



Neutral Citation: [2022] UKFTT 334 (TC)

Case Number: TC 08591

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

By remote video hearing

Appeal reference: TC/2017/04834

*VAT. Whether supplies made by the Appellant are properly categorised as financial intermediation and, therefore, exempt under Item 5, Group 5 of Schedule 9 to the Value Added Tax Act 1994. Volker Ludwig v Finanzamt Luckenwalde (Case C-453/05) & CSC Financial Services [2001] ECRI-10237 considered. Held: the Appellant's supplies are exempt.*

**Heard on:** 20-22 July 2022

**Judgment date:** 09 September 2022

**Before**

**TRIBUNAL JUDGE ASIF MALEK**

**Between**

**EMERCHANTPAY LIMITED**

**Appellant**

**and**

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

**Respondents**

**Representation:**

For the Appellant: Ms. Hui Ling McCarthy QC of counsel & Ms. Sarah Black of counsel, instructed by Grant Thornton UK LLP

For the Respondents: Ms. Eleni Mitrophanous QC of counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs

## DECISION

### INTRODUCTION

1. This hearing was conducted remotely by video. Prior notice of the hearing had been published on the gov.uk website, with information about how representatives of the media or members of the public could apply to join the hearing remotely in order to observe the proceedings. As such, the hearing was held in public.
2. The Appellant (“EMPL”) and merchant OOD (“EMPO”) are in the same corporate group, the eMerchantPay Group (“the Group”). EMPO is a Bulgarian company and EMPL is incorporated and resident, for tax purposes, in the UK.
3. EMPO makes supplies to EMPL and, on 17 November 2015, EMPL sought a ruling from the Respondents (“HMRC”) on the nature of these supplies. In a decision dated 3 February 2017 (“the Decision”), HMRC determined that the supplies made are taxable and are not exempt supplies under Item 5, Group 5 of Schedule 9 to the Value Added Tax Act 1994 (“VATA”). HMRC issued an assessment to the Appellant under s.73(1) VATA for £64,618 for the VAT period 02/13 on 23 February 2017, and an assessment for £64,617 for the VAT period 05/13 on 31 May 2017 (together “the Assessments”).
4. EMPL appealed the Decision on 8 June 2017.

### ISSUES IN THIS CASE

5. It is common ground that there are only two issues for my determination. Namely:
  - (1) Whether the supplies by EMPO to EMPL are exempt under Item 5 of Schedule 9 to VATA as EMPL contends (“the Exemption Issue”), and
  - (2) Whether, if they are not, the Assessments were issued within one year after evidence of facts, sufficient in the opinion of HMRC to justify the making of the Assessments came to their knowledge pursuant to section 73(6)(b) VATA (“the Time Limit Issue”).

### EVIDENCE AND FINDINGS OF FACT

6. In this remote hearing evidence was given in the usual way. The Appellant relied upon Mr. Stephen Dixon, the Group’s Chief Financial Officer. He produced two witness statements which he adopted as his evidence in chief. He was cross-examined on the evidence that he provided and there was an opportunity for me to ask questions of him.
7. HMRC relied upon the evidence of Officer Alistair Niven. He produced a witness statement which he also adopted as his evidence in chief. However, he was not cross-examined and I also had no questions for him.
8. In addition, I was referred to documents contained within an extensive and agreed bundle.

### Background and pertinent findings of fact

9. After assessing all the evidence and acknowledging that the Appellant carries the burden of proof, I make the following findings of fact upon the balance of probabilities.
10. EMPL is the main contracting and trading entity within the Group and was incorporated in 2004. EMPL has three directors, and no other employees.

11. EMPO is the main operational company in the Group, supporting the Group's business. It was incorporated on 19 July 2006. In 2013, EMPO had approximately 50 employees based in Sofia, Bulgaria.

12. In the marketplace merchants sell goods and services to consumers. Where consumers pay by credit card a card acquirer collects the payment from the credit card institution and transmits it to the merchant. Sometimes a Payment Services Provider ("PSP") will be interposed between the merchant and the card acquirer. The role of the PSP is to introduce merchants to card acquirers and a number of alternative payment methods.

13. At all relevant times EMPL carried on the business activity of a PSP. It would attract merchants who needed payment services, conduct due diligence on the merchant in question and then introduce it to one of the card acquirers. It also acted as a guarantor in relation to these payments- although I accept that, in reality, this guarantee was very rarely called upon.

14. In more detail, EMPL entered into agreements with the payment provider or card acquirer to introduce business to them in return for an agreed commission or profit share. EMPL also enters into agreements with merchants so as to enable these merchants to use its services and be introduced to one or more PSP and to use the services provided by the PSP. The agreements entered into could be bi-partite (i.e. between EMPL and a PSP or EMPL and a merchant) or tri-partite (i.e. between EMPL, a merchant and a PSP).

15. During the course of the hearing I was taken, in some detail, to samples of both the bi-partite and tri-partite agreements. Each sample agreement was redacted to remove commercially sensitive information and each one was slightly different. However, the evidence shows that the agreements entered into by EMPL required it to, in general terms, do the following:

- (1) Market the PSPs card acquiring services to merchants,
- (2) Guarantee the PSPs debts to merchants,
- (3) Carry out due diligence and ongoing monitoring on merchants,
- (4) Provide payment processing, support and customer services to merchants, and
- (5) Provide the requisite technology to include providing a platform for payment and integration of the systems of the merchant and PSP.

16. However, EMPL did (perhaps could) not, itself, carry out any of the obligations or perform the services that it had agreed because, put simply, as a company with no employees (other than perhaps its directors) it lacked the resources to do so. Instead, it chose to sub-contract those services to another member of the Group: EMPO. There is no "outsourcing" or other agreement setting out the exact services that EMPO was to provide, the basis upon which it was to be remunerated, or any other similar terms that might commonly be found in a contract of this nature. Where group companies are concerned the absence of such a contract is not unusual and I do not seek to criticise the Appellant for not having such an agreement.

17. To assist with what EMPO was doing for EMPL at the relevant time I was referred to a Transfer Pricing Agreement between EMPL and EMPO dated 30 August 2013 (although the commencement date is recorded as 1 September 2011) ("the TPA"). The TPA provides that EMPO is the "main operational company" of the group providing underwriting, account management, risk management, cash management, administration and IT staff in support of all group activities and companies.

18. It is fair to say that the TPA does not say that EMPO is providing mediation or ‘matching’ services. However, this does not mean that these services were not, in fact, being provided by EMPO. This is because, firstly, one must look at the purpose of the TPA: this was to ensure that costs incurred by companies in the group for the benefit of other companies in the group were correctly and equitably recharged to the benefiting company. It is, therefore, first and foremost, an analysis of the costs incurred and not the services provided (although the two can, and perhaps are likely to, be the same). Secondly, the terms “mediation” or “matching services” have no magic in themselves. Just as if the TPA had set out that EMPO provided “mediation” or “matching” services that would not, in of itself, have been dispositive of the issue; neither is their absence. In short, the TPA is not very helpful in deciding the issue.

19. The only other evidence that was presented in relation to the services provided by EMPO to EMPL was the written and oral evidence of Mr. Dickson. He described how EMPL, essentially, “buys in” all the services that it requires to perform its obligations to its clients from EMPO. These consist of underwriting/account management, risk management, treasury/cash flow management, IT, payment processing and marketing.

20. The underwriting / account management activities constituted the main part of the services supplied by EMPO to EMPL and are the most resource intensive. In 2013 there were approximately 12 employees at EMPO involved in this work and it might take approximately two weeks’ worth of work hours to undertake the underwriting, due diligence, onboarding and initial set up required by the treasury team. This work consists of EMPO employees, firstly, following up leads for potential merchants received from third parties (“Resellers”) contracted to EMPL. Once potential merchants have been identified due diligence (such as verifying the merchant company, its directors, and shareholders and reviewing the merchant’s business model and website) is carried out on the merchant. On successful completion of the due diligence process the merchant’s application and supporting documentation is presented to the appropriate credit committee at EMPO. Once the credit committee has approved the application the EMPO credit underwriting team will forward the application to one or more merchant acquirers (who will have been matched based upon their sector and/or other preferences and risk appetites). The EMPO underwriting team then works with the EMPO risk team to “on board” the merchant onto the Group’s payment gateway. The ongoing relationship with the merchant is then managed by EMPO account managers.

21. As well as assisting with the “on boarding” of merchants the risk management team will, in accordance with instructions from the credit committee, put in place specific monitoring in relation to each merchant. This can take the form of using fraud checking tools or placing limits on transaction numbers or volumes. In the event transactions are not in line with expectations an investigation is carried out. In 2013 there were approximately 10 EMPO employees involved in this work.

22. The treasury/cash flow team becomes involved once an application from a merchant has been accepted. It is responsible for (a) reconciling the funds received with the transactions processed in the payment gateways, and (b) the calculation of EMPL’s fees and commissions and the commissions due to resellers. In 2013 approximately 5 EMPO employees were involved in this work.

23. In 2013 the IT team was primarily focussed on merchant support, that is to say helping with the integration of EMPL’s gateway and integration with merchant acquirers and alternative payment methods. In 2013 there were around 14 people in the IT team.

24. The payment processing is done through technology and requires minimal human involvement. The process starts with the customer entering their card details on the merchant’s website following which the rest of the process is entirely automated. The transaction is

automatically reviewed for fraud and against set criteria leading, ultimately, to the card either being accepted or declined and a record being kept. The process takes a matter of seconds and represents a minimal part of the service provided by EMPO to EMPL.

25. In 2013 EMPO provided minimal marketing support to EMPL. This consisted of the upkeep of a fairly basic website and some attendance at trade shows and events.

26. Mr. Dickson's evidence in relation to the above was consistent and, cogent. He answered questions put to him in a straightforward manner and came across as a credible witness. I, therefore, accept his evidence as summarised above.

## **THE LAW**

### **The Exemption Issue**

27. Under European Community law Art. 135 Directive 2006/112/EC ("the PVD") provides:

(1) Member States shall exempt the following transactions:

...(d) transactions, including negotiation, concerning deposit and current accounts, payments, transfers, debts, cheques and other negotiable instruments, but excluding debt collection...

28. Under domestic law section 31 VATA provides:

"(1) A supply of goods or services is an exempt supply if it is of a description for the time being specified in Schedule 9..."

29. Schedule 9 "shall be interpreted in accordance with the notes" contained in it (per s.96(9) VATA ).

30. Group 5 of Schedule 9 to VATA provides:

"1. The issue, transfer or receipt of, or any dealing with, money any security for money or any note or order for the payment of money.

...

5. The provision of intermediary services in relation to any transaction comprised in item 1, 2, 3, 4 or 6 (whether or not any such transaction is finally concluded) by a person acting in an intermediary capacity."

31. The relevant parts of the notes to Group 5 provide:

"...

(4) This Group includes any supply by a person carrying on a credit card, charge card or similar payment card operation made in connection with that operation to a person who accepts the card used in the operation when presented to him in payment for goods and services.

(5) For the purposes of item 5 "intermediary services" consist of bringing together, with a view to the provision of financial services-

(a) persons who are or may be seeking to receive financial services, and

(b) persons who provide financial services,

together with (in the case of financial services falling within item 1, 2, 3 or 4) the performance of work preparatory to the conclusion of contracts for the provision of those financial services, but do not include the supply of any market research, product design, advertising, promotional or similar services or the collection, collation and provision of information in connection with such activities.

(5A) For the purposes of item 5 a person is “acting in an intermediary capacity” wherever he is acting as an intermediary, or one of the intermediaries, between –

- i. a person who provides financial services, and
- ii. a person who is or may be seeking to receive financial services.

(5B) For the purposes of notes and 5A “financial services” means the carrying out of any transaction falling within item 1, ...”

### **The Time Limit Issue**

32. Section 73 VATA states:

“(1) Where a person has failed to make any returns required under this Act (or under any provision repealed by this Act) or to keep any documents and afford the facilities necessary to verify such returns or where it appears to the Commissioners that such returns are incomplete or incorrect, they may assess the amount of VAT due from him to the best of their judgment and notify it to him.

...

(6) An assessment under subsection (1), (2) or (3) above of an amount of VAT due for any prescribed accounting period must be made within the time limits provided for in section 77 and shall not be made after the later of the following—

(a) 2 years after the end of the prescribed accounting period; or

(b) One year after the evidence of facts, sufficient in the opinion of the Commissioners to justify the making of the assessment, comes to their knowledge,

but (subject to that section) where further such evidence comes to the Commissioners’ knowledge after the making of an assessment under subsection (1), (2) or (3) above, another assessment may be made under that subsection, in addition to any earlier assessment.”

33. Section 77 VATA provides:

“(1) Subject to the following provisions of this section, an assessment under section 73, 75 or 76, shall not be made—

- i. more than 4 years after the end of the prescribed accounting period or importation of acquisition concerned, or

...”

### **DISCUSSION**

#### **The Exemption Issue**

34. The key issue between the parties is the nature or categorisation of the supplies made by EMPO to EMPL. HMRC says that these supplies are taxable. EMPL contends that they are exempt because, in short, EMPO is providing financial intermediation services to EMPL. That is because, it is argued, EMPO is bringing together merchants (who are “*persons who are... seeking to receive financial services*”) and merchant acquirers (who are “*persons who provide financial services*” within Item 1 of Group 5 of Schedule 9) and performing the work preparatory to the conclusion of those contracts.

35. The Appellant took me to the CJEU's decision in *Volker Ludwig v Finanzamt Luckenwalde* (Case C-453/05) ("*Ludwig*") arguing that it made supplies to EMPL in analogous circumstances. Whilst I found the facts of the *Ludwig* decision illuminating (especially in giving context) I should prefer to concentrate, as with any authority, on the key principles that can be derived therefrom. In this case these principles are:

(1) "Exemptions covered by Art 13 of the Sixth Directive are to be interpreted strictly..." [par 21]

(2) "... the concept of 'negotiation' applies to the activity of an intermediary who does not occupy the position of a party to a contract relating to a financial product and whose activity amounts to something other than the provision of contractual services typically undertaken by the parties to such contracts. Negotiation is, in effect, a service rendered to and remunerated by a contractual party as a distinct act of mediation. In that regard, the purpose of such an activity is to do all that is necessary in order for two parties to enter into a contract, without the negotiator having any interest of his own in the content of the contract (see, to that effect, Case C-235/00 *CSC Financial Services [2001] ECR-I-10237*, paragraph 39). On the other hand, it is not negotiation where one of the parties entrusts to a sub-contractor some of the clerical formalities related to the contract (see, to that effect, *CSC Financial Services*, paragraph 40) [par 23].

(3) "...transactions exempted under Article 13B(d)(1) of the Sixth Directive are defined in terms of the nature of the services provided and not in terms of the person supplying or receiving the service..." [par 25] and "The same observation may be made as regards the nature of the relationship between the negotiator and the parties to the contract..." [par 26]

(4) "...The Courts case-law makes clear that, in order to be regarded as exempt transactions for the purposes of Article 13B(d) of the Sixth Directive, the services provided must, viewed broadly, form a distinct whole, fulfilling in effect the specific and essential functions of the service of negotiation ..." [par 27] and "In that regard, the Court has held that negotiation is an act of mediation, which may consist, amongst other things, in pointing out to one of the parties to the contract suitable opportunities for the conclusion of such a contract, in making contact with another party or negotiating, in the name and on behalf of a client, the detail of the payments to be made by either side, the purpose of such an activity being to do all that is necessary in order for two parties to enter into a contract, without the negotiator having any interest of his own in the terms of that contract..." [par 28]

(5) "... the recognition of an activity of negotiation which is exempt for the purposes of Article 13B(d)(1) cannot necessarily depend on the existence of a contractual link between the provider of the negotiation service and one of the parties to the credit agreement..." [par 29]

(6) "...the Sixth Directive cannot depend on the existence of a contractual link between the provider of the service of negotiation and one of the parties to the credit agreement, but must be assessed with regard to the very nature of the service rendered and its purpose..." [par 33]

(7) "...As stated in paragraph 39 of *CSC Financial Services*, negotiation is an act of mediation which may consist, amongst other things, in pointing out to one party to the contract suitable opportunities for the conclusion of such a contract, the purpose of such an activity being to do all that is necessary in order for two parties to enter into a contract, without the negotiator having any interest of his own in the terms of that contract. The concept of negotiation does not, therefore, necessarily presuppose that the negotiator, as

subagent of the main agent, enters into direct contact with both parties to the contract, in order to negotiate its terms, provided, however, that his activity is not limited to dealing with some of the clerical formalities related to the contract” [par 38]

(8) “...the fact that the taxable person has no contractual link with any of the parties to a credit agreement to the conclusion of which he has contributed and that he does not establish direct contact with one of those parties does not preclude that taxable person from providing a service of negotiation of credit which is exempt...” [par 40]

36. HMRC rely upon *CSC Financial Services* and took me, in particular to paragraph 40 which was not quoted in *Ludwig*. Paragraph 40 provides:

“On the other hand, it is not negotiation where one of the parties entrusts to a sub-contractor some of the clerical formalities related to the contract, such as providing information to the other party and receiving and processing applications for subscription to the securities which form the subject-matter of the contract. In such a case, the subcontractor occupies the same position as the party selling the financial product and is not therefore an intermediary who does not occupy the position of one of the parties to the contract, within the meaning of the provision in question”

37. Bearing in mind these authorities (and in particular the referenced paragraphs) and applying them to the facts it seems to me that EMPO’s supplies to EMPL can and should be characterised as the provision of intermediation services.

38. This is because, firstly, when one stands back and looks at the services as a whole one can see that the core of the services provided by EMPO to EMPL relate to those elements which are essential in bringing merchant acquirers together with merchants with a view to the former providing financial services to the latter. The elements that I have in mind here are attracting merchants in the first place, carrying out due diligence on the merchants, matching the merchants with suitable merchant acquirers, arranging for the contractual formalities to be completed and finally “onboarding” the merchant. The bringing together of merchants and merchant acquirers is core not only because, from the merchant’s perspective, the end goal must be to enter into a contract with one or more merchant acquirers to enable card payments to be taken; but also because this is what EMPO committed most of its human resources to doing.

39. Secondly, I agree with HMRC that EMPO’s supply to EMPL is a single composite supply as defined in *Mesto*, and I did not understand the Appellant to be arguing otherwise. However, I cannot agree that the principal feature of the supplies made by EMPO to EMPL was payment processing for services in relation to which the latter was, apparently, remunerated as opposed to intermediation between merchant acquirer and merchant. It is clear to me that without the introduction of merchant to merchant acquirer there was, during the relevant period, no business to be done for EMPL. This is because, absent the introductions, there would have been no transactions in relation to which a commission or profit share could be earned. There would, accordingly, have been no payments for EMPL to process or, indeed, carry out any of the other functions that Mr. Dickson’s evidence shows EMPO carried out. So, it is not the payment processing that is the principal feature of the supply, but the introductions of merchants to merchant acquirers. It does not matter that there was a focus by EMPO or the Group on ensuring that the payment processing that EMPO carried on was faster, more secure, more reliable, more widely available and better integrated than the competition. This, it seems to me, is simply a feature that would make EMPO more attractive to both merchants and merchant acquirers.

40. Neither does it matter that EMPL is rewarded according to the number of transactions processed by EMPL.



41. Thirdly, I reject the contention that all EMPO is doing is carrying out “clerical formalities”. This is simply not supported by the evidence. EMPO clearly does more. Further, the fact that some of the services provided (such as the payment gateway, risk management, payment processing, treasury services, account management) are key needs of EMPL, are technical in nature or occurred after a merchant had entered into the relevant contract(s)) does not advance the argument any further. The test is whether or not the services provided are properly categorised as intermediation or merely “clerical formalities”.

42. Fourthly, I agree with the Appellant when it asserts that the supplies provided by EMPL are irrelevant. The supplies that we are concerned with in this appeal are those made by EMPO to EMPL. EMPL’s supplies are, put simply, irrelevant to that consideration and this remains the case whether or not EMPL sub-contracted or outsourced to EMPO all the services it needs to provide for its operations. There is no contradiction in holding, on the one hand, that the services provided by EMPO to EMPL are part of the bundle of services provided to EMPL so as to enable the latter to fulfil its contractual obligations, and on the other, holding that these supplies are properly characterised as intermediation. Developing this a little further: the reason why the activities are being carried out (i.e. to enable EMPL to fulfil its contractual obligations) is irrelevant if there is, in fact, financial intermediation being carried on.

43. Lastly, it is clear that whilst the contractual position might inform the nature of the supplies it is the ‘economic reality’ that is fundamental to the analysis. The evidence suggests that the ‘economic reality’ is that the Appellant is providing financial intermediation.

#### **The Time Limit Issue**

44. Given my decision with regards to the Exemption Issue it is not necessary for me to deal with the Time Limit Issue. I do not propose to do so. Any further comment that I make under this head would be *obiter*, might detract from the clarity of my decision in relation to the core issue and would, certainly, unnecessarily lengthen it.

#### **CONCLUSION**

45. For the reasons that I have given I find that the supplies from EMPO to EMPL are exempt and I, accordingly, allow the Appellant’s appeal.

46. I make no findings as to whether or not the Assessments were issued out of time.

#### **RIGHT TO APPLY FOR PERMISSION TO APPEAL**

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

**ASIF MALEK  
TRIBUNAL JUDGE**

**Release date: 09<sup>th</sup> SEPTEMBER 2022**