus it is not possible for FC's hypothetical purchase of goods for itself to be subject to the terms of such a contract, because FC cannot be restricted in that way. It cannot contract with itself to restrict the terms on which it can dispose of goods.

88. In broader principle, we doubt in any event whether the hypothetical purchase can be regarded as affected by any contractual terms, as the test is limited to the purchase of goods identical in every respect to those which are treated as having been supplied. Contractual conditions are not part of that test.

89. The other element of the test in para 6(2)(a) Sch 6 VATA 1994 is the time by reference to which the valuation is to be made. This is "at the time of the supply". Those words refer back to the words "the person making the supply"; this is the supply by virtue of para 5(1) Sch 4 VATA 1994. The relevant time is therefore the time at which the goods, ie the items of clothing, are provided to the staff member. We consider below the issues of fact to determine the point at which this occurs.

(b) The factual issues

90. We consider the factual issues by reference to the four questions set out in Mr Morgan's decision tree; for ease of reference, we set out those questions again in dealing with the facts relating to each subject.

91. The first of these is whether the clothing supplied by FC free of charge to its retail store staff is provided for the purposes of FC's business.

92. In his evidence, Mr Marks, the founder, Chairman and Chief Executive of FC PLC, explained that the rationale for supplying the "uniform clothing" to staff was to promote products and so sell more. The badges worn by staff, attached by magnets to their clothing, were fundamental in security terms for identifying staff members to customers.

93. Staff members could be distinguished from members of the public by the fact that at the beginning of the season, staff members would be wearing clothes which would be different from those generally being worn by members of the public.

94. The whole concept of FC was to have an individual look. To that end, FC's management chose very carefully what staff were to wear. This was a real selling tool, and part of FC's business. It was paramount to FC's business that the staff should be wearing FC new season clothes. In his capacity as a director of FC, he was firmly of the view that the provision of clothing to the staff was for the purposes of FC's business.

95. Mr Marks confirmed that these arrangements were customary throughout the industry.

96. Mr Donoghue explained the importance of the retail store staff as ambassadors of the French Connection brand. Under his direction, Brand Ambassador Guidelines and Uniform Guidelines were issued each season to store managers. The purpose of the arrangements was to help sell French Connection clothes. Members of staff were, in effect, FC's "live" mannequins. This supported the French Connection brand and its ethos. It would be bad for staff members to be wearing other non-French Connection clothing.

97. We accept the evidence given by Mr Marks and Mr Donoghue, and find as a fact that the provision by FC of clothing to its staff members was for the purposes of FC's business.

98. The second question was whether clothing provided free of charge to FC staff should be treated as their "uniform".

99. In his evidence, Mr Donoghue did not accept that a French Connection clothing outfit worn by a staff member without a magnetic badge did not constitute a uniform. The meaning of the term was very clear, and was used in FC and in other similar businesses.

100. He referred to photographs included in the evidence. These were taken on 26 September 2014 of FC's retail staff working on the sales floors at two flagship London stores (Oxford Street and Regent Street). In his view these illustrated that customers on the sales floor could recognise instantly FC's retail store staff by the French Connection uniforms that they were wearing. The pictures showed staff members helping to sell French Connection merchandise.

101. He explained that not all the photographs showed genuine customers; FC did not wish to interfere unduly with its customers' experience within the store.

102. Mr Morgan submitted that the clothing did constitute a uniform. The important point was that the uniform clothing could be recognised as such when seeing the staff members in the context of their work within the store. The photographs demonstrated that the clothing constituted a uniform, even in the absence of a magnetic badge.

103. Mrs Carroll emphasised that in HMRC's submission, whether or not the clothing was a uniform was irrelevant. On the facts of FCL's case, HMRC did not accept that the clothing being considered in its appeal constituted a uniform. A uniform should make an employee instantly recognisable as such; that was not the

case here. From the photographs included in the evidence, it was impossible to distinguish from the clothing alone whether the staff member was an employee, or simply shopped at the store as a customer.

104. Mr Donoghue had explained that not all the people appearing to be customers in the photographs were genuine customers. In HMRC's submission, this illustrated the difficulty in identifying individuals as employees as opposed to genuine customers. The clothing was exactly the same as available retail stock; in addition, under the terms of the policy, every member of staff could wear something different. The only way in which members of staff could be identified was by their detachable badge. The badge did not turn the clothing into a uniform. In HMRC's submission, the confirmation by Mr Morgan for FCL that the badge was a security requirement itself confirmed that the clothing alone was not a uniform. A staff member could only be recognised by a badge.

105. We find it necessary to refer to the text of the "Uniform Guidelines" in force at the relevant time. We acknowledge that in his evidence, Mr Donoghue explained that he had changed the wording in the corresponding 2015 Uniform Guidelines. The 2014 wording was:

> "As always there are no restrictions on what you should wear you just need to ensure that your uniform choices reflect the brand image and you represent French Connection at all times . . ."

106. We do not find it necessary to examine the wording of the revised version. In each case, the staff member is to make a choice from the relevant range of French Connection clothing. Managers are involved to ensure that the choice is appropriate. The effect of the policy is that there is no standard choice to be made by the staff member; he or she could select any of a wide range of items.

107. As a result, the clothing selected does not, except in the very broadest terms, identify the wearer as a member of staff. The very fact that staff members are required to wear their badges while working in the store, and (as Mr Donoghue explained in evidence) are not permitted to wear their badges outside FC's stores, indicates that the badges are an essential means of identifying staff members. Mr Donoghue said that the reason why staff members were not permitted to wear badges outside the stores was for security, to minimise the risk of shoplifters getting hold of the badges and masquerading as retail store staff. If the clothing was sufficient on its own to identify staff members, we would not see the need for badges as having quite the level of importance in the context of security referred to by Mr Donoghue.

108. We find as a fact that, although staff members wear the French Connection clothing as "brand ambassadors", this does not constitute a "uniform" in the normally accepted sense of that word. The relevant definition contained in the Oxford English Dictionary is:

> "A distinctive uniform dress worn by the members of any civilian body or association of persons".

109. The wide variety of clothing which staff members may select, particularly to assist in promotion of the French Connection brand, means that in formal terms the description of such clothing as a "uniform" is not appropriate. The adjective "uniform" as defined in the Concise Oxford English Dictionary is:

> "the same in all cases and at all times; not varying".

We do not consider that the clothing is "uniform" in that sense.

110. Thus, although we fully accept the commercial reasons for the policy followed by FC, and similarly by its competitors, of providing clothing to staff for them to act as "brand ambassadors", we do not regard the clothing as constituting a uniform. We do not share Mr Donoghue's view that the clothing can be viewed as a uniform even without a badge; instead, we consider that the badge is an essential means of distinguishing between a staff member and a customer who happens to be wearing an outfit of latest season French Connection clothes.

111. The third question posed by Mr Morgan was whether uniform clothing supplied by FC free of charge to its retail store staff should be treated as a series of "business gifts".

112. In his witness statement, Mr Marks stated that the provision of clothing to staff was contractual, not gratuitous, and therefore not a gift. We accept that the arrangements for provision of clothing are part of the overall terms on which the staff members are employed, and that these are therefore contractual arrangements. We are satisfied that FC enters into these arrangements for commercial reasons. We are not persuaded that the provision of items to staff can never constitute a gift; to accept the contrary argument could mean that if a staff member were to be provided with items under £50 in value and received no other items in the same year, FC would not be able to rely on the business gifts exception in para 5(2)(a) Sch 4 VATA 1994. That would not be consistent with the way in which the assessment under appeal was calculated to take account of such excepted transactions.

113. Mr Morgan submitted that the assessment was on business gifts with a cost of more than £50. Mrs Carroll responded that the assessment had not been made on business gifts as such, but by reference to the related statutory provision (para (1) Sch 4 VATA 1994).

114. In his letter to Mr Castleton dated 20 December 2013, Mr Jemson of HMRC explained the effect of the legislation, and included the following comments:

> "Where a business makes assets it has bought and it owns to any private use [*sic*] a VAT liability arises as we discussed at our recent meeting. Schedule 4 of the VAT Act 1994 deals with matters which are to be treated as a supply of goods or services. Paragraphs 5(1) and (2) are in point. Where goods forming part of the assets of a business are transferred or disposed of by or under the direction of the person carrying on a business, whether or not for a consideration, this is a supply of goods. Where goods with a cost value greater than £50 are given to a person such as free staff clothing which can be worn in and

> out of the store, then VAT is due based on the cost value of the goods given to that person and Output Tax is due.
>
> As discussed, I understand French Connection provides free staff clothing throughout the year but has not been declaring any Output Tax relating to the same.
>
> Please provide a schedule of the cost value of clothing supplied to staff free of charge by VAT quarter for the last 4 years so that the appropriate adjustment can be made."

115. We have reviewed the rest of the correspondence leading up to the assessment and the subsequent revision of the assessment, and have found nothing which specifies that the assessments were made on "business gifts" as such. We find that the assessment and its revision were made on the basis of the application of para 5 Sch 4 VATA 1994, without reference to "business gifts". Mr Jemson's letter dated 8 April 2014 explaining the reduction in the amount of the assessment did not refer to business gifts as such; instead, he commented:

> "I have reduced the quarterly amounts by the entries shown where the amount per person did not exceed £50."

116. The subsequent correspondence relating to reduction in the amount of the assessment to take account of VAT already paid on amounts received from staff who had left within three months of the start of the season makes no reference to business gifts.

117. In determining the question whether VAT liability arises, we do not consider that deciding whether the supplies of clothing to FC staff are to be regarded as a series of business gifts assists that process.

118. Mr Morgan's fourth question was whether the cost of purchasing clothing identical in every respect to that supplied by FC free of its charge to its staff was ascertainable at the time of supply.

119. He referred to the conditions under which members of FC's store staff were provided with clothing under the "Employee Uniform and Discount Agreement". The clothing was transferred to the employee, and the agreement specified that the employee would not be required to return the clothes. However, if the employee resigned or was dismissed within three months of the start of the new season, or agreed a reduction in working hours during the course of the season, the employee's pay would be reduced by 30 per cent of the employee clothing allowance used. The employee agreed to be an ambassador for the brand by wearing the uniform and French Connection badge at all times whilst on the sales floor.

120. He submitted that the conditions meant that the clothing had no readily ascertainable value. Although no special label was placed on staff clothing, the conditions were behind the arrangement. The practical effect of the conditions was that the clothing could not be sold immediately. Thus the transaction value was the net present value of second-hand clothing worn frequently for three months. This was what FC would have to pay in accordance with para 6(2)(a) Sch 6 VATA 1994.

121. Mr Donoghue explained in evidence that FC had attempted to establish the value of second-hand French Connection clothing, but despite searching on line and in various shops, it had not proved possible to find any process for used French Connection clothing.

122. Certain articles of French Connection clothing were shown to us. There were two ladies' tops which had been used for approximately three months by staff members in one of the major London stores. For comparison, a new and unused example of one of those tops was provided.

123. Mrs Carroll submitted that for the purposes of para 6(2)(a) Sch 6 VATA 1994, the conditions of use were irrelevant. It had been agreed by both parties that the time of supply was when the employee took the clothing. At that point, the clothing was brand new. This was the value to be taken into account under para 6(2)(a).

124. She further submitted that it could not be correct that a supply was deliberately devalued just in case a staff member might leave in the future. She commented that the charge imposed under the Employee Uniform and Discount Agreement was based on the amount of the clothing allowance used, which reflected the retail value of the clothing at the time when it was first taken.

125. We commented to Mrs Carroll that there appeared to be a difference between the terms of the agreement and the basis on which the valuation was to be carried out under para 6(2)(a). Mrs Carroll confirmed to us that in HMRC's view, the valuation was to be based on the cost price.

126. We find that the conditions under which the staff members are provided with the clothing do not affect the valuation which is required to be made pursuant to para 6(2)(a) Sch 6 VATA 1994. As we have stated above, FC cannot itself be regarded as bound by those terms when considering the hypothetical purchase.

(c) Conclusions on law and facts

127. We are satisfied that the clothing provided by FC to store staff members under the Employee Uniform and Discount Agreement is provided for the purposes of FC's business. However, this does not affect the operation of para 5(1) Sch 4 VATA 1994; the items of clothing are goods in respect of which credit has been received for the input tax borne by FC, and para 5(5) Sch 4 VATA 1994 makes clear that the para 5(1) charge therefore applies.

128. We have found that the clothing does not as such amount to a "uniform", but this does not affect the application of para 5(1) Sch 4 VATA 1994. In circumstances where the title to the goods is transferred to the employee, nothing turns on whether the clothing does or does not constitute a uniform; the only part of the guidance in paragraph 4.4 of Notice 700 which is relevant in such circumstances is the first sentence relating to the passing of exclusive ownership.

129. We are satisfied that the concept of "business gifts" is not relevant to the cases where employees have used a substantial part of their "employee uniform allowance". However, it appears from the correspondence that a certain number of transactions have occurred where the value of the item or items provided to an individual staff member within the "same year" (as defined in para 5(2ZA) Sch 4 VATA 1994) has been no more than £50, so that in such cases the "business gifts" exception applies, as agreed between the parties.

130. Our finding that the supply of clothing falls within the charge under para 5(1) Sch 4 VATA 1994 results in the need to arrive at a valuation of the supply. We are satisfied that, in applying para 6(2)(a) Sch 6 VATA 1994, it is not appropriate to take into account the conditions under which staff members take the clothing, as those conditions cannot be regarded as applying to FC itself. The question is what FC would have to pay if at the time of the supply it were to purchase goods identical in every respect, including age and condition, to the clothing provided to the staff members. As title to the clothing passes to the staff member at the time of transfer, that is the time of supply, as both parties accepted; the goods are brand new at that point. Accordingly, the question is what the replacement cost of identical items would be at the beginning of the new season, the point at which the clothing is provided to staff members. We therefore agree with HMRC's view that the valuation is to be based on the cost price. Under para 6(2)(3), the cost to be taken into account is the purchase price of the identical goods exclusive of VAT.

131. In the light of all our findings, FCL's appeal must be dismissed. The charge under para 5(1) Sch 4 VATA 1994 applies, and the basis of valuation is clear, as we have explained.

132. The assessment was reduced from £51,663 to £35,724. This took into account the VAT already paid in cases where employees had left within three months and had therefore had their pay reduced under the terms of the agreement. Although the result is that the full liability is accounted for by taking into account the VAT previously paid and the reduced assessment, we would emphasise that the correct analysis is that the supply is made at the time of providing the clothes to the staff member; the reduction in a staff member's pay to recoup 30 per cent of the uniform allowance used is not relevant to the calculation of the VAT chargeable in accordance with para 5(1) Sch 4 VATA 1994. Thus in future there should be no VAT charge in respect of the "retrospective" payments deducted from staff members in those circumstances.

Right to apply for permission to appeal

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

JOHN CLARK
TRIBUNAL JUDGE

RELEASE DATE: 23 April 2015