Retailers fly high with VAT in airport shops

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Commercial analysis: It has been reported that airport retailers are reducing the total amount of VAT that they pay each quarter to HMRC without passing on the benefit to the consumer. David Bowden examines the revelation that producing a boarding pass when making a purchase is not a legal requirement and talks to Andrew Loan, a VAT expert in the tax and structuring group at Macfarlanes LLP on the implications of this.

What are the issues that have been raised in relation to this?

David Bowden (DB): Thousands of air passengers who had up until now been under the impression that producing their boarding pass was a legal requirement have been outraged to find out that this is not the case.

Airport retailers such as WHSmith and Boots have admitted that fliers are entitled to say 'no' when asked to show their pass and have said that they use the information to calculate how much VAT is due to HMRC because they do not need to account for HMRC for purchases made by customers flying to non-EU destinations. Two-thirds of customers in a recent poll called for airport shops to operate dual pricing for EU and non-EU customers, so that the savings retailers make can be passed onto the customer.

Information on a boarding pass shows a passenger's entire itinerary. Stores such as WHSmith say they don't hold onto data such as flight bookings when scanning passes. It says it allows it to analyse the purchasing trends by time of day and by product category for customers travelling to different locations. It claims the information is limited to the International Air Transport Association's (IATA) three digit destination airport codes and does not give access to any personal data of individual travellers. It says any VAT relief obtained is reflected in its single airport price all passengers pay.

Retailers say they are following rules set by HMRC and say claiming back VAT on a proportion of purchases made by customers flying to non-EU destinations complies with the current VAT rules. This raises three main issues:

- What do airside shops have to do to comply with HMRC's rules about VAT?
- Will showing a dual price solve the problem?
- Are airside retailers compliant with privacy rules set out in the Data Protection Act 1998 (DPA 1998)?

What exactly is the tax position around VAT in airports?

Andrew Loan (AL): The basic starting point under VAT legislation is that a retailer is required to charge VAT on the supply of taxable goods or services that are treated as made in the UK. Most goods sold by retailers will attract VAT at the standard rate, which is currently 20%. The retailer collects VAT from its customers as part of the sale price, and accounts for the VAT it collects on its sales to HMRC--with credit for VAT that the retailer pays on the goods and services that it purchases.

Although airport passengers may have checked in their luggage and passed through passport control and security, and so have mentally left home, 'airside' at an airport is still within the territory of the UK, and so 'airside' airport retailers are still required to charge VAT on the taxable goods that they sell, just like those on 'landside'.

One exception to the general rule is that a sale of goods which are then exported out of the EU can be treated as zero rated, so no VAT needs to be charged by the seller. In most cases to claim this exception one of the following must apply:

- the seller must arrange for the export of the goods by engaging a haulier or courier, for example, to take the goods out of the EU
- the buyer must be based outside the EU and arrange for the goods to be exported themselves (see HMRC Notice 703)

Neither of these conditions is met by UK resident individuals who buy goods at an airport, so a retailer would still have to charge VAT, but the second condition could apply to customers based outside of the EU who can reclaim VAT under the rules on tax free shopping (see HMRC Notice 704/1).

However, the first condition is extended by an extra statutory concession (ESC) (see ESC 9.1 HMRC Notice 48) under which an airport retailer which is approved by HMRC and which sells goods to passengers who intend to leave the EU may treat the customer as exporting the goods on behalf of the retailer. This provides as follows:

'VAT on goods supplied at duty-free and tax-free shops.'

'The supplier of goods which are liable to VAT and which are supplied to intending passengers at duty-free and tax-free shops approved by the Commissioners may, for those goods which are exported directly to a place outside the VAT territory of the member states, be regarded as the exporter and zero rate the supply.'

To apply the zero rate, the retailer will need to retain some evidence that the customer is actually intending to leave the EU imminently, including the name of the passenger, their destination, and the date of travel, unless HMRC agrees otherwise. This is the reason why passengers have been asked to show their boarding card at 'airside' shops--if the boarding card indicates that the customer will be travelling directly to a place outside the EU, the retailer can treat the sale as zero rated.

Are these companies doing anything wrong?

AL: Like most UK retailers, airport shops typically display a single ticket price for each item which is inclusive of VAT, if any, chargeable on the sale of that item. VAT legislation protects customers to some extent by providing that the consideration for a supply includes any VAT chargeable on that supply, unless the parties agree otherwise. The position can be different for sales taxes in other countries, such as the US, where customers can get an unpleasant surprise when state and local sales taxes are added to the ticket price at the till.

It is certainly possible for airport retailers to reduce their prices when the zero rate applies, but some airport retailers have been taking advantage of these rules by displaying a single ticket price, which includes any VAT that may be chargeable, and then using the ESC to avoid accounting for VAT to HMRC where customers show they are leaving the EU.

If the retailer has no evidence to show that a customer is leaving the EU, then it will need to account for 1/6th of the sale price to HMRC as VAT, but if the customer shows a boarding pass that indicates they are travelling directly out of the EU, the retailer can keep that amount for itself. The retailer does not have to change the price that it charges to the customer.

Similar rules apply to retailers selling goods that can attract excise duties, such as alcohol or tobacco, where the seller needs to be sure that a customer is leaving the EU if the sale is to be duty free. In other cases, even if the law does not require customers to show a boarding pass, a retailer can decline to sell goods to them if they do not.

These rules assume that the goods are exported from the UK and remain outside the EU. There are strict limits on the amount and value of goods that can be imported back into the UK from outside the EU without VAT or customs duties being applied, not just alcohol and tobacco, but other goods too.

Are there any laws on dual pricing?

AL: Although most retailers display a single ticket price, it is perfectly possible under the VAT rules for a seller to display parallel ticket prices, one including and one excluding VAT. For example, the price for an item may be £100, excluding VAT and £120, including VAT.

This practice is adopted by some retailers, particularly those with many business customers that can recover VAT on their purchases such as builders' merchants. In most cases, the seller will have to charge VAT, but the business customer knows that it can recover the VAT so is not concerned about the VAT being added. The peculiarity with the airport retailers, which is not seen in other situations, is that the seller's obligation to charge VAT depends on the circumstances of the customer.

DB: In the case of *Brogden v Marriott* [1836] (3 Bing NC) 88 4 judges in the court of common pleas considered the validity of a contract for the sale of a horse. The horse had been sold for 200 guineas 'provided that he trots 18 miles within 1 hour', but if not he would be sold for 1 shilling. Tindal CJ found this conditional price contract to be unenforceable as a betting contract. Gaselee J found the sums so far apart to be a bet or penal, but questioned where the line should be drawn where the two sums were nearer.

There is a possibility that a passenger may not get any flight, for example if he or she is taken ill, or if the connecting flight is in Madrid, Paris or Amsterdam and they decide not to catch it. Is an airside retailer selling something VAT free to a passenger entering into a bet with him that he will leave the EU as he has promised to do?

AL: This is a different situation and I am not convinced the common law betting analogy has any application here. The ESC only requires a seller to keep evidence showing a buyer intends to leave the EU. A seller is not required to establish that a buyer has actually left the EU. The ESC is not withdrawn if for some reason a customer changes his mind about travelling after the sale.

Are there any data protection repercussions?

DB: The DPA 1998, s 29(1) (c) permits the processing of personal data for the purpose of the assessment or collection of any tax or duty and it grants certain exemptions. Personal data processed for tax purposes is exempt from the first data protection principle's fair and lawful processing requirement with the proviso that DPA 1998, Schs 2 and 3 still apply where such processing is 'likely to prejudice' the assessment or collection of taxes.

Personal data processed for tax purposes is also exempt from the data subject access provisions. DPA 1998, s 29 is not a blanket exemption and can only be claimed on a case by case basis (*R (on the application of Alan Lord) v Secretary of State for the Home Department* [2003] EWHC 2073 (Admin)).

The Data Protection Directive 95/46/EC, para 1(c), art 6 provides that personal data must be: 'adequate, relevant and not excessive in relation to the purposes for which they are collected and/or further processed'. This is reflected in the third data protection principle in the DPA 1998. Is it 'excessive' for airside shops to see boarding cards of all passengers when they need to see and record data relating to only those who are travelling outside the EU? Is it 'excessive' to record data not just relating to a final airport destination, but also the passenger's passport number, whether a passenger is travelling in economy or business class, the date and time of day of travel and whether they are flying with a budget airline or not?

In DA/90 24/49/3 *Community Charge Registration Officers of Runnymede BC v Data Protection Registrar* [1990], the Data Protection Tribunal (DPT) looked at the data that various local authorities held and recorded on their citizens to administer the poll tax. This included cross-referencing data held on the electoral roll. The tribunal held that while the holding of some additional information was permissible in certain circumstances--the holding on that database of a substantial quantity of property information obtained from voluntary answers on the canvass forms was far more than necessary for the purpose.

In DA/90 25/49/2 *Community Charge Registration Officer of Rhondda BC v Data Protection Registrar* [1990] the DPT looked at a council which asked all those registering for the poll tax to provide their date of birth. It claimed it wanted to differentiate between those with common surnames, such as Jones, who shared similar or identical first names and lived at the same property. The DPT found that recording this information for everyone 'exceeds substantially the minimum amount of information which is required' in order to compile or maintain the poll tax register.

The Supreme Court will hear a final appeal in *Vidal-Hall and others v Google Inc (The Information Commissioner intervening)* [2015] EWCA Civ 311, [2015] All ER (D) 307 (Mar) next year. This relates to a claim that Google had collected private information about a claimants' internet use on its Apple Safari browser without their consent. Damages were claimed for distress under three heads:

- misuse of private information
- breach of confidence
- breach of the DPA 1998

Permission was granted on two grounds relating to the DPA 1998.

AL: The ESC requires a retailer to have evidence that a customer is travelling to a destination outside the EU.

Are the companies being sufficiently transparent on the purposes for which the data is processed?

DB: The Data Protection Directive 95/46/EC, art 7 provides that personal data may be processed only if 'the data subject has unambiguously given his consent' to the data processing. Processing is also permitted where it is 'necessary' for the

performance of a contract to which the data subject is a party. DPA 1998, Sch 2, para 1 more loosely provides that 'the data subject has given his consent to the processing'.

An airside retailer could obtain this consent in a number of ways. There could be a notice in the shop or by the till providing a fair processing explanation. The customer could be given a copy either with or on the back of a till receipt. Where a customer asks why a retailer wants to see and take a copy of his/her boarding pass, then a retailer could give either a summary of what the data will be processed for a copy of any fair processing notice.

AL: A retailer needs to collect sufficient data to comply with the HMRC rules in order to apply the correct VAT treatment. To apply the ESC, that will include as a minimum the name of a customer and their final travel destination.

Interviewed by David Bowden.

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