

VAT INPUT TAX RECOVERY: THE TESCO CLUBCARD CASE

The First-tier Tribunal (FTT) has recently released its decision in a case concerning the VAT treatment of supplies made in relation to the Tesco Clubcard loyalty scheme.

The *Tesco* decision is certainly helpful but it also underscores the importance of ensuring that the contractual arrangements and other features of a loyalty scheme are such that they support VAT recovery by the sponsor of the scheme, taking into account all of the decisions of the courts and tribunals which have considered similar loyalty schemes.

In a similar way to the earlier cases of *Loyalty Management UK (LMUK)* and *Baxi*, the FTT in *Tesco* considered whether the sponsor of a loyalty scheme was entitled to recover VAT on goods and services provided to members of the scheme by parties other than the sponsor.

In *LMUK*, the European Court (CJEU) decided that the sponsor was not entitled to VAT recovery. However, the Supreme Court subsequently held that the sponsor was entitled to VAT recovery, justifying its departure from the CJEU's decision on the basis that the questions put to the CJEU had been misleading with the result that the CJEU's decision was based on an incorrect understanding of the facts.

In *Tesco*, HMRC made two main arguments:

- ◆ the Supreme Court in *LMUK* had been wrong to reach a different conclusion from that of the CJEU; departing from the decision of the CJEU was not a course which was open to the Supreme Court. As a result, the FTT in *Tesco* should consider the questions raised in the case in light of the decision of the CJEU in *LMUK* rather than that of the Supreme Court; and
- ◆ even if the FTT based its decision on that of the Supreme Court in *LMUK*, the facts in *Tesco* differed from those considered in *LMUK* to the extent that the Supreme Court decision did not create a precedent enabling *Tesco* to recover VAT on goods and services provided to members of the scheme. The important difference – so HMRC

alleged – was that in *LMUK* each point earned by a scheme member gave that member a contractual right to receive goods or services for no cost or at a reduced cost whereas in *Tesco* the member had to convert his / her points into vouchers before he / she had a right to goods or services from the third party provider.

The FTT rejected both arguments. The judge, Judge Bishop, found that the FTT was bound to follow the Supreme Court decision and that the difference in facts between *LMUK* and *Tesco* was immaterial.

The *Tesco* decision is only a FTT decision (and so could be appealed). But some lessons can be taken from it:

- ◆ it should be possible to structure loyalty programmes in a manner which allows for input tax recovery, based on the principles of the Supreme Court decision in *LMUK*;
- ◆ the VAT analysis will turn on the structure of the scheme and its underlying agreements. Minor differences in the facts can result in a significant difference in the VAT treatment; and
- ◆ it is important to avoid features of loyalty programmes which have been subject to adverse decisions of the CJEU in *Baxi* and *Kuwait Petroleum*. In its decision, the FTT distinguished the Clubcard scheme from those schemes.

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