



TC06087

Appeal number: TC/2016/05307

*VAT – single or multiple supply where single prepayment but customer
unable to participate in all components – single supply – appeal dismissed*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

RDS DRIVING SERVICES LTD

Appellant

- and -

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

Respondents

TRIBUNAL: JUDGE ANNE SCOTT

Sitting in public at North Shields on Wednesday 5 July 2017

Mr M Hetherington of UNW LLP, for the Appellant

Mr D Wilson, Litigator, Solicitors Office & Legal Services, for the Respondents

DECISION

The Issue

1. In HMRC's Statement of Case and Skeleton Argument it appeared that this is an appeal against a ruling by the respondent ("HMRC") in a letter dated 25 May 2016. The Notice of Appeal suggested that it was a decision dated 9 September 2016. In fact it was a decision dated 19 July 2016 which was confirmed on review on 9 September 2016. Furthermore that decision of 19 July 2016 stated that it should be read in conjunction with the earlier decision of 25 May 2016. I have done so.

2. For the avoidance of doubt, although the point did not arise in the hearing, I make it explicit that, notwithstanding the protestations of the appellant's agent in the correspondence, I accept that it was entirely appropriate for HMRC to treat the original request for review as a request for reconsideration and then to issue a new decision on 19 July 2016. The appellant's arguments until that point had not overtly raised the question of whether there were multiple supplies, or not. Consequently, HMRC had not addressed that issue.

3. The ruling which is challenged was to the effect that the appellant ("RED") was making a single supply to its customers of a Driving Instructor Training Course ("the Course") and VAT is due on the whole of the supply, even if the customer failed to complete any one or more of the three Parts of the Course. RED argues that it is entitled to make a retrospective adjustment to output tax in the event that a customer fails to commence one or more Parts of the Course.

The Hearing

4. Regrettably, there was no Statement of Agreed Facts and nor was there any witness evidence. However, with consent, Mr Hetherington gave oral evidence since there was a paucity of detail as to how RED operated. We had Skeleton Arguments from both parties, a Bundle of Legislation and Authorities, the details of which are annexed at Appendix A, and a slim Bundle of correspondence which included the "RED Instructor Training Course Agreement" ("the Agreement").

Background

5. On 7 April 2016, Mr Hetherington wrote to HMRC's Non-Statutory Clearance Team seeking agreement from HMRC in relation to the VAT treatment applicable to money retained by RED from customers who failed to progress on to different parts of the Course. That letter confirmed that RED did not query the VAT treatment applicable at the time it receives the prepayment from each trainee/customer ("trainee") because it was recognised that that payment, "at that time", represented advance consideration for the subsequent delivery of the different Parts of the Course.

6. RED argued that if a trainee did not progress to Parts 2 or 3 timeously, RED was not obliged to deliver those Parts and therefore any prepayment made by the trainee, having been forfeited, did not represent "direct consideration for the provision of any (taxable)

supply by RED". In those circumstances it was argued that RED should be entitled to treat the monies forfeited as outside the scope of VAT and reclaim the output tax previously accounted for when the prepayment was originally received. It was argued that the analogy was with the hotel sector when a guest cancels a booking and loses their deposit.

7. RED referred to *Air France* and *Esporta* arguing that they were in conflict with HMRC's published guidance.

8. HMRC responded on 25 May 2016 rejecting the claim and pointing out that the cases of *Air France and Esporta* were not relevant and *NCP* supported their view. That view was upheld on reconsideration and review.

RED's arguments at the hearing

9. RED acknowledges that each Part of the Course represents a supply for VAT purposes and to the extent that the trainee commences one of the Parts, then the element of the prepayment made for that part is subject to UK VAT in accordance with Sections 4 and 5 Value Added Tax Act 1994 ("VATA").

10. However, RED argued that where an individual does not commence one or more of what it describes as "discrete" parts of the Course, then the element of prepayment made for those parts no longer represents direct consideration for a supply of training and is therefore outside the scope of VAT.

11. RED relies on *Secret Hotels 2*, *Airtours* and *ING* for the proposition that, provided the contractual arrangements reflected the economic realities then, the Agreement dictates the VAT treatment.

12. At the hearing RED also relied on paragraph 43 of *NCP* which reads:

"The meaning of consideration for VAT purposes is clear from the *Dutch Potato* case and *Campsa*: it is the value actually given by the customer (or a third party) in return for the service supplied and actually received by the supplier and not a value assessed according to objective criteria. The service and the value given or to be given in return for it may be ascertained from the legal relationship between the supplier and the customer. Under the contract between NCP and the customer which is formed when the customer inserts money into the ticket machine at the car park and receives a ticket, NCP grants the customer the right to park his or her car for one hour in return for inserting not less than £1.40. If the customer wishes to park for up to three hours then he or she must pay not less than £2.10. It follows that NCP agrees to grant a customer the right to park for up to one hour in return for paying an amount between £1.40 and £2.09. If a customer pays £1.50, that amount is the value given by the customer and received by the supplier in return for the right to park for up to one hour. Accordingly, that is the taxable amount for VAT purposes."

13. The arguments set out at paragraph 6 above, were reiterated with the explanation that at the point at which the fees are forfeited the prepayment no longer represents consideration for a supply of services as covered by Section 5(2) VATA. Effectively, the actual time of supply for each Part is when that Part commences.

14. RED also argued that *Telewest* is authority for the proposition that the fact that the Course is supplied in different Parts and by different suppliers, means that it cannot be categorised into a single supply for VAT purposes.

5 15. Lastly, RED argued that it acted as agent for the Company in regard to payment for Part 1.

HMRC's submissions

16. HMRC certainly agree that output tax is due at the time the trainee pays the upfront fee for all three Parts of the Course as VAT becomes due at the time of the supply of the services.

10 17. The time of the supply of services under Section 6(3) VATA is generally treated as taking place when the services are performed. However, Section 6(4) VATA supersedes Section 6(3) and reads:-

15 “6(4) If, before the time applicable under subsection (2) or (3) above, the person making the supply issues a VAT invoice in respect of it or, before the time applicable under subsection (2)(a) or (b) or (3) above, he receives a payment in respect of it, the supply shall, to the extent covered by the invoice or payment, be treated as taking place at the time the invoice is issued or the payment is received”.

18. HMRC also rely on paragraph 43 of *NCP* on the basis that that case is authority for the proposition that it is the amount of the consideration paid that determines the VAT due in output tax and not the extent of the service provided. The supply in this instance is, in effect, access to all three Parts of the Course regardless of whether Parts 2 and 3 are actually commenced.

19. HMRC submit that, from an economic point of view, what is being supplied by RED is a single supply of the Course and it is irrelevant that there is a different entity providing one Part of the Course. It is RED that receives the consideration for the whole Course from its trainees. The fact that RED has effectively sub-contracted Part 1 of the Course to the Company, does not mean that the supply of the course should be split.

20. HMRC rely on the *ECJ* judgment in *CCP* but the quotation they used is not to be found in that judgment and is presumably a paraphrase. However the Court does state at paragraph 29:

35 “...first, that it follows from Article 2(1) of the Sixth Directive that every supply of a service must normally be regarded as distinct and independent and, second, that a supply which comprises a single service from an economic point of view should not be artificially split...the essential features of the transaction must be ascertained in order to determine whether the taxable person is supplying the customer, being a typical consumer, with several distinct principal services or with a single service.”

The Law

40 21. Although Mr Hetherington referred me to paragraphs 31-34 of *Secret Hotels 2*, paragraphs 47-49 of *Airtours* and paragraphs 35-37 of *ING*, his analysis went only as

far as stating that the Agreement established the parameters and it reflected the commercial and economic reality.

22. However, I place particular stress on paragraph 32 of *Secret Hotels 2* which reads:-

5 “When interpreting an agreement, the court must have regard to the words used, to the provisions of the agreement as a whole, to the surrounding circumstances insofar as they were known to both parties, and to commercial common sense.”

23. I was not referred to *WHA Limited v HMRC* (“WHA”)¹ but Lord Reed noted at paragraph 26 that decisions about the application of VAT are fact sensitive and a
10 small modification of the facts can render the legal solution in one case inapplicable to another. It is therefore necessary to consider the facts and all the circumstances in which the transaction took place carefully before looking at the matter as a whole in order to determine its economic reality. At paragraph 27, Lord Reed stated:-

15 “The contractual position is not conclusive of the taxable supplies being made as between the various participants ... but it is the most useful starting point.”

I adopt that approach.

What then are the facts?

24. RED is a company and is registered for VAT as part of a VAT group registration with its parent company. We were not provided with details of the representative
20 member but it was not thought to be RED.

25. RED’s business has two core elements namely:

(a)The franchising of driving instructor businesses (who are usually individuals) under the “Red Driving School” brand; and

(b)The training of driving instructors.

25 26. As part of the franchise model RED provides a range of services to its franchisees (including the use of a branded car) all of which are taxable at the standard rate.

27. In this appeal I am not concerned with the franchise business.

28. RED promotes the Course on its website and elsewhere. Mr Hetherington produced a page from the website dated 28 June 2017 and the relevant excerpts from
30 that read as follows:-

“With RED, you can purchase your driving instructor training on a pay-as-you-go basis, or as a combined package to take advantage of available discounts.

Option One – Full Course

¹ 2013 UKSC 24

Purchase the complete package for a one-off payment of just £1,795. Places are limited, though – secure your spot today to make sure you don't miss out.

Option Two – Full Course with the opportunity to get your training fees back

5 Purchase the complete package for a one off payment of £2,599. By choosing this option, you may be entitled to get a refund on your training fees, see 'Maximise your return with RED' below for full details.

Option Three – Pay as you go

Option three allows you to pay monthly for the course, from £199 per month. Contact us for more details."

10 Although the prices are different to the Agreement, that was assumed to be because the Agreement is dated December 2015. Mr Hetherington confirmed that although promotions varied the website correctly reflected the trading model. He states in the Skeleton Argument that: "An individual is able to purchase each Part separately, albeit the most cost effective way is for an individual to prepay the three different Parts in advance."

15 29. In this appeal I am only concerned with the VAT treatment where there has been prepayment for the three different Parts in advance.

30. RED trades with a logo which reads RED in bold with the wording "Driving School" below. It is on every page of the primary documentation which is the Agreement and that comprises:

20 A. Enrolment details

B. Course Packages & Payment Method

C. Terms & Conditions

D. Declaration (comprising an acceptance of the Terms & Conditions and a Customer Declaration).

25 31. It is B and C and, to a much lesser extent, D that are relevant.

32. At the bottom of D it states in small print, when giving relevant contact details and the company registration number, that the trainee is contracting with RDS Driving Services Ltd trading as RED Instructor Training. Inconsistently, in the body of the Agreement at C 1.1 it states that RDS Driving Services Ltd trades as RED Driving
30 School and provides the RED Instructor Training Course. Thereafter in the Agreement it is referred to as RED.

33. I am not replicating the whole of the Agreement but highlight the salient facts derived therefrom.

B. Course Packages & Payment Method

35 34. That reads as follows and is worthy of attention:

B. Course Packages & Payment Method
Packages included:
<p>Part 1</p> <p>Online home study modules, unlimited mock theory tests and a hazard perception test. Supplementary workbooks may be provided (additional costs apply) if you do not have access to the online facility. Telephone and study support, together with any additional books and publications RED deem relevant, will be provided.</p>
<p>Part 2</p> <p>Training consists of 10 hours practical training behind the wheel on a one to one basis (one student to one instructor).</p>
<p>Part 3</p> <p>Training consists of 42 hours training. This will be a mixture of practical and theoretical training. The practical training sessions will be delivered in car on a one to one basis. The theoretical training will be provided through online home study.</p> <p>Trainee licence holders with RED Driving School only.</p> <p>If you choose to start working as a driving instructor on a trainee licence (PDI Licence) with RED Driving School, you will also be entitled to additional validation training at no extra cost. The amount and format of this validation training may vary in line with best practice and Driver and Vehicle Standards Agency (“DVSA”) requirements – currently it comprises 20 hours one to one in car training.</p>
Promotions included: RIO 2
Course price: £2,295.00

35. The Course price is due on enrolment.

C. The Terms & Conditions

5 36. At clause 1.2 it reads: “Access to Part 1 of the Course is made available to you by RED Driving School Ltd. Parts 2 and 3 are to be delivered by RED subject to clause 1.7”.

37. Clause 1.7 states that: “The Course must be completed within 12 months of the Start Date (unless a material delay is caused by RED), excluding any additional or extra training recommended (additional costs apply).”

10 38. RED Driving School Ltd (“the Company”) is apparently another subsidiary of RED’s parent company and does not form part of the VAT group registration.

39. Currently its sole function is to hold the intellectual property rights for bespoke RED software. At clause C 6.1 of the Agreement it states that “The Software is the copyrighted property of RED Driving School Ltd ...”.
40. The Company has no employees.
- 5 41. If a trainee successfully completes Part 2 of the Course, clause C 1.8 states that the individual may have the opportunity “...to take a trainee license with RED”.
42. Clause C 1.9 states that on completion of Part 3 of the Course, RED guarantees the trainee a franchise within its “Driving School”. Considerable incentives are offered to stay with RED once partially or fully qualified.
- 10 43. At clause C 4.1 RED reserves the right to alter the amount and format of training from time to time.
44. At clauses C 4.3 and 10 RED reserves the right, but not the obligation, to terminate the Agreement if a trainee does not complete the course within 12 months and any fees paid in advance of delivery of Parts 2 and / or 3 will be forfeited and retained by RED.
- 15 45. On receipt of payment from the trainee, VAT at the standard rate is accounted for as output tax by RED on the basis that the payment represents advance consideration for the provision of the three different Parts of the Course.
46. The relevant provisions of clause 7 of the Agreement reads as follows:-
- 20 “7.1 Course fees for the Package you have selected or set out in Section B (Course Packages Payment Method). 20% of the Course Fee is applicable for Part 1 and you authorise RED to pay this fee to RED Driving School Ltd on your behalf.
- 7.2 20% and 60% of the Course Fee is allocated to Parts 2 and 3 respectively.
- 25 7.3 Any apportionment of Course Fees has no bearing on the right to a refund, which in turn is governed solely by Clause 9.”
47. RED pays the Company that 20% and the Company in turn accounts for VAT thereon.
48. In the event that the trainee changes his/her mind, then there is a cooling off period during which the trainee is able to obtain a refund of all or part of the prepayment.
- 30 49. As can be seen from paragraph 13 above, if a trainee chooses the most expensive payment option a refund of fees might be available. Clause C 12 sets out the terms for that, which is credit against the franchise fees being offered for the first seven weeks of operation as a franchisee and then again after 15 months of continuous operation as a franchisee. If 24 continuous months of operation as a franchisee is achieved then a lump sum of £1,295, being the final instalment, is repaid.
- 35

50. Lastly, clause C 9.4 provides that any complaints or cancellations should be addressed to RED.

Discussion

5 51. The first and most obvious point is that the Company is not a party to the Agreement.

52. Obviously, because the Company has no staff, it cannot deal with cancellations or complaints and no doubt it is for that reason that the Agreement provides that issues with those should be addressed to RED.

10 53. I accept that the Agreement contains three references to the Company, namely that it owns the software, provides the software for Part 1 and is paid 20% of the fees for that. However, the interface with the trainees is entirely with RED. Since RED trades as RED Driving School it would probably only be a particularly astute trainee who would even note that there were two different entities.

15 54. Whilst it is perfectly in order for intellectual property rights to be held in a different company, one of the problems with the purported supplies from the Company are that although Part 1 refers to telephone and study support, together with any additional books and publications, those are in fact provided by RED since the Company has no operational staff. Accordingly, even in the provision of Part 1 there
20 is in fact a supply by both RED and the Company yet the whole amount of the fee, apparently attributable to Part 1, is paid by RED to the Company.

55. The further issue is that the Company owns the intellectual property and the substantive problem is that both Parts 1 and 3 involve online home study using that. Mr Hetherington was unable to explain why the Company would receive payment for
25 Part 1 but did not for Part 3. That is wholly inconsistent and also points to this being a single supply.

56. The detailed Customer Declaration means that any trainee enrolling on the Course should be fully aware that:

30 (a) If (s)he fails any Part or does not complete the Course timeously fees will be forfeited, and

(b) If (s)he cancels the enrolment more than 8 days after the Start Date then, even if there has been no login to the online software, 50% of the fees will still be forfeited,

35 In choosing to pay the full fees for the Course in advance, and in the case of the Agreement, the highest cost for the Course, the trainee has therefore taken a calculated risk that (s)he may lose some of that payment.

57. As can be seen from paragraph 49 above, the period of exposure to risk is approximately three years for the trainee choosing to pay for Option Two (in this case

£2,295 although it is more in 2017). The trainee is gambling on the fact that (s)he will pass the Course timeously and will remain with RED as a franchisee for a continuous period of 24 months thereafter.

5 58. In paying for Option Two rather than the Option One (see paragraph 28 above) a trainee has chosen that greater risk in order to have access to the opportunity to obtain what amounts to a full refund of the training fees.

10 59. In choosing to pay for the Course in advance, whether at the higher or lower amount, the trainee has accepted the risk of forfeiture of fees in order to have access to all Parts of the Course, provided that the trainee honours its obligations. The trainee knows at all times that if (s)he does not commence or complete any Part, unless the cooling off provisions apply, then (s)he would not be able to obtain a refund. If that is unpalatable then the Pay as you go option is available. It is the trainee's choice and it is negotiated with RED.

15 60. The relevant hotel analogy is not where customer cancels and loses a deposit, as argued by RED, but rather where a customer chooses a prepayment rate for a stay for which cancellation is not available, pays that and then does not turn up. When payment is made, the supply is made. It is not necessarily the bed that is the supply. The customer has paid for the right to access a bed for that stay.

61. *Air France* is in point firstly where the Court states at paragraph 33 that:

20 "...the price paid by the 'no-show' passenger corresponds to the full price to be paid...the sale is final and definitive",

secondly at paragraph 34 that:

"It must therefore be held that the sum retained by the airline companies...constitutes remuneration, even where the passenger did not benefit..."

25 and lastly at paragraph 49 that:

"...performs the service it was required to perform solely by virtue of the fact that the passenger had the right to benefit from the fulfilment of the obligations under the contract".

That is precisely the position in this matter.

30 62. The trainee is making one payment for the supply of a course to be provided in three Parts.

63. I do not accept Mr Hetherington's argument that, whilst he accepted that the tax point, and therefore the liability to account for VAT, arose when the payment was made, nevertheless there was not a supply made to a trainee who did not commence Part 2 and/or 3.

35 64. Sections 1(2) and 6(4) VATA read together make it explicit that the supply for which the trainee makes payment **shall** be treated as taking place at the time the

payment is made. Whether or not the trainee continues to Parts 2 and/or 3 cannot change that.

5 65. As can be seen, both parties relied on paragraph 43 in *NCP*. Looking to that, in summary, I find that the legal relationship as set out in the Agreement is formed when the trainee enrolls for the Course, signs the Agreement, having chosen the payment option and made payment of the greater or lesser prepayment. The trainee is supplied with the right to embark on all three Parts of the Course. It is a single supply. I find that as each Part of the Course is integral to the Course as a whole, and the trainee has prepaid for the whole Course, it would be artificial to split the supply.

10 66. What then of RED's argument based on *Telewest*? Mr Hetherington requested that I pay particular attention to paragraph 71 which simply states that where there are two suppliers there can be no principal and ancillary supply.

15 67. For the reasons outlined above I do not find that there is any question of a principal and an ancillary supply in this matter. RED offer a Course, deliverable in three Parts and the trainee, in opting for one of the prepayment methods elects to have a single supply. RED accesses the software from the Company and elects to pay the Company only for Part 1. That is a matter for RED and the Company.

68. For all these reasons the appeal is dismissed.

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

30 **ANNE SCOTT**
TRIBUNAL JUDGE

RELEASE DATE: 31 AUGUST 2017

Legislation & Authorities Bundle

Section 1 VAT Act 1994

Section 2 VAT Act 1994

5 Section 5 VAT Act 1994

Section 6 VAT Act 1994

HMRC Guidance – VAT Supply & Consideration VATSC42100

ECJ Case C-349/96 Card Protection Plan and HMRC (“*CCP*”)

ECJ Case C250/14 & C289/14 Air France KLM/HOP!-Brit Air SAS (“*Air France*”)

10 HMRC and Secret Hotels 2 LTD [2014] UKSC 16 (“*Secret Hotels*”)

Telewest Communications plc and HMRC [2005] EWCA Civ 102 (“*Telewest*”)

National Car Parks Ltd and HMRC [2017] UKUT 247 (TCC) (“*NCP*”)

ING Intermediate Holdings Ltd and HMRC [2016] UKUT 298 (TCC) (“*ING*”)

Article 2 Sixth Council Directive (77/388/EEC)

15 Article 10 Sixth Council Directive (77/388/EEC)

Article 11 Sixth Council Directive (77/388/EEC)

Airtours Holidays Ltd and HMRC [2016] UKSC 21 (“*Airtours*”)

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