[2016] UKFTT 0372 (TC)

TC05126

Appeal number: TC/2014/05466

VAT – Zero-rating for equipment or appliances designed solely for use by handicapped persons- Value Added Tax Act 1994, Sch 8, Group 12, item 2(g) – whether mobile device with software installed met the requirements – yes, appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

IANSYST LIMITED **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE ABIGAIL MCGREGOR
HELEN MYERSCOUGH

Sitting in public at Cambridge County Court on 25 January 2016

Ian Litterick, Executive Chairman of the Appellant, for the Appellant

Alan Bates, Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

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DECISION

Introduction

1. The Appellant, Iansyst Limited ("**Iansyst**") appeals against a decision on review by HMRC dated 9 September 2014 in which HMRC confirmed its earlier decision that supplies of mobile phones and tablets with a software package pre-installed ("**Capturatalk**") do not qualify for zero-rating for the purposes of VAT.

Preliminary issue on the appeal

2. The decision under appeal was a forward looking appeal, i.e. did not relate to any actual supplies of mobile devices with Capturatalk installed.

3. The appeal was made under s 83(1)(b) of Value Added Tax Act 1994 ("**VATA 1994**"), which provides that an appeal lies to the tribunal with respect to "the VAT chargeable on the supply of any goods or services".

4. We concluded that, although there were no actual supplies in question, the Tribunal could consider an appeal against a decision of HMRC on whether a zero-rating applied as that decision affected the amount of "VAT chargeable on the supply of goods". We also concluded that our decision could only relate to the law in place at the date of that decision, i.e. 9 September 2014.

Evidence

5. Iansyst submitted:

(1) a witness statement from Mr Ian Litterick, executive chairman of Iansyst;

(2) a bundle of documents including original patent applications and historical correspondence with HMRC about both Capturatalk and other items supplied by Iansyst; and

(3) oral evidence of both Ian Litterick and John Lamb, of the British Assistive Technology Association.

Law

6. The relevant zero-rating provisions are found in Group 12 of Schedule 8 to VATA 1994 which allows for zero-rating of certain drugs, medicines and aids for the handicapped. Specifically, zero-rating is allowed under Item 2(g) for:

> (Item 2) The supply to a handicapped person for domestic or his personal use, or to a charity for making available to handicapped persons by sale or otherwise, for domestic or their personal use, of
>
> …(g) equipment and appliances not included in paragraphs (a) to (f) above designed solely for use by a handicapped person.

7. For the remainder of this decision "**Item 2(g)**" refers to this item of Group 12 of Schedule 8 to VATA 1994. Although "handicapped persons" might not be the phrase

of choice in 2016, it will be used throughout this judgment because that is the wording found in the legislation.

Facts

8. A number of facts were agreed between the parties, as follows:

5 (1) Iansyst carries on a business of supplying IT software and hardware for persons with disabilities, including visual impairments and persons with dyslexia;

(2) Iansyst was at the relevant time (and continues to be) registered for VAT;

(3) Capturatalk is software that (when installed on a mobile phone or tablet
10 computer (to be referred to in this decision as "**mobile devices**")):

(a) reads text aloud, e.g. can read out the text of web-pages navigated to on the mobile device;

(b) can convert text in a picture taken by the camera on the mobile device and then read it aloud;

15 (c) can write text from speech, i.e. when dictated to;

(d) contains a link to a dictionary; and

(e) assists the user to distinguish between homophones, e.g. there, their, they're;

(4) Capturatalk is installed on mobile devices only (not on laptop or desktop
20 computers); and

(5) a mobile device is a piece of "equipment" for the purposes of Item 2(g).

9. Since the appeal did not relate to any specific supplies of mobile devices, we did not consider the meaning of the pre-amble of Item 2, i.e. the requirement that the supply had to be made to "a handicapped person for domestic or his personal use, or
25 to a charity for making available to handicapped persons by sale or otherwise, for domestic or their personal use"; it was agreed that this condition would also have to be met in order for zero-rating to apply to any particular supply.

The issue under appeal

10. The issue under appeal can be very simply put: are supplies of mobile devices
30 with Capturatalk pre-installed on them entitled to zero-rate under Item 2(g)? In order to answer that question, we must decide whether the mobile devices so supplied are "designed solely for use by a handicapped person".

11. There is a secondary issue about the applicability of an extra-statutory concession ("**ESC**") and the jurisdiction of the Tribunal regarding ESCs which is
35 discussed in paragraphs 35-40.

Parties arguments

Iansyst's arguments on item 2(g)

12. Iansyst submitted that:

(1) the installation of the Capturatalk software onto a mobile device renders the mobile device an assistive technology ("**AT**") system which has been designed solely for use by handicapped persons, because the process of putting Capturatalk onto it alters the design of the whole system;

5 (2) non-disabled persons would not buy a mobile device with Capturatalk installed on it because the parts of the software that they would use are also available for free as downloadable apps, which supports the conclusion that the AT system as a whole has been designed solely for use by handicapped persons (and in any event, even if they did, the purchase would not be zero-rated 10 because it would not be supplied to a handicapped person in accordance with item 2(g)); and

(3) although Iansyst does not make alterations to the physical characteristics or hardware of the mobile devices, it does test the mobile devices before deciding whether to install Capturatalk to ensure that the mobile device meets 15 the needs of the software, in particular the quality of the camera and the anti-shake mechanisms associated with it. Without sufficient quality in either of those elements of the mobile device, the Capturatalk software would not work properly (in particular the part of Capturatalk that converts photographs of text into speech); Iansyst submits that this process is part of the creation of the AT 20 system.

HMRC's arguments on Item 2(g)

13. HMRC submitted that the provisions which relate to zero-rating in the UK legislation derive from a "transitional saving" in Article 110 of VAT Directive 2006/112/EC, which provides:

25 "Member States which, at 1 January 1991, were granting exemptions with deductibility of the VAT paid at the preceding stage or applying reduced rates lower than the minimum laid down in Article 99 may continue to grant those exemptions or apply those reduced rates.

The exemptions and reduced rates referred to in the first paragraph must be in 30 accordance with Community law and must have been adopted for clearly defined social reasons and for the benefit of the final consumer."

14. HMRC submitted that the cases of *Talacre Beach Caravan Sales Ltd v Customs and Excise Commissioners* [2006] STC 1671 (paragraphs 22 – 24) and *Commission v* 35 *Luxembourg* [2015] STC 1714 (paragraph 38) supported its contention that the zero-rating provisions (which equate to the concept of 'exemptions with deductibility of the VAT paid at the preceding stage' within the VAT directive) are to be interpreted strictly and cannot be enlarged beyond the position in domestic law on 1 January 1991.

40 15. HMRC submitted that the mobile devices that are being supplied by Iansyst are the same before the installation of the Capturatalk software as any other mobile devices available on the market and that the installation of the software does not change the item itself. The phone is still a phone and the tablet computers are still tablet computers. Capturatalk, like any other piece of software or application, uses the 45 mobile device as a platform but does not change the device.

16. HMRC also submitted that the phrase "designed solely for use by handicapped persons" must be looked at from the perspective of the equipment being supplied "as a whole" and that, while the software enables the device to be used in a particular way, it does not turn the device into something designed solely for use by a handicapped person.

17. HMRC also submitted that the Capturatalk software itself had not been designed solely for use by handicapped persons because all the elements of the software were of general use by non-handicapped persons, e.g. voice recognition software is used for dictation.

Discussion

Interpretation of zero-rate provisions

18. The guidance of the Court of Justice of the European Union in *Talacre Beach* is clear that zero-rating provisions, as derogations from the general principle that supplies of goods and services are taxable, should be interpreted strictly.

19. However, a strict interpretation is not the same as a restrictive interpretation. As Chadwick LJ said in *Expert Witness Institute v Customs and Excise Comrs* [2002] STC 42 at [17] (and endorsed by the Court of Appeal in *InsuranceWide.com Services Ltd v Revenue and Customs Comrs, Revenue and Customs Comrs v Trader Media Group Ltd* [2010] STC 1572 at [83]):

> "A "strict" construction is not to be equated, in this context, with a restricted construction. The court must recognise that it is for a supplier, whose supplies would otherwise be taxable, to establish that it comes within the exemption, so that if the court is left in doubt whether a fair interpretation of the words of the exemption covers the supplies in question, the claim to the exemption must be rejected. But the court is not required to reject a claim which does come within a fair interpretation of the words of the exemption because there is another, more restricted, meaning of the words which would exclude the supplies in question."

20. Following that guidance, the question we must answer is whether a fair interpretation of the words "designed solely for use by handicapped persons"' includes the supplies of mobile devices with Capturatalk software installed.

Interpretation of Item 2(g)

21. The Upper Tribunal has considered the interpretation of Item 2(g) in *British Disabled Flying Association v Revenue and Customs Commissioners* [2013] STC 1677 ("**BDFA**").

22. The issue in *BDFA* was whether two aircraft, which had been altered post-manufacture to allow them to be piloted by a handicapped person, were designed solely for use by a handicapped person as required by item 2(g).

23. The Upper Tribunal, when considering the meaning of the word "designed" drew a distinction between the intended use of the item and its characteristics (para 28):

> "We consider that, looking at the other paragraphs of item 2 of Group 12, 'designed' is used in conjunction with 'adapted' and refers to the physical characteristics of an item rather than its intended use. The required intended use is described in the opening words of item 2 and it would, therefore, be unnecessary to refer to it again. For those reasons, we consider that 'designed' in item 2(g) refers to the physical characteristics of the equipment that make it suitable for use by a handicapped person."

24. The Upper Tribunal also concluded that it was at the time of supply that this question had to be determined and "that seemed to us to point towards an interpretation of 'designed' as referring to the present rather than the historic design of the object" (para 29).

25. The Upper Tribunal referred in *BDFA* to "physical characteristics that make it suitable for use by a handicapped person". That case concerned aircraft where the elements that were altered were physical items such as pedals and levers and the disabilities being considered were physical ones, therefore there was no need to consider characteristics that were not physical ones. In this case we are concerned with technology and a disability that affects the way in which a person can interpret information and does not necessarily require physical adaptation. Our interpretation of *BDFA* is that it can be read to refer to any "characteristics of the equipment that make it suitable for use by a handicapped person", not just physical ones.

26. Applying those principles to the supply of a mobile device with Capturatalk installed, we must decide whether, at the time of supply, the item being supplied has the characteristics of an item that is designed solely for use by handicapped persons. We need not look at the original patent applications for the building blocks of Capturatalk and the purpose for which those elements were designed at that time, rather the package that is being supplied to the handicapped person.

27. As set out above, when we are determining this question, we must not be left in doubt whether a fair interpretation of the words "designed solely for use by a handicapped person" covers the supplies in question. If we are left in doubt, we must reject the appeal.

28. The requirement for the design to be "solely" for handicapped persons would be very difficult to meet if it is to mean that the item in question was not in any way useful to a non-handicapped person. It is clear that a mobile device and all the elements of the Capturatalk software are capable of use by a non-handicapped person. However, we would follow the opinion of the VAT Tribunal in *Kirton Designs v Commissioners of Customs and Excise* (1987) VAT Decision 2374, that "a product can be designed solely for use by a handicapped person notwithstanding that it is capable of use by a normal person".

29. Therefore we do not find that the fact that a non-handicapped person could and would use a mobile device with similar software installed (e.g. apps for dictation) prevents it from being capable of meeting the requirement of Item 2(g).

30. However, we agree with HMRC's submission that it is the package supplied 'as a whole' that must be considered. This conclusion is also consistent with the submissions of Iansyst that the item supplied should be considered as an AT system.

31. We do not find that HMRC's submission that stepping back and finding that what is being supplied is still just a mobile device is a helpful way of addressing the question. In *BDFA,* what was being supplied was still an aircraft used for flying. The fundamental purpose of the item being supplied had not changed. What had changed was the way in which a person might use it.

32. Based on the agreed facts as to what Capturatalk does, we find that once Capturatalk is installed a handicapped person can use the mobile device to access webpages (as on any other mobile device) but, once accessed, the use of the webpage has changed substantially. The user will listen to the content of the web-page rather than read it. The ability of the phone to convert text within a photograph to spoken word is not something that is usually possible with an unaltered mobile device. Therefore we find that the package as a whole allowed a handicapped person to use the device differently from the way in which a non-handicapped person would use it and to use it more effectively than such a handicapped person would be able to use it without the technology installed.

33. Therefore we find that, looking at the package as a whole at the time of supply, the supply of a mobile device with Capturatalk pre-installed would meet the requirements of a piece of equipment designed solely for use by a handicapped person, and should therefore be zero-rated for VAT purposes (provided the conditions of supply in the pre-amble to Item 2 are also met).

34. For completeness, HMRC's submission that the Capturatalk software was itself not designed solely for use by handicapped persons is not relevant to the question at hand. The question relates to the supply of a package of a mobile device with Capturatalk installed.

Jurisdiction to consider extra-statutory concessions

35. Given our decision on the application of Item 2(g) set out above, it is not necessary to consider the question of our jurisdiction to consider the application of the ESC. However, we set out our position for the benefit of the parties.

36. The ESC in question was, at the time of the decision under appeal, set out in paragraph 9 of VAT Notice 701/7 (the version of the VAT notice that was published in August 2002). It provided for 'central processors' to be zero-rated if certain conditions were met and/or for a composite rate of VAT to be applied to the sale of computer systems over a period where some elements were entitled to zero-rate and others were not.

37. This Tribunal is bound by the decision of the Court of Appeal in *The Trustees of the BT Pension Scheme* [2015] EWCA Civ 713 (para 142) (as applied in a VAT context by *Shanklin Conservative and Unionist Club v HMRC* UKFTT 2015 (para 96)) that an appellant cannot rely on its legitimate expectations arising from the application of an extra-statutory concession in the First-tier Tribunal.

38. Mr Bates had suggested that we might consider the application of the ESC on the basis of the pragmatic approach applied in *The Reform Club v HMRC [2015] UKFTT 0241*. Iansyst were happy to adopt this approach. However, at the hearing, HMRC did not formally consent to the tribunal considering the application of the ESC and therefore this was not an approach we could in fact take.

39. In addition, it transpired at the hearing that both HMRC and Iansyst were of the view that the ESC was not in fact a concession, but rather an aid to interpretation of the legislation. Further in HMRC's view it could not be a concession because that would be applying a zero-rated provision more broadly than is set out in the legislation and therefore contrary to the restrictions of zero-rating provisions as set out above.

40. We heard a number of arguments relating to the meaning of 'central processor' and its application to modern technology when compared to the 'three-box' computers of the 1990s. However, given that we have been able to conclude on the application of the legislation to the facts at hand without need to consider the wording set out in VAT Notice 701/7, we need not come to a conclusion on these points.

41. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

ABIGAIL MCGREGOR

TRIBUNAL JUDGE
RELEASE DATE: 1 JUNE 2016