

## VAT treatment of customer loyalty schemes

[Loyalty Management UK Ltd \(LMUK\) and Baxi Group Ltd \(Baxi\) \(C-53/09 and C-55/09\)](#)

### Summary

The ECJ has held that the taxpayers were not entitled to recover VAT paid in respect of loyalty rewards but are entitled to recovery in respect of services which benefit the taxpayers' own business activities.

### Background

#### LMUK

LMUK is the operator of the 'Nectar' loyalty card scheme. It makes payments to businesses (redeemers) which supply reward goods and services to loyalty card holders (collectors) in return for redemption of 'Nectar' points. LMUK sought to recover the VAT charged to it by the redeemers.

HM Revenue & Customs (HMRC) considered the payments by LMUK to be third party consideration paid by LMUK for supplies of reward goods and services to collectors, and therefore that LMUK was not entitled to recover the VAT.

#### Baxi

Baxi is a boiler manufacturer which awards points to boiler installers buying its products. @1 is a loyalty scheme operator which supplies reward goods and services to the installers redeeming their points. @1 invoices Baxi for the value of points redeemed and Baxi sought to recover the VAT.

HMRC considered that the payments to @1 were third-party consideration for the reward supplies to the installers (except to the extent that they represented consideration for @1's supply of scheme administration).

As the issues in these two cases were similar, the ECJ heard them together.

### Held

"In relation to a customer loyalty rewards scheme such as those at issue in the cases in the main proceedings, Articles 5, 6, 11.A(1)(a) and – in the version resulting from Article 28f(1) – 17(2) of Sixth Council Directive 77/388/EEC ..., as amended by Council Directive 95/7/EC of 10 April 1995, must be interpreted as meaning that:

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- payments made by the operator of the scheme concerned to redeemers who supply loyalty rewards to customers must be regarded, in Case C 53/09, as being the consideration, paid by a third party, for a supply of goods to those customers or, as the case may be, a supply of services to them. It is, however, for the referring court to determine whether those payments also include the consideration for a supply of services corresponding to a separate service; and
- payments made by the sponsor to the operator of the scheme concerned who supplies loyalty rewards to customers must be regarded, in Case C 55/09, as being, in part, the consideration, paid by a third party, for a supply of goods to those customers and, in part, the consideration for a supply of services made by the operator of that scheme for the benefit of that sponsor."

### **Implications**

In essence, the ECJ agreed with HMRC that the payments by the taxpayers to the redeemers and @1 included third-party consideration for the supplies of the rewards to the collectors and installers. The VAT on this element of the payment was therefore not recoverable by the taxpayers. However, to the extent that it was possible to identify a separate supply of a marketing, advertising, promotional or other service to the taxpayers by the redeemers or @1, and to identify consideration for the service, the taxpayers would be entitled to recover that input VAT.

### **What happens next?**

It is likely that these cases will return to the UK courts for determination of the extent to which payments made by the taxpayers constitute consideration for services of the redeemers and @1. As a result, it may be some time before these cases are decided, as it may be necessary to provide further evidence and factual information on valuation, and that may necessitate remittal of these cases to the First Tier Tribunal. Alternatively, the taxpayers may negotiate agreements on valuation with HMRC.

We expect HMRC to issue guidance on the outcome of this case fairly soon and to enforce any assessments of VAT raised, or reject claims from businesses.

### **Comments**

Whether your business is an operator of a loyalty scheme (such as LMUK), a scheme sponsor (such as Baxi) or a redeemer, the judgment in this case is likely to have some impact, whether direct in terms of VAT recovery, or indirect in terms of the economics of the scheme. All affected businesses will clearly have to consider carefully how best to proceed in their own particular circumstances.

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As regards the retrospective position, businesses should ensure that, where there is a service element identifiable in the amounts paid out, input VAT recovery is secured.

Going forward, despite the ECJ's judgment in the circumstances of this case, loyalty schemes may still be structured in such a way as to minimise the detrimental effect of irrecoverable VAT.

*If you would like to discuss the implications for your organisation, please contact 4 Eyes Ltd.*

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