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Landmark ECJ Ruling on TOMS

The European Court of Justice gave its decision in the cases on the application of the Tour Operators' Margin Scheme (TOMS) on 26 September 2013. This day is likely to be remembered as a landmark in the taxation of travel. For many the news is not good: VAT costs will increase; administration will increase.

BACKGROUND

The European Commission launched legal proceedings against eight member states on the central question of whether wholesale supplies should be within TOMS. The eight states all maintained that wholesale business must be in TOMS; the Commission thought otherwise. A wholesale supply is one made to another person for re-sale. This question is of huge importance for large parts of the travel sector.

The Commission also argued that certain aspects of Spain's TOMS system are not permitted under EU law and should be stopped.

WHOLESALE TRAVEL

The Court has decided that the Commission's arguments were unfounded. Wholesale travel supplies should be included in TOMS. This will have huge implications for many.

The Commission argued that EU Directives must be interpreted in such a way that limits the use of TOMS to sales made to a 'traveller'. The client of a wholesaler is by definition re-selling the services and therefore cannot be a traveller and the supply must fall outside TOMS. For the Commission, the reason for the lack of uniformity in approach of member states on this question is the mistaken substitution of the word 'traveller' by 'customer' in some language versions of the Directive.

The Court did not agree. All versions of the Directive must be considered and where, as in this case, there is inconsistency the Directive must be interpreted in the light of the objectives of the legislation in question. The objectives of TOMS are simplicity and a fair and efficient allocation of tax revenue to member states. Both objectives are best served if wholesale business is included in TOMS.

This is in stark contrast to the UK position. Since 1996, UK procedures have made it clear that wholesale travel falls outside TOMS (although it was possible to opt-in to TOMS before 2010). The UK was not a party to the cases, but nevertheless the findings affect us too. As things stand, it is to be expected that UK rules will have to change, although timing is uncertain. For many in the wholesale sector, a change to TOMS accounting would have serious consequences.

TRANSPORT COMPANY SCHEME

ABTA and HM Revenue & Customs (HMRC) agreed a set of arrangements in the mid-1990s, all of which are designed to ensure that tour operators need not pay VAT on the margin made on passenger transport services, which ordinarily qualify for zero rating. The most widely used of the arrangements is the transport company scheme.

However, the transport company arrangements rely on the exclusion of wholesale supplies from TOMS. The Court's decision therefore must bring into question how long this arrangement can continue. Tour operators will no doubt consider which of the other arrangements (the agency option and the airline charter option) best suits their circumstances.





CALCULATING TOMS VAT DUE

HMRC's procedures require an annual TOMS calculation. All TOMS revenue and related costs are assessed for a financial year and the calculation determines the output VAT due.

Spain has an arrangement whereby taxpayers can calculate a global margin

made on all relevant transactions in a tax period. The Commission argued that the Directive does not permit such an aggregated or global approach to the assessment of VAT due.

On this point, the Commission succeeded: the Court decided that the Directive does not allow for anything other than the calculation of TOMS VAT due individually on each sale.

We must conclude therefore that the UK arrangements are also insupportable within the terms of the Directive and that change may be required. It is hard to imagine, however, that there will be much appetite to change an arrangement which has operated quite happily since TOMS was introduced in the UK 25 years ago.

There is great irony, of course, in the fact that the Court, having stated that simplicity is a key objective of TOMS, should then introduce great complexity to the calculation of VAT payable.

INVOICING

Spain was also taken to task on its approach to the invoicing of TOMS supplies. Again, the Court agreed with the Commission that Spain's procedures could not be supported by the Directive.

This, itself, is of no real consequence in the UK. More important are comments of the Advocate General (AG) in her opinion on the cases. The AG thought that the rules might be interpreted as requiring the issue of a VAT invoice for a TOMS supply. This would involve the disclosure of the margin made by the supplier. The decision, however, does not address this point directly. There is a suggestion that a client has a right to recover VAT declared on the margin (which of course must be known by the supplier given the conclusion above on the nature of the calculation) but no statement was issued by the Court that a VAT invoice should be given.

CONCLUSION

There is much in the decision of great importance to travel businesses. The VAT landscape for the travel sector may look very different as a result of the decision. The reactions of the Commission and of HMRC will now be vital in understanding the decision's practical effects and the timing of any changes.

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