UK TRAVEL RETAIL FORUM

Association of International Retail

<u>UKTRF and AIR response to HM Treasury's *Myth buster on the VAT Retail Export Scheme and tax-free airside sales* document</u>

1. Duty-free sales will be extended to EU-bound passengers for the first time in over 20 years

- *Duty-free applies to the sale of alcohol and tobacco free of UK VAT and excise duty when passengers leave the UK and purchase these goods past security control points in airports.*
- *As regional airports serve more EU than non-EU destinations, they will also benefit significantly from the extension of duty-free sales to EU-bound passengers.*
- *Ports and international train stations serving EU destinations will be able to offer duty-free for the first time in over 20 years.*

2. Alcohol allowances will be roughly quadrupled, the first significant change in over 20 years

- *Alcohol allowances will be roughly quadrupled for passengers to enable them to bring in to GB, for example, three crates of beer, two cases of wine and one case of sparkling wine for personal use, without having to pay the relevant taxes.*
- *These changes will enable UK residents to save up to £120 on UK duty if maximising their allowance1 and provide one of the most generous alcohol allowances in the world.*
- *As we leave the EU these allowances will also apply to passengers entering GB from the EU.*

This is a welcome step by the Government– but increased allowances will not help struggling UK airports – especially regional airports – and travel operators to preserve their revenue streams and protect the jobs put at risk by the decision to remove Airside VAT free sales.

Arrivals stores in UK airports are not currently permitted under UK law, so any additional alcohol purchases taking advantage of the increased allowances will take place overseas.

3. The VAT Retail Export Scheme (RES) will be withdrawn in GB and will not be extended to EU residents

Most visitors to the UK are from the EU and they come despite not being able to claim back VAT on the goods they purchase and take home (24.8m EU vs 16.0m non-EU visitors in 2019).

It's not just about visitor numbers, it's about visitor spend. The 24.8m EU visitors spend £10.6 bn (average £427 each) while the 16m non-EU visitors spent £17.8 bn (average £1,112 each). Non-EU spend is therefore around three times more than EU. HMT's point here demonstrates that tax free shopping attracts high spending visitors.

Fewer than one in ten non-EU visitors (8%) use the VAT RES. Those that do are often charged substantial administration fees. The net refund is unlikely to act as a significant motive.

HMT has misunderstood the tax-free shopping system. 8% is the number of VAT refunds made (1.2 million), not the number of users. In fact, 1.6 million sales are made (only 75% of sales are reclaimed due to the difficulty in reclaiming at Heathrow because the validation system is not digitalised). HMT assumes that visitors all travel as individuals. That is not true. Most visitors travel in groups (average 3) so the actual number of users is 3x1.6 million = 4.8 million (30%). By HMT's logic, if one person pays a restaurant bill for three people, the restaurant only has one user.

The administration charges in the UK are the same or less than every other EU country. They could be further reduced if HMRC had digitalised the validation system.

Extending to the EU would result in a large amount of deadweight loss by subsidising spending from EU visitors which already happens without a refund, potentially taking the total cost up to around £1.4 billion per annum

HMT has miscalculated the cost of extending the scheme to EU visitors. In its Technical Note it says "In 2019, HMRC estimate VAT RES refunds cost around £0.5bn for around 1.2m non-EU visitors at UK exit points. In 2019 the ONS estimate there were 1.7 EU passengers (24.8m) for every non-EU passenger (16.0m) to the UK. This implies an extension to the EU could significantly increase the cost of the scheme by up to an estimated £0.9bn." HMT has estimated the additional cost by multiplying £500 million by 1.7 to reach £0.9 billion. This is not correct because:

- There are not 1.7 EU passengers for every 1 non-EU passenger, there are 1.55 (24.8m/16m = 1.55)
- The calculation of the predicted cost should also include relative spending. As HMT stated in its Technical Note, the 24.8 million EU visitors spend £10.6 bn while the 16 million non-EU visitors spend £17.8 bn. With Non-EU visitors spending an average of £1,112 and EU visitors spending £427, each EU visitor spend is just 38% of non-EU spend
- So, the cost is not (£500m x 1.7 = £900 million) it is (£500 million x 1.55 x 0.38=£294 million), three times lower than the HMT estimate

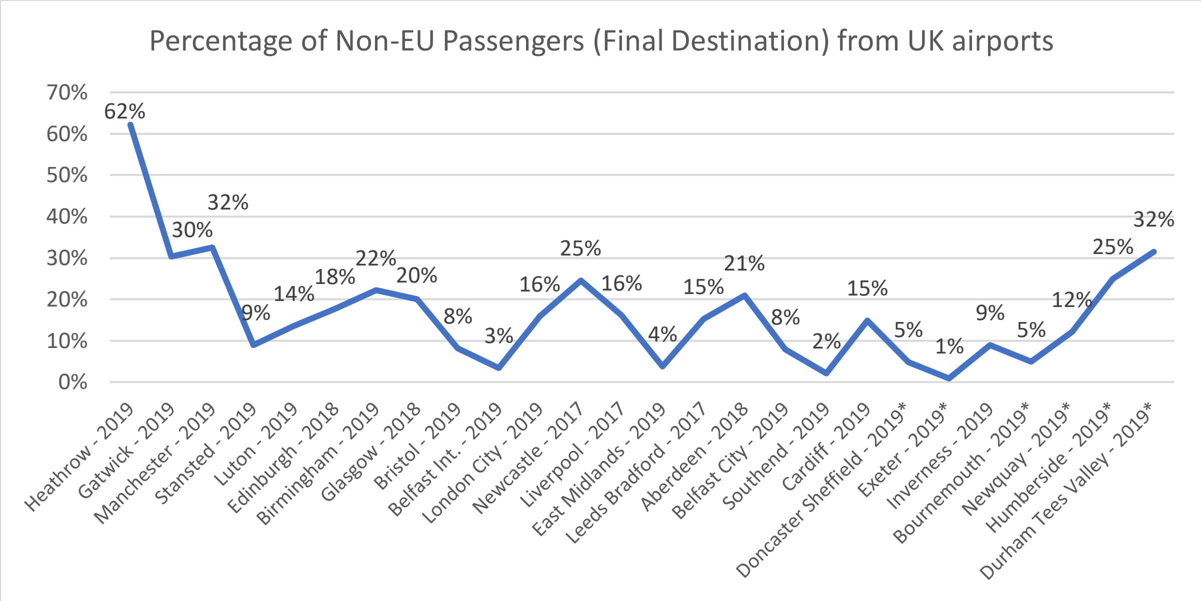
Furthermore, industry figures suggest that EU visitors are responsible for only 10% of total shopping spend, so the cost would be only around £50 million.

4. Tax-free airside sales will be withdrawn across the UK and will not be extended to EU passengers

- *Tax-free applies to the sale of non-excise goods (for example, confectionery, clothing, electronics and cosmetics) free of UK VAT when passengers leave the UK, bound for a non-EU country, and purchase these goods past security control points in airports.*
- *Ports and international train stations have not previously been able to offer tax-free sales as they only serve EU destinations. Regional airports serve significantly more EU than non-EU destinations, so have only able to offer tax-free sales to a limited number of passengers.*
- *HMRC estimate that around £150 million of VAT is not charged as a result of tax-free airside sales. Extending the relief to the EU would significantly increase the cost and result deadweight loss by subsidising spending from EU-bound passengers which already happens.*

This is misleading. While it is true that many regional airports fly primarily to EU destinations, a significant percentage of these passengers are transiting via the EU to a final destination outside the EU, making them eligible for tax-free shopping at UK airports.

If the Airside VAT ESC is removed, passengers will still be able to make tax free purchases in the EU and on arrival in other non-EU countries, but will not be able to do so in the UK – diverting millions of potential purchases away from regional airports.



VAT RES: rationale for withdrawal

5. The status quo is not an option for the VAT RES. WTO rules meant that after the end of the transition period the Government must either extend the VAT RES to the EU or remove it completely. An extension could cost up to £1.4 billion a year and would result in a large amount of deadweight loss by subsidising spending from EU visitors which already occurs. The Government has decided not to extend this costly scheme and is therefore withdrawing it.

As demonstrated in the point above, HMT has overestimated the cost of extending the scheme to EU visitors by 300%. It will not cost £1.4 billion.

6. Fraudulent use of the VAT RES was estimated to cost up to £50 million in 2018, and this could significantly increase if extending the scheme to the EU – for example, the ONS estimates there to be around 3.7 million EU nationals residing in GB, who could potentially use the scheme by using their EU passport as fraudulent 'proof' of their eligibility.

Most fraud is due to HMRC's failure to digitalise their element of the system. Most other countries have fully digital systems which prevents most fraud. The industry has submitted a proposal to the Government to digitalise the HMRC element of the system, at no cost to the Government, within 6-12 months.

7.The benefit from the VAT RES flows almost entirely (c90%) to just two places: Central London (80%, West End and Knightsbridge) and Bicester Village (10%). This is not levelling up.

HMT underestimates the importance of the VAT RES scheme to cities and regions around the UK. Edinburgh, Manchester, Glasgow, Liverpool, Leeds and Birmingham generate over £225 million of tax-free sales for their local economies, as well as the indirect increases in other visitor spending.
We believe that Ministers should listen to the people in the regions who understand the importance of the tax-free shopping to their regions, rather than London-based HMT officials

- Marketing Manchester - "The visitor economy of Greater Manchester, which secures over 100,000 jobs, will be dealt a hammer-blow by this decision."
- Birmingham Chamber of Commerce - "The abolition of the VAT Retail Scheme would be a major blow to our visitor economy. The proposal to remove the tax-free shopping scheme undermines

a central pillar of Government policy – notably the desire to 'level up' the country and bring prosperity to all four corners of the country."

- The North West Business Leadership Team - "Tax free shopping is not just a stimulus for us as an international retail destination. It is a crucial part of our visitor economy offer."
- Essential Edinburgh - "Tax-free shopping is fundamentally crucial for Edinburgh city centre. On top of the existing challenges, the loss of tax-free shopping would be catastrophic for the city"

HMT misunderstands that London is the global shop window for British brands that manufacture their goods all around the country. Burberry, for example, manufactures its products in the North East. Mulberry manufactures in the South West. There are around 160,000 manufacturing jobs all over the UK that make luxury goods to sell to international visitors in London stores. Ending VAT RES puts many of these jobs at risk. This is not levelling up.

VAT RES: impact on international tourism

8. Fewer than one in ten non-EU visitors (8%, c.1.2m) actually use the VAT RES. For 92% of non-EU visitors to the country this simply isn't a consideration. Even for the visitors that do use the VAT RES, it is hard to argue it is a significant, let along primary, determinant of their travel decision and that they would no longer visit the UK:

HMT has misunderstood the tax-free shopping system. 8% is the number of VAT refunds made (1.2 million), not the number of users. In fact, 1.6 million sales are made (only 75% of sales are reclaimed). Most visitors travel in groups (average 3) so the actual numbers of users is 3x1.6 million = 4.8 million, (30%). This misunderstanding of the VAT RES scheme invalidates many of HMT's following points and calls into question their conclusions.

• Once you account for admin fees charged by agents and retailers, which can range between 10- 70% of the refund, net VAT RES savings account for less than 6% of total trip costs. The average refund, net of fees, is around £270 compared to an average trip cost of around £4,900.

Admin fees do not range from 10-70%. The average is 10-25%. They are the same, or less, than fees in other EU countries. The draw for visitors is the prospect of buying goods at a discounted rate. They do not look at this as a proportion of their total trip cost.

The "average refund" is a meaningless figure. What is important is spending by key markets. We have actual sales data that show that high spending Chinese shoppers spend £8,800 on shopping per trip and non-high spending Chinese spend £2,500 on shopping per trip with an average of £3,400 per Chinese family.

• A HMRC survey of VAT RES user visitors from China, India and the USA found that two thirds said they would have purchased the items regardless of the scheme, and 28% would still have purchased fewer items. In other words, a total of 95% of people would still shop.

Real sales data, collected globally over many years by the industry, show conclusively that this is not the case. High spending international visitors, who are highly mobile and price sensitive shop in countries where they get the best value. Once Britain becomes known as the only country charging VAT but not offering tax-free shopping, these visitors will shop elsewhere.

There is no reference provided for this survey. Given HMT's selective and misleading use of surveys (the penultimate bullet point in this section shows how HMT has selectively used a VisitBritain report to mislead) we place no credibility on this point.

• *The UK is not the cheapest place to buy designer luxury goods in Europe today. If this is the key driver of a trip to Europe, then tourists would not visit the UK over France or Italy.*

The cost of luxury goods is relatively standard across Europe. But the attraction to international visitors is the prospect of buying these goods at a discount rate. Once Britain is known as the only European country charging VAT but not offering tax free shopping, international visitors, who are highly mobile, will chose to take their custom elsewhere.

• *24% of Chinese visitors to the UK already do multi-country trips according to the ONS. So even if they prefer to shop elsewhere, they still can shop in the UK as part of a European holiday.*

Shopping is the largest expenditure item for Chinese visitors. Those on multi-country tours (they average 2.6 countries per trip) are most likely to divert this spending to other EU countries where they can shop tax-free. Britain will have Chinese visitors (but fewer, staying less time) but not their money.

• *The UK visa offer is also better. It involves similar prices and processing time as the visa for France and Italy, but we give a two-year multi-entry (vs single entry) and a longer stay – 180 vs 90 days.*

The UK visa offer is not as attractive to international visitors (especially Chinese) compared with the Schengen visa. Most visitors will not visit the UK more than once in two years and few stay more than a few weeks, so these elements are not attractive. But the Schengen visa allows access to 26 European countries. Visitors wanting to add the UK to a multi-country tour have to go through the biometric application process twice, which most don't do.

• *The average cost for a two week stay in London for a Chinese tourist ranges from £2,035 for mid-range to £5,986 for luxury. The average net refund would therefore only account for £122 and £360 of respective trip costs, without considering any import taxes due on their return.*

HMT lists the source for this as "according to HMT research using budgetyourtrip.com, farecompare.com, and booking.com.". This is not how Chinese tourists book their trips. Most use tour operator packages. HMT officials using western websites to imitate Chinese tourists is not a robust basis for policy making.

• *Tourists visit the UK for a number of reasons, with the key motivator being cultural attractions. Tax-free shopping does not even make the list of reasons for visiting GB.*

HMT is being selective. HMT is referring to the VisitBritain Foresight 150 report. This cites consumer research where respondents were asked to chose key motivators from a list of 30. Shopping was not included on that list, so it was not an option. But two pages later, the same report cites an ONS International Passenger Survey in which nearly a quarter of visitors cite shopping as a motivator (this includes EU visitors who can't use tax free shopping). For non-EU visitors (can use tax free shopping) it was a far greater motivator (e.g. Saudi Arabia 51%, UAE 41%)

• *Even after these changes, VAT-free shopping is still available for non-EU visitors who purchase items in store and have them sent directly to their overseas addresses.*

The existing VAT-free shopping is unattractive to visitors, more expensive and less popular than tax-free shopping. Few use the current scheme and visitors will simply divert their shopping to countries offering tax-free shopping

9. Canada and New Zealand do not offer this type of tax-free shopping and the USA does not have a country wide system. Yet the USA is the top non-Asian country on China's most visited list, ahead of any European countries that have tax-free shopping.

America does not have a countrywide system because sales taxes are state-wide, not federal. States that do not have a sales tax are already offering tax free shopping. Most states that attract international visitors, and have a sales tax, offer tax free shopping.

Unlike New Zealand, Britain has many competing destinations nearby, all offering tax free shopping

VAT RES: Centre for Economic and Business Research (CEBR) report

10.The CEBR has produced a report on the costs and benefits of ending the VAT RES. Commissioned by Global Blue, one of the refund agents referred to above, it makes some alarming predictions about the effect on the British tourist industry. However, these claims are based on the patently implausible assumption that the end of the scheme will cut non-EU visitor numbers by 4.96 million – four times as many people as currently use the scheme!

This is a misleading statement. The Cebr report gave three different scenarios. The first two are based on orthodox economic modelling, using elasticity of 1.3 to predict the impact of ending VAT RES on visitor numbers. The third, was an extreme scenario, which incorporated the findings of consumer research into visitor behaviour change. HMT here is ignoring the two orthodox scenarios and focusing on the extreme. The orthodox scenarios predict that the end of the scheme will cut non-EU visitor numbers by 1,160,000.

As explained above, HMT has confused the number of refunds (1.2 million) for the number of users (around 5.4 million). So, the Cebr estimate is a fall of 21% of users of the VAT RES. This is an entirely reasonable conclusion.

11. If the report's dire predictions were likely, then the government's announcement would have prompted a significant adverse reaction in the share prices of companies exposed to tourism levels. In fact, there has been no such reaction.

Many quoted companies operate throughout Europe and the world. Visitor spending will not decline worldwide, it will simply relocate out of Britain to countries offering tax-free shopping (particularly France and Italy) where these brands operate.

12.Officials have held a meeting with the report's author to review the analysis and have shared further information to help inform future work.

This is not helpful and does nothing to change the report conclusions.

VAT RES: consultation with industry

13.The notion the Government did not consult with industry is false. The consultation ran from 11 March to 20 May 2020 and explored a broad range of options for the VAT RES, including the potential withdrawal of the scheme. In particular, paragraph 4.21 references the possibility of abolition and 4.23 ask specifically about the impacts of abolition.

The potential withdrawal of the scheme was mentioned in just two sentences in a 22 page document.

VAT RES: current operation

14.The international norm is that VAT on goods should be paid in the country of consumption. Currently, visitors to the UK who are resident in a non-EU country, can use the VAT RES to obtain a VAT refund on high-street goods they buy and take home with them in their luggage, with the expectation that they pay the relevant taxes on arrival in their home country. The VAT RES is only one mechanism to achieve taxation in the place of consumption and is an imperfect way to ensure this, not least due to the risk of fraud and non-compliance.

What alternative ways are HMT offering to comply with the international norm that VAT on goods should be paid in the country of consumption? The VAT-free scheme is not used because it is unattractive, administratively difficult and expensive. Ending the VAT RES results in the UK breaking international norms.

15.The scheme is paper-based and passengers must be prepared to show the goods, the till receipts and the VAT refund document to a Border Force official when they leave the UK to evidence the fact that the goods are to be exported. An administrative fee is charged by retailers or refund agents on the refund claim, reducing the refund's value.

The scheme is paper based because, in the eight years since it first decided to digitalise its element of the scheme (validating claims), HMRC has failed to do so. Almost every other country offering the scheme has digitalised within two years of making the decision.

The retailer elements are already digitalised and the industry has offered to digitalise the HMRC element at no cost to government within 6-12 months.

Digitalisation would provide capacity, reduce reclaim queues, reduce pressure on Border Force, cut administration fees and reduce fraud. It is HMRC's failure to digitalise that has caused many of the problems with the VAT RES.

16. For the first time in over 20 years, the Government is providing duty-free sales for UK travellers when they visit the EU (c.67m UK travellers visit the EU). This also boosts regional airports which primarily deal in EU travel. Duty-free sales to non-EU passengers cost approximately £245 million in 2019. Extending duty-free to EU-bound passengers will significantly increase the cost of the scheme as more people travel to the EU than non-EU destinations.

There will be a welcome benefit of additional duty free sales on alcohol and tobacco to EU-bound passengers. However, this will be insignificant compared with the blow of losing all VAT free sales to all passengers.

Non-duty free sales (goods other than alcohol and tobacco) make up roughly 70 per cent of all the sales that take place at an airport. In some London airports, alcohol and tobacco sales account for as little at 6 per cent of total sales and ca 15% in a midsized regional airport.

Furthermore, airside retail sales can account for as much as 35 – 40 per cent of total airport revenues in some cases – particularly in regional airports.

The benefit of additional duty free sales on alcohol and tobacco to EU-bound passengers will be insignificant compared with the blow of losing all VAT free sales to all passengers.

The loss in revenue for smaller airports will materially and immediately affect their ability to reinvest in infrastructure, attract new routes, and maintain a competitive offering to passengers. UK regional airports will struggle to compete with their EU counterparts because of this decision.

It is worth remembering that nearly every other country maintains a duty and tax free sales regime. It is an anticipated and indeed expected part of the passenger journey.

Tax-free airside concession: legal issues

17. As with VAT RES, WTO rules mean we cannot continue tax-free airside sales as they operate today.
18.The current rules that have allowed tax-free airside sales for those travelling to non-EU destinations are not set out formally in legislation and have previously been permitted through an HMRC extra statutory concession (ESC). The wording of the ESC for tax-free airside sales specifies that the relief shall only apply to "goods which are exported directly to a place outside the VAT territory of the member states" and, following a 2005 Judgement from the House of Lords HMRC's discretion to provide, or update, tax reliefs through an ESC has been limited. As such, the ESC for tax-free airside sales, as it stands, could not be amended, nor could it apply solely to non-EU bound passengers after the end of the transition period.

This is incorrect. Multiple sources of independent legal advice have concluded the Government is not obliged to remove the ESC from 1 January 2021, and in fact retaining it and extending it to passengers travelling from the UK to the EU is the most appropriate course of action for HM Treasury. A more detailed summary is at the bottom of this document, based on a detailed legal analysis by Slaughter and May.[i]

There is nothing preventing the Government from continuing the ESC in its present form. Furthermore, if, as anticipated, English law changes to permit zero-rating of exports to the EU, the ESC can simply be amended to bring it in line with those changes, as this is clearly the will of Parliament, and therefore not in breach of the Wilkinson Decision.

Tax-free airside concession: rationale for withdrawal
19. The VAT saving is not consistently passed on to consumers, and goods are often brought back into the country by UK residents, undermining the high street. HMRC estimate that around £150m of VAT is not charged as a result of tax-free airside sales. Legislating to extend the relief to the EU could significantly increase the cost of the scheme and result in a large amount of deadweight loss by subsidising spending from EU-bound passengers which already happens.

This view demonstrates a fundamental lack of understanding by HM Treasury officials. This statement makes the assumption that all the sales that look place in the last 12 months would have taken place whether VAT was exempted or not. Furthermore, airports do not compete with the UK High Street – they compete with their international counterparts

The reality is that passengers shopping in duty and tax free are extremely price conscious, and often plan their purchases in advance. Most passengers – knowing that an item will be available at a cheaper price overseas if VAT is included in the UK – will simply defer their purchase.

Independent Economic Analysis by York Aviation has shown that the withdrawal of the Airside VAT ESC will remove up to £2.1bn from the UK economy, and put thousands of jobs up and down the country at risk.

20. Due to the nature of the relief as a concession, there is no requirement for passengers to receive any of the VAT relief. As a result, it is applied inconsistently by retailers and forms part of a complex financing arrangement in airports. The scheme received negative media coverage in 2015, with passengers unhappy that there was no discernible price reduction on many goods. A HMRC review concluded that the relief was being passed on to customers but not necessarily in a transparent way:

This is misleading. The industry acknowledges that a small number of retailers were rightly criticised by HM Treasury and HMRC in 2016. At that time the UK Travel Retail Forum and Airport Operators Association worked constructively with the Government to deliver the industry Code of Practice for Airport Retailers; VAT Relief Concession (click link for further detail). In September 2016 HMRC a statement support of the Code (see end note)[ii]

Since 2016, the industry has regularly attempted to seek feedback on the implementation and effectiveness of the Code from HMRC. To date HM Treasury and HMRC have not provided further input to the Code – nor indicated before September 2020 that they had enduring concerns around the passing on of savings to customers.

Similarly, beginning in early 2019, UKTRF and World Duty Free began offering Treasury officials a briefing on World Duty Free's intended post-Brexit pricing model (again demonstrating industry commitment to transparent and fair pricing).

HM Treasury has declined all offers to meet on this subject to date.

- *Some retailers retain the VAT relief and offset their operating costs. Others use some of the saving to 'lower' prices for both non-EU and EU-bound passengers. The ESC was intended to relive goods from VAT which are sold for export but it is being applied to sales of goods for immediate consumption, e.g. snacks and drinks.*
- *UK residents can also use the scheme for goods they will likely use in the UK. For example, retailers can sell a camera VAT-free to a UK resident passenger on departure, who then brings the camera back into the country on arrival for long-term use, without having paid tax. If this camera was purchased on the high street, then VAT will be accounted for. The use of the ESC in this way directly undercuts the high street.*

UKTRF has written to the Exchequer Secretary addressing both of the above points in the last two weeks with clear, practical proposals for alternative policy settings that address the concerns above. To date Treasury has not provided substantive feedback.

We propose to:

- Apply VAT to snacking and soft drink products sold at airports – including all snack / confectionary / fine food products below an agreed size or volume.
- Require retailers to pass on VAT savings direct to passengers at point of sale, allowing a single price to be displayed, but passing a full VAT refund to international passengers.
- Actively inform passengers that it is illegal to re-import goods without paying the necessary VAT.

UKTRF and industry have submitted these detailed proposals to HM Treasury mid-October and are yet to receive acknowledgement that they are being seriously considered, or a response. We stand ready to work with Government on solutions to their concerns.

Tax-free airside: consultation with industry

20. [sic] The consultation did state that the Government was initially minded to extend tax-free sales to EU passengers. However, the consultation document also discussed the Government's concerns with the operation of the scheme and asked about the impacts of abolishing airside tax-free sales. In particular, paragraph 4.26 asks an open question about whether the Government should extend airside tax-free sales and paragraph 4.27 asks specifically about the impacts of abolishing airside tax-free sales.

UKTRF and industry met with HM Treasury and HMRC on a number of occasions in 2019 and 2020. At no stage was it made clear that the abolition of the Airside VAT ESC was a material risk, instead the consultation document in March 2020 stated clearly that the Government was "minded to extend airside tax-free sales to those travelling to the EU".

Further, in early 2019, the Chancellor announced that the UK government were planning to maintain the ESC on airside tax free sales in the event of a no-deal Brexit. This would have allowed tax free sales to continue for all passengers leaving the UK, apart from those travelling to the European Union. This was presented as a temporary measure, which would allow for a permanent regime for airside tax free sales to be developed and agreed. These concepts were communicated to industry in March 2019 but kept confidential till later in the year. See below a slide published by HM Treasury in September 2019 at the end of this briefing note.[iii]

The nature of perceived legal complexities surrounding airside tax free sales to travellers were not communicated in the 2020 UK government consultation on duty and tax free sales post Brexit. Some (but not all) consultation participants have been verbally briefed on the detail of these complexities by HM Treasury, though written detail of those complexities has only been released by Treasury in mid-October 2020. We note this 'myth busters' document has not been shared proactively with industry.

<u>Conclusion</u>

Despite these clear statements in the consultation document, the Government's subsequent decision in September 2020 reflected an abrupt change in policy direction. A material portion of the aviation, travel, tourism and retail industries have clearly stated the severe economic damage this decision will inflict. Only one respondent to the Government's consultation (out of 73) disagreed with the Government's stated intention to extend airside tax free shopping to EU travellers after Brexit.

[i] **<u>Further legal detail</u>**

A combination of the *Value Added Tax Act 1994 (VATA 1994), VAT Notice 48 (12 September 2017)* and *HMRC guidance VEXP50305* means that where goods are sold airside through a tax free shop to a passenger bound for a non-EU destination, HMRC are satisfied that this constitutes the export of those goods by that shop to a non-EU destination, so that the supply may be is zero rated under *s.30(6) VATA 1994.*

Furthermore, the precedent set in *R v CIR ex parte Wilkinson [2005] UKHL 30* remains consistent with the application of the airside ESC – it is clear that Parliament intended that where a person exports goods to a territory outside the EU, those goods should be zero-rated for VAT purposes.

What the Airside ESC does is practically interpret that principle. A person operating a tax-free shop who sells goods to a person leaving the EU is exporting goods to a territory outside the EU for the purposes of *s30(6) VATA 1994*. Further, the wording of *s30(6) VATA 1994* itself makes it very clear that this is an area where Parliament intended that HMRC should have more discretion afforded to it than it has under its normal collection and management powers.

The test, therefore, is simply whether HMRC is satisfied that the supplier exported goods to a place outside the Member States.

While *s30(6) VATA 1994* prevents HMRC from extending the ESC before the end of the transition period, <u>it clearly does not constrain HMRC from doing so after the end of the transition period</u>.

The *Cross-border Trade Act 2018* will further amend *VATA 1994* to ensure the UK's VAT on exporting goods position does not discriminate between exports to the EU and other non-EU territories after the end of the transition period.

The material effect of this will be to change the test on whether a good can be zero rated to <u>whether HMRC are satisfied that a supplier has exported the goods.</u>

Article 147 of the EU VAT Directive which states that only non-EU residents can buy tax free goods, does not apply to airport tax free sales as our shops have always been exempted from this via *Article 146 of the same Directive.*

It would also be rather unusual for the UK Government to change its interpretation of the EU VAT Directive on exiting the EU, after having allowed such practices since adoption of the VAT Directive in 2006.

On this basis therefore, there is nothing preventing the Government from continuing the ESC in its present form. Furthermore, if, as anticipated, English law changes to permit zero-rating of exports to the EU, the ESC can simply be amended to bring it in line with those changes, as this is clearly the will of Parliament, and therefore not in breach of the Wilkinson Decision.

[ii] **Statement from HMRC in September 2016 regarding the Code of Practice:**

"HMRC welcomes the United Kingdom Travel Retail Forum's intention to ensure that airside retailers improve transparency by introducing the code of practice for airport sales.

We will work with the industry to evaluate the effectiveness of the code and take this into account in our consideration of longer-term developments for airside retail VAT and retail exports more generally."

[iii] **Slides presented by Treasury to industry in 2019 showing the Government's intention to extend the Airside VAT ESC beyond Brexit in the event of no deal.**