[2016] UKUT 0104 (TCC)
Appeal number: UT/2013/0023

TYPE OF TAX – keywords - Excise Duty – exemption under art 27(1) of Directive 982/83/EEC – whether conditional refund system for importing manufacturers in s 4 FA 1995 adequately implemented the exemption – held: on the facts the appellant importers had a directly effective right to exemption which was not given effect by s4 and which could not be given effect by excising the conditions from s4 – the charge to excise duty should be read as subject to that right – appeal allowed.

UPPER TRIBUNAL
TAX AND CHANCERYCHAMBER

REPERTOIRE CULINAIRE LTD **Appellant**

- and -

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

TRIBUNAL: MR JUSTICE BIRSS
JUDGE CHARLES HELLIER

Sitting in public in the Rolls Building on 18 and 19 January 2016

Hugh Mercer QC and Philippe Dewast, Advocate, instructed by Wilkins Kennedy for the Appellant

Kieron Beal QC, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. This appeal relates to two assessments to excise duty made by HMRC on Repertoire Culinaire Limited ("RCL") in relation to various cooking liquors it imported. The smaller of the assessments is for £5,884 and relates to a quantity of cooking liquors which were in RCL's warehouse; the larger is for £53,853 and relates to cooking liquors which RCL had sold.

2. In 2002 HMRC seized cooking wine, cognac and port ("cooking liquors") which had been imported by RCL and, following a visit to RCL, made the assessments under appeal. RCL sought restoration of the seized goods and HMRC refused. Cooking liquors are alcoholic drinks to which have been added substantial amounts of salt and pepper. This renders them undrinkable but does not prevent their use as cooking ingredients.

3. In a decision of 2012 the FTT set aside the decision made by HMRC not to restore the seized goods but dismissed RCL's appeals against the assessments. In the course of the appeal the FTT had referred four questions to the CJEU. The judgment of the CJEU is recorded *in Repertoire Culinaire Ltd v HMRC* C-163/09 [2011] STC 465 ("*RCL*"). No appeal is brought against the FTT's decision in relation to the restoration.

4. In summary on this appeal RCL says that the cooking liquors were exempt from duty by virtue of the direct effect of Article 27 of Council Directive 92/83/EEC (the "Directive").

5. HMRC say it is not that simple. They contend that (i) the cooking liquors were liable to duty on import as the result of domestic legislation, which was authorised by the Directive; (ii) in implementing the Directive the UK took advantage of Article 27(6) and gave effect to the exemption in Article 27 by a refund scheme set out in section 4 Finance Act 1995; (iii) a refund scheme presupposes the payment of the duty in the first place; and (iv) RCL was always under an obligation to pay the duty and, because the duty has never been paid, did not satisfy the requirements for a refund under that scheme. Hence the appeal should be dismissed. RCL must pay the assessed duty and, if it wishes, it should apply for a refund. If RCL can prove it is entitled to a refund of that duty then a refund will be given.

6. RCL answer this in a number of ways. It says that HMRC's approach is wrong because it makes unreasonable demands on RCL. It says that there can be no serious argument but that the cooking liquors in issue were used in such a way as to fall within the exemption, but what HMRC is doing is seeking to impose on RCL a requirement to establish today, 14 years after the relevant events, what specifically happened or was going to happen to each individual batch and how it was used by each customer. That is unreasonable and RCL should not be required to do it. RCL argues that this approach does not give effective protection to RCL's EU law rights. RCL says it has a right to exemption under the Directive. That right is directly

effective by an individual against the State and must be given effect to. The FTT's decision under appeal does not do that.

The EU Legislation

7. Article 19 of the Directive provides that:

> Member States shall apply an excise duty to ethyl alcohol in accordance with this Directive.

8. Article 20 defines the term ethyl alcohol for the purposes of the Directive.

9. Article 27 provides:

> 1. Member States shall exempt the products covered by this Directive from the harmonised excise duty under conditions which they shall lay down for the purpose of ensuring the correct and straightforward application of such exemptions and of preventing any evasion, avoidance or abuse:
>
> ...
>
> (f) when used directly or as a constituent of semi-finished products for the production of foodstuffs, filled or otherwise, provided that in each case the alcoholic content does not exceed 8.5 litres of pure alcohol per 100 kg of the product for chocolates, and 5 litres of pure alcohol per 100 kg of the product for other products.
>
> …
>
> (6) Member States shall be free to give effect to the exemptions mentioned above by means of a refund of excise duty paid.

The Domestic Legislation.

10. The Alcoholic Liquor Duties Act 1979 ("ALDA") provides, in Part IV, section 54 and 55 for a charge to excise duty on the import into the UK of spirits, wine and made wine, and the Excise Goods (Holding, Movement Warehousing and REDS) Regulations 1992 (the "REDs Regulations") provide for the time at which the duty becomes payable.

11. Section 4 Finance Act 1995 provides:

> "4 **Alcoholic ingredients relief**
>
> (1) Subject to the following provisions of this section, where any person proves to the satisfaction of the Commissioners that any dutiable alcoholic liquor on which duty has been paid has been-
>
> (a) used as an ingredient in the production or manufacture of a product falling within subsection (2) below, or
>
> (b) converted into vinegar,
>
> he shall be entitled to obtain from the Commissioners the repayment of the duty paid thereon.
>
> (2) The products falling within this subsection are-

(a) any beverage of an alcoholic strength not exceeding 1.2 per cent,

(b) chocolates for human consumption which contain alcohol such that 100 kilograms of the chocolates would not contain more than 8.5 litres of alcohol, or

(c) any other food for human consumption which contains alcohol such that 100 kilograms of the food would not contain more than 5 litres of alcohol.

(3) A repayment of duty shall not be made under this section in respect of any liquor except to a person who-

(a) is the person who used the liquor as an ingredient in a product falling within subsection (2) above or, as the case may be, who converted it into vinegar;

(b) carries on a business as a wholesale supplier of products of the applicable description falling within that subsection or, as the case may be, of vinegar;

(c) produced or manufactured the product or vinegar for the purposes of that business;

(d) makes a claim for the repayment in accordance with the following provisions of this section; and

(e) satisfies the Commissioners as to the matters mentioned in paragraphs (a) to (c) above and that the repayment claimed does not relate to any duty which has been repaid or drawn back prior to the making of the claim.

(4) A claim for repayment under this section shall take such form and be made in such manner, and shall contain such particulars, as the Commissioners may direct, either generally or in a particular case.

(5) Except so far as the Commissioners otherwise allow, a person shall not make a claim for repayment under this section unless-

(a) the claim relates to duty paid on liquor used as an ingredient or, as the case maybe, converted into vinegar in the course of a period of three months ending not more than one month before the making of the claim; and

(b) the amount of the repayment which is claimed is not less than £250.

(6) The Commissioners may by order made by statutory instrument increase the amount for the time being specified in subsection 5(b) above; and a statutory instrument containing an order under this subsection shall be subject to annulment in pursuance of a resolution of the House of Commons.

(7) There may be remitted by the Commissioners any duty charged either-

(a) on any dutiable alcoholic liquor imported into the United Kingdom at a time when it is contained as an ingredient in any chocolates or food falling within subsection (2)(b) or (c) above; or

(b) on any dutiable alcoholic liquor used as an ingredient in the manufacture or production in an excise warehouse of any such chocolates or food.

(8) This section shall be construed as one with the Alcoholic Liquor Duties Act 1979, and references in this section to chocolates or food do not include references to any beverages."

12. Thus the UK's domestic legislation does not refer to an exemption from duty as such but instead provides, in section 4 FA 1995, for the refund of duty paid subject to a number of requirements. The requirements are:

(1) that the duty to be repaid has been paid, and a claim for a repayment made in prescribed form;

(2) that the person making the claim is a manufacturer of the foodstuffs in which the product the liquor has been used and a wholesaler of those products (for the purposes of this Decision we refer to such a person as a "manufacturer" and this condition as the Manufacturer Condition);

(3) that the claim be made for a period of three months (the Time Condition);

(4) that the amount of the repayment claimed should be not less than £250 (the Amount Condition).

13. The rationale for each of these requirements is clear enough. The first one reflects the simple point that a refund presupposes payment in the first place. The idea behind the second requirement (the Manufacturer Condition) is that it will be the manufacturer who is in a position to know and demonstrate what the liquor has actually been used for. The provision identifies the person who can claim and receive the repayment. The third requirement (the Time Condition) sets a period within which the refund claim must be made and the fourth (the Amount Condition) prevents claims for small amounts. We refer to the Manufacturer, the Time and the Amount Conditions as the Three Conditions.

14. RCL was not a manufacturer. It was instead an importer and wholesaler of such cooking liquors. It is thus that it did not fall within the provisions of section 4 conventionally construed without reference to EU law. It could not satisfy the Manufacturer Condition.

The UK administration of the Scheme

15. Section 4(4) requires that a claim be in such form as HMRC shall direct. At the relevant time HMRC specified a form which contained the following:

"**You may only claim relief if you are a manufacturer who uses alcoholic ingredients in the production of eligible articles for wholesale supply**

You must make a separate claim for each set of premises where alcoholic ingredients are used to make eligible articles

…

Claims must-

- **cover a period of not less than three months…**
- **amount to at least £250 (you may carry over claims until you reach £250.**

…I declare that the information given on this form…is true and complete.

16. The form then sought details of the products made using the alcoholic ingredients and the quantities so used.

17. It is clear that a person who was not a manufacturer would have some difficulty in making a claim using this form.

The reference to the CJEU

18. In its decision in 2009 the FTT referred four questions to the CJEU. Dealing with them in the same order the CJEU did: the first question asked if cooking liquors are subject to excise duty under the Directive. The next question addressed was the third question. It was whether, if they are liable to duty, cooking liquors are exempt under provisions in Art 27(1). Then the court addressed the fourth question, which was whether the UK was bound to accept treatment of the cooking liquors by the exporting State, France, as conclusive. Finally the second question related to s4 of the Finance Act, asking whether the Three Conditions are consistent with the UK's obligation to give effect to the Directive.

19. RCL lost on the first question, which had been at the heart of its case up to that point. RCL had argued that cooking liquors were not dutiable at all because of their unpalatable nature. CJEU held that the cooking liquors fell within Article 20. The decision on the third question did not go entirely in RCL's favour either. Rather than cooking liquors being exempt by definition under the relevant provision (held to be Art 27(1)(f)), the CJEU held that they would only be exempt as long as they were used in the production of foodstuffs (and the alcoholic content of the foodstuffs satisfied the relevant criterion).

20. RCL did not win on the fourth question either. The decision of the CJEU was that while the UK must generally abide by a decision made on duty and exemption by the exporting State, it need not do so if the decision was demonstrably incorrect. When the case returned to the FTT in 2012, the tribunal held that in this case the UK was not bound by the treatment applied in France in this case. Thus the cooking liquors were dutiable in the UK.

21. However on the final question (the second question) RCL had much more success. A key point was the legality of the Three Conditions. The CJEU decided that the exemption depends on the end use of the products [paragraph 49] and decided [paragraph 53] that although Member State may give effect to the exemption by means of a refund of excise duty paid depending on how the products in question are used, the Member State:

> "cannot, on the other hand, make the application of that exemption conditional on compliance with conditions which are not proven by concrete, objective and verifiable evidence to be necessary to ensure the correct and straightforward application of such an exemption and to prevent any evasion, avoidance or abuse."

22. Turning to the facts, the CJEU doubted that the Three Conditions in section 4 were justifiable, saying:

> "The evidence submitted to the Court seems to indicate that the [Three Conditions] are not necessary" for those purposes. … However it is for the national court … to ascertain …" [paragraphs 54 -55]

The return of the appeal to the FTT.

23. When the appeal returned to the FTT a procedural problem arose. The case up to that time had been an appeal against HMRC's refusal to restore the seized cooking liquors. The effect of *HMRC v Jones and Jones* [2011] EWCA Civ 824 limited the issues that RCL could raise and prevented the FTT from addressing the underlying issue which both sides wished to deal with, i.e. the liability to excise duty of the cooking liquors. By agreement with RCL, HMRC and the FTT, the appellant brought a fresh appeal, out of time, against a Departmental Review of the two assessments for excise duty referred to in paragraph 1 of this decision. The fresh appeal was called the new appeal in the FTT whereas the appeal against the refusal to restore was called the original appeal. RCL has not sought to appeal to the Upper Tribunal any issues arising from the original appeal. What is before us is the new appeal.

24. Following the CJEU's decision, before the FTT HMRC did not seek to offer evidence to support the Three Conditions. As they repeated before us, HMRC said that they "did not rely" on those parts of section 4 which contained them. While this was a pragmatic course for HMRC to adopt, we believe it may have led to error by taking the focus away from a consideration of the consequences of the CJEU's decision on section 4.

25. The new appeal raised two points. The first was whether the UK was bound by the treatment by France of the cooking liquor. As mentioned already the FTT held the UK was not bound [paragraphs 88-97] and there is no appeal from that decision before us. The FTT then considered the liability of cooking liquor to excise duty owed to HMRC in paragraphs [98 - 102]. In those paragraphs the FTT does not address expressly the Three Conditions but concentrates on the nature of the requirement that the cooking liquor had to be used in order to be exempt and whether the adoption of a refund scheme meant that duty was payable but could be refunded on proof of use:

> "98. We turn now to consider whether, in the light of the Judgment of the Court of Justice, the UK could properly require the payment of excise duty on the cooking liquors in issue pursuant to section 4, FA 1995.
>
> "99. Here we consider that Mr Beal is on strong ground when he bases his submissions on [53] of the Judgment – the Court of Justice's recognition that a Member State may give effect to the exemption under Article 27(1)(f) of the Excise Directive by means of a refund of excise duty paid, depending on how the products in question are used.

> "100. We do not accept the submission of Mr Mercer and Mr Dewast that the requirement to pay duty before it can be refunded on proof of a qualifying use of the products concerned is a condition, to compliance with which the exemption is subject. It is a direct consequence of the explicit link in the language of Article 27(1)(f) of the Excise Directive between the exemption and the use of the products to be exempted. Once a use within Article 27(1)(f) is shown the duty paid must be refunded. It does not prejudice the unconditional nature of the exemption, because once the use is shown the benefit of the exemption accrues unconditionally.
>
> 101. Nor do we accept that HMRC is guilty of any abuse of process in advancing the contention that an exemption with refund of excise duty paid is a legitimate implementation of the [Directive]. …
>
> 102. We conclude, therefore, that excise duty was properly payable on the cooking liquors…in respect of which the assessments were raised on 18 July 2002. No 'reading down' of the guidance given by the Court of Justice into section 4, FA 1995, or invocation of the direct effect of Article 27(1)(f) of the [Directive] can avail RCL on this point. The establishment in the UK of a system of exemption with refund of excise duty paid is, in our judgment, immune to either of these attacks."

26. Thus the FTT held that in the context of the adoption of a refund scheme, RCL had an absolute duty to pay the tax, albeit with a right to repayment. The excise duty had become due and, since it had not been paid, the condition for refund was not satisfied.

27. In reaching this conclusion the FTT had in effect concluded that the refund scheme in section 4 could be so construed or partially disapplied in a way which gave effect to any rights RCL had under the Directive. The UK had lawfully given effect to the right of exemption from duty by means of a right to repayment.

The Parties' Arguments in more detail

28. Mr Beal says that because section 4 must be read as not incorporating, and as never having incorporated, the Three Conditions, at all times it has provided a regime which gave effect to RCL's rights under Article 27. In other words while the Three Conditions (or at least the Manufacturer Condition) excluded RCL from obtaining a refund under section 4 as it was enacted, by reading the section without those conditions, RCL was not excluded from claiming a refund. Therefore any right to an exemption which RCL had in relation to the goods in issue has been given effect to by a refund of duty paid. As a result RCL's obligation to pay the duty remained, and its EU law right was only to a refund. That refund was only available if it had paid the duty, made a claim and shown that the goods had been used in the relevant way. He says that the FTT made no finding as to the use to which the goods sold by RCL had been put. The UK is entitled to proof of the end use of the goods. Without such proof RCL has no right to exemption.

29. Mr Mercer acknowledges that the FTT did not make an explicit finding as to whether or not RCL satisfied the use condition in relation to the goods in issue, but says that other factual findings in the decision are an adequate basis for concluding that the cooking liquors (at least those actually sold by RCL) were in fact used for a qualifying purpose. He says that the FTT should have found that the use condition was satisfied.

30. As a result he says RCL had an enforceable EU law right to exemption from duty under Article 27. He argues that the mechanism adopted by the UK did not give effect or effective protection to that right:

(1) section 4, as it stood at the date of the assessment, excluded RCL from its scope because it was not a manufacturer;

(2) HMRC's administrative practice provided no route by which RCL could claim the exemption to which it was entitled;

(3) section 4 cannot be treated as moulded so as to permit (or to have permitted) RCL to have made the claim. That is because either

(a) the section should be completely disapplied leaving RCL with a direct right to exemption unalloyed by any refund system; or

(b) even if the section is moulded so as to delete the Three Conditions, it did not, in 2002, give effect to RCL's rights to exemption (by converting it to a right to a refund) either because such moulding could not be read back into 2002, or because the hurdles which the domestic legislation in its form at the time and HMRC practice placed on RCL's exercise of its right did not satisfy the principle of effectiveness.

31. RCL also adopts an argument discussed in the oral submissions, as follows. The section 4 regime as enacted could be regarded as a scheme for refunds for manufacturers. That regime may have had features which were precluded by EU law (in the form of the Time and Amount Conditions), but the effect of a finding that those two conditions cannot be supported is to remove them from the manufacturer's refund scheme. A manufacturer's refund scheme without those conditions is compliant with EU law as a way of giving effect to a manufacturer's Art 27 rights.

32. However by limiting the refund to manufacturers, the UK has not given effect to the right to exemption held by other persons under Art 27, either by direct exemption or by giving effect to the exemption via a refund. Those persons are entitled to exemption one way or another, but no exemption is provided for in section 4. Therefore section 4 must be read as subject to that right held by those persons. There is nothing which permits HMRC to seek to give effect to that right via a refund.

Discussion

33. Inherent in HMRC's argument is the proposition that the Three Conditions should be treated as struck out with retrospective effect and that RCL's rights should be judged against a scheme which, so construed, permitted RCL to obtain a refund at the

time. Under such a scheme RCL had an obligation to pay duty and the assessments were valid.

34. This is an appeal against an assessment and we are not directly tasked with declaring the effect of EU rights on section 4 as a whole or the Three Conditions in section 4; but, by not having produced to the FTT the evidence of their necessity required by the CJEU, and by their concession before us that they do not intend to rely on the Three Conditions, HMRC effectively ask us to treat them as removed from section 4.

35. RCL's complaint is that the way in which HMRC contend section 4 should be read does not give effect to RCL's EU law right to be exempt from duty under Art 27. On the other hand HRMC's submission is that the only right RCL has is a right under section 4, in its form which is compliant with EU law, and that is a right to a refund *after* it has paid the duty. The problem on this appeal is that these submissions do not meet head on. However unless we know how section 4 is to be construed we cannot determine whether the UK regime gives effect to any EU law rights held by RCL. On the other hand unless we know whether RCL actually does have a directly effective EU law right to be exempt, and what the nature of that right is, we cannot determine whether the UK regime gives effect to that right.

36. It seems to us that in order to deal with this case, it is appropriate and necessary first to consider what the nature of any right under Art 27 is and whether RCL have established such a right in this case. Then we can test that against section 4 of the Finance Act.

37. In *Braathens* (Case 346/97) the CJEU considered the effect of a Directive which provided, in words matching those of Article 27 that "Member States shall exempt…mineral oils supplied for use as aeroplane fuel". The Court held that the obligation to exempt such fuels was sufficiently clear precise and unconditional to confer a right on an individual to rely on it in contesting national rules or asserting a right against the State.

38. The wording in Article 27 differs in two respects from that in *Braathens*: (i) the exemption in Art 27 is for alcohol "used " for food production while the *Braathens* Directive related to oil "supplied for use"; and (ii) the *Braathens* Directive did not encompass an option for the State to give effect to the exemption as a refund.

39. Neither of these differences, in our judgment, prevents the relevant provisions of Art 27 from being sufficiently clear precise and unconditional to confer on an individual a right under the Article on which an individual can rely against the State. We find that the right under Article 27, however it is to be given effect, is one which can be directly enforced by an individual against the State. We turn to consider the scope of that right.

40. Article 27(1) provides that the products will be exempt from duty as long as the products are used for the production of foodstuffs which satisfy Art 27(1)(f). Mr Mercer emphasises that Art 27(6) provides that states may "give effect" to this

exemption by a refund of duty paid. He also referred to paragraph 51 of the CJEU's judgment in which it held that "exemption is the rule, refusal is the exception". His point is that these submissions show that the right created by Art 27 is a right to be exempt and the fact that this right may be given effect to by a refund does not change the fundamental nature of the right conferred by the Article. We agree. Article 27 is not conferring a right to a refund, it confers a right to be exempt from duty in the relevant circumstances. If the State wishes to give effect to that right by a refund mechanism it is free to do so but that is another matter.

41. In order to decide this appeal, the next question therefore is a question which the FTT did not feel it was necessary to answer directly: whether RCL has in fact established that it has a right to exemption under Art 27 in relation to the two assessments.

42. Section 12(4) TCEA 2007 permits this tribunal to make such findings of fact as it considers appropriate if it sets aside and decides to remake any decision of the FTT, having decided that that decision is erroneous on a point of law. Given that, it must be open to this tribunal to make a finding of fact on an issue which the FTT did not decide if it is necessary to do so in order to determine whether the FTT erred in law. Put another way, if the FTT did not make a factual finding in relation to whether the cooking liquors had or had not actually been used for a qualifying purpose the FTT would in effect have determined that even if qualifying use were proven the appeal would fail, and that in our judgment would be an error of law which enables us to make a factual finding on the issue if we are able to do so.

43. Article 27(1)(f) requires that the alcohol be used for a qualifying purpose. It is not enough that it is destined or intended for such use. The CJEU in *RCL* said that "the application of the exemption …depends on the end-use of the products in question" ([49]).

44. Mr Mercer argues that the Article does not demand an absolute requirement of qualifying use, and that the fact that a product is manifestly intended for qualifying use is sufficient. He relies on *Profisa* (Case C-63/06) in this regard. This case concerned the application of Article 27(1)(f) to chocolates containing alcohol imported into Lithuania. The Lithuanian legislation gave exemption to alcohol "intended for use " in chocolates but did not apply the exemption to the alcohol once it had been incorporated into chocolates. The CJEU reviewed various linguistic versions of the Directive and concluded that it required Member States to exempt ethyl alcohol when "used directly in the production of foodstuffs"([18]), It held that the alcohol when contained in the chocolate benefitted from the exemption. We do not regard the Court's failure to comment on the Lithuanian legislation's acceptance of "intention", as diluting its conclusion that the alcohol had to be used. The language of the Court in *RCL* is clearer still: end-use is a condition of the exemption.

45. Did the FTT make a finding in relation to use? In giving permission to appeal the FTT said:

"6.The tribunal decided that there can be no exemption at source of cooking liquors, without any reference to how the products in question are used. The exemption is tied in to end use of the cooking liquors (Decision paragraph 96) Duty is payable on importation subject to refund, once a use within article 27(1)(f) has been shown (Decision paragraph 100).

…

8. The second ground advanced by RCL…is that the [FTT] has failed to determine whether the cooking liquor is exempt. As I have indicated above, I consider that the tribunal has determined this issue in the sense that the cooking liquor is not exempt without proof of an end use within article 27(1)(f)…"

46. Paragraph 100 of the Decision is set out above. In paragraph 96 the FTT had said:

"[96] We also accept Mr Beal's submission that the Judgment of the Court of Justice makes clear that there can be no exemption at source, without any reference to how the products in question are used. We consider that this is inherent in the Court's agreement that 'the Member States may give effect to the exemption under Article 27(1)(f) of [the Excise Directive] by means of a refund of excise duty paid, depending on how the products in question are used' and that it also follows from the wording of Article 27(1)(f) itself, applying the exemption to products 'when used directly or as a constituent of semi-finished products for the production of foodstuffs ...'. The exemption is, as Mr Beal submitted, tied in to the end use of cooking liquors. We cannot accept the submission of Mr Mercer and Mr Dewast that it is sufficient for the purposes of Article 27(1)(f) that the cooking liquors were, as a matter of fact, destined for culinary use…"

47. We agree with the FTT that there can be no exemption at source, in the sense that cooking liquors are not inherently exempt by their nature. They only become exempt if they are actually used for the qualifying purpose. However just because there is no exemption at source, it does not follow that the goods in issue in this appeal have not been established to be exempt. Mr Mercer submitted that the evidence was that they were exempt.

48. Given the way the FTT considered the issues, it did not consider whether the liquor had actually been used for a qualifying purpose. It is apparent that in the paragraphs quoted above that the FTT makes no finding in relation to the use of the products which were assessed. It makes the point, with which we agree, that use means actual end use rather than destined use but makes no express finding. It may be that at this point the FTT had in mind only the goods which were in the Appellant's warehouse (in relation to which the smaller £5k assessment was made), for the best that could be said of them was that they were destined for qualifying use, but the larger assessment was in respect of goods which had been sold and for which there was some evidence relating to end use.

49. We turn to consider Mr Mercer's submission that the cooking liquors that are the subject to this appeal, were indeed used for the qualifying purpose and were therefore exempt under Art 27.

50. Elsewhere in its Decision the FTT made the following findings:

(1) the cooking wine had had added to it salt and pepper (SOF 14);

(2) it was not possible (at any rate as a matter of economic practicality) either to reverse the mixing process to separate the alcoholic beverage from the pepper and salt or to isolate the alcoholic content of the wine in its entirety. (First Decision 14);

(3) this made it unfit for consumption as a beverage, but suitable for use in culinary products (SOF14);

(4) cooking wine when used as an ingredient always yielded a final product with less than 5% alcohol (SOF19);

(5) at [18] The tribunal accepted that the Appellant had sold cooking liquor to 59 restaurants, 3 outside caterers, 3 hotels and one wholesaler, whose customer base consisted entirely of restaurants; that the Appellant's customers use cooking liquor purchased from the Appellant as an ingredient incorporated into foodstuffs; that even before incorporation into a sauce or dish, the alcohol content of cooking wine is never above 5%; and that after incorporation, because of the process of simmering, the alcohol content is further diluted;

(6) in the section of its decision in which it considered the restoration of the seized goods (a decision which is not challenged on this appeal) the FTT said at [110]: "Furthermore, we consider that it is relevant at this point to have regard to the evidence that RCL's use of the cooking liquors which it successfully imported was overwhelmingly likely to lead to their use in the manufacture of foodstuffs giving rise to a qualification for the exemption by way of refund of duty paid. Although no appropriate proof of any specific use has been shown, we find, from the evidence of RCL's trade, that in all probability all cooking liquors taken into stock by RCL are in fact eventually used in the manufacture of foodstuffs giving rise to qualification for the exemption";

(7) and at [117]: "Mr Beal submitted that the fact that RCL has been unable to establish the end use of the excise goods (having not accounted for excise duty) was a reason for upholding the decision to refuse restoration. We do not understand how RCL could have established the end use of excise goods which had been seized by HMRC. As we have indicated above, we regard it as reasonably certain that if the cooking liquors had not been seized their end use would have been one which would have qualified them for exemption from excise duty pursuant to Article 27(1)(f) of the Excise Directive. This submission does not, therefore, establish a reasonable ground for the decision".

51. Bearing all this in mind, it is much more likely than not that the cooking liquors which were the subject of the larger assessment, i.e. the products which had been sold by RCL in and before 2002, have been used for a qualifying purpose. We make that finding of fact. This is not a conclusion that goods are exempt at source nor is it a conclusion the likely destiny of a given bottle of cooking wine is sufficient for the exemption; it is a conclusion that on the balance of probabilities all the products which were sold were in fact used for a qualifying purpose.

52. The evidence before the FTT did not go so far as to show the specific use made of any individual batch of liquors which had been sold. If the hearing had taken place shortly after 2002, the tribunal could justifiably have held against RCL the failure to offer evidence from its customers etc. Considered contemporaneously, an absence of such evidence would give a decision maker good grounds for rejecting a broad assertion that a particular batch of cooking liquors had been used in that way. But with a gap of many years between the hearing, and given that the fate of the goods covered by the assessment only became the subject of this appeal at all after 2012, there is no reason to draw an inference against RCL from the lack of such evidence. Moreover it is also relevant to take into account that at the relevant time in 2002, under UK law, RCL was not entitled to claim a refund and so had no reason to ask its customers to provide evidence of the specific use of any given batch of product.

53. However the cooking liquors which were held in RCL's warehouse are in a different position. It is plain that they had not been used at all. Mr Mercer thought that they were still there in a corner of the warehouse. Since they have not been used for a qualifying purpose, those goods cannot benefit from any exemption from duty.

54. Thus we find that (i) the cooking liquors which were the subject of the lesser assessment were not exempt but (ii) that the cooking liquors which were the subject of the larger assessment were shown to be exempt under Art 27.

55. It follows from these findings that RCL has not established any right to exemption in relation to the lesser assessment and so the part of the appeal against that assessment should be dismissed in any event.

56. In order to decide the appeal in relation to the larger assessment, we turn to consider whether section 4 gives effect to RCL's EU law right to exemption under the Directive. Our finding of fact means that RCL has established a directly effective right to exemption from duty.

Does section 4 of the Finance Act give effect to RCL's right to exemption?

57. In its form as enacted section 4 contains the Three Conditions which HMRC has not offered any evidence to support. Thus the effect of the decision of the CJEU in this case means that the UK cannot make the application of the exemption in Art 27 conditional on compliance with those Three Conditions. Nevertheless this still leaves open the question of how section 4 is to be approached given the inconsistency between it and European law. Handling inconsistencies between UK legislation and EU law is an important topic addressed in a number of cases. We will only mention the following.

58. In *Autologic* [2006] 1 AC 118 Lord Nicholls explained that the effect of section 2 European Communities Act 1972 was that where there was an inconsistency between a provision of UK legislation and directly applicable EU law the statutory provision was to be read and take effect as though it was without prejudice to directly enforceable community rights "Accordingly if an inconsistency with Community law exists, formal statutory requirements must where necessary be disapplied or moulded

to the extent needed to enable those requirement to be applied in a manner consistent with Community law."([17]).

59. In *Vodafone 2* [2009] EWCA Civ 446 The Chancellor, Sir Andrew Morritt, distinguished between the process of reaching a conforming construction of the provision and its disapplication ([26]). He summarised the principles applicable to a conforming construction, derived from a number of cases, in paragraphs 37-38. Such a construction had a broad and far reaching nature permitting departure from the strict literal meaning of the words and did not require legislative precision, but could not provide an interpretation which did not "go with the grain" of the legislation in the sense that it produced a result which was inconsistent with a fundamental feature of the legislation, or require a court to make an decision for which it was not able or equipped to evaluate.

60. The Chancellor said that it was inevitable that conforming construction would be retrospective in operation, but that was no more an objection to the process than it was in the case of domestic statutory construction ([56]).

61. Where conforming construction was not possible, the process of disapplication involves treating the relevant domestic provisions as if expressed to be without prejudice to the relevant person community rights. In *Fleming/Condé Nast* [2008] UKHL 2 *[49]* Lord Walker explained that disapplication "involves the identification of the class or classes of taxpayers who are so circumstanced that the offending provisions must not be invoked against them, either in particular cases or at all." In *Vodafone 2* the Court of Appeal rejected the disapplication of the whole of the CFC legislation and preferred an interpretation which provided a further exception for certain EU companies.

62. Mr Mercer referred to *Litster v Forth Dry Dock* [1990] 1 AC 546 as an example of a case in which the House of Lords, following *Pickstone v Freemans* [1989] AC 66, decided that words had to be implied into the relevant Regulations in order to give effect to what must be assumed to have been the intention of the legislature, to pass a Regulation which gave effect to a European Directive.

63. Mr Beal submits that the way to read s4 today is simply to treat as struck through paragraphs (a), (b) and (c) of s4(3) and (a) and (b) of s4(5). Those are the enactments which apply the Three Conditions and they must be set aside. His case is that the rest of the section can be read in an appropriate way with minor adjustments as necessary as if those paragraphs are absent. Read that way there is a regime which provides that duty has to be paid in every case (in fact that arises from the charging provisions in ALDA) and then a repayment of duty paid can be obtained on application with proof of use. Mr Beal informed us that within a few weeks a statutory instrument was due to be enacted which would amend s4 in an essentially similar way in order to give effect to the judgment of the CJEU, but he recognised that the fact this was going to happen is not relevant to the appeal.

64. Mr Mercer submits the right way to approach the UK legislation is simply to read it as implicitly subject to RCL's directly effective right to exemption while leaving all

the words of section 4 (and the charging provision) as enacted. This is a similar approach to the legislation as was taken in *Litster*. The implicit exception proposed cannot be one which refers to RCL, we will consider the submission on the footing that section 4 should be read as implicitly subject to the directly effective right of anyone who is entitled to an exemption but who does not satisfy the Three Conditions.

65. Mr Mercer supports his argument by reference to the well established EU law principle of Effectiveness and to *Metallgesellschaft* (Case C-397/98). This case concerned group income elections which when made permitted a UK company to pay dividends to its parent without accounting for ACT. The elimination of the requirement to pay ACT on such dividends provided a cash flow benefit to the paying company. Under the UK domestic legislation such an election could be made only if the recipient company was UK resident. An election had to be made by notice to an Inspector of Taxes, and if she rejected it there were standard rights of appeal.

66. In 1974 and later years Metallgesellschaft had paid dividends to its non resident parent and had not attempted to make a group income election. As a result it had suffered a cash flow disadvantage. In 1994 it brought proceedings against HMRC for the loss it had suffered on the grounds that the loss arose from the UK's failure to permit a group income election for a non resident which was indirect discrimination on the grounds of nationality contrary to the Treaty

67. The ECJ held that failing to permit a group income election when the parent was in another member state was contrary to Art 52 of the Treaty and that a restitutionary remedy should be available. The Court then considered whether the UK was entitled to answer such a claim on the grounds that, despite the terms of the national legislation, the company should have made an election, and if it had been refused should have appealed relying on the direct effect of Community Law.

68. This defence was later characterised by Lord Walker in *Fleming* as the UK relying on its own wrong. The ECJ regarded the UK as blaming the companies for their lack of diligence in not contesting the national provisions – as if criticising them for not complying with the national legislation. It responded that this breached the principle of Effectiveness:

> "106. The exercise of rights conferred on private persons by directly applicable provisions of Community law would, however, be rendered impossible or excessively difficult if their claims for restitution or compensation based on Community law were rejected or reduced solely because the persons concerned had not applied for a tax advantage which national law denied them, with a view to challenging the refusal of the tax authorities by means of the legal remedies provided for that purpose, invoking the primacy and direct effect of Community law.
>
> "107. The answer …. must therefore be that it is contrary to Community law for a national court to refuse or reduce a claim [in the situation of M] on the sole ground that they did not [attempt to make a group income election] and that they therefore did not make use of the legal remedies available to them to

challenge the refusals of the tax authorities, by invoking the primacy and direct effect of the provisions of Community law…

69. We are not in the position of a court hearing a restitutionary claim. Our function is to determine the assessments. But we take from *Metallgesellschaft* the principle that it can be a breach of the principle of Effectiveness to treat, as a reason for withholding the benefit of an EU law right to which a party was entitled, a failure by that party to apply to the State for a remedy which, at the time, was prohibited by the relevant legislation.

70. On the other hand in *Autologic* Lord Nicholls, with whom the majority agreed, said (at [30]) that to require a claimant to make a group relief election which, as the law stood, would inevitably be refused and which would require statutory adaptation on appeal to accommodate the claim, did not render the statutory route practically impossible or excessively difficult. As a result he did not view the Effectiveness principle as requiring that the claim could not be brought through the normal statutory appeal mechanism rather than as a separate action. Lord Nicholls distinguished between the position of a claimant against whom the defence had been raised that it had not pursued the statutory channels and a claimant who had open to it the possibility of pursuing that course and wished to pursue another.

71. Mr Mercer submits that here the effect of HMRC's arguments is to say that RCL's claim is blocked, not because it did not pursue an appeal against the Review, which it did after all, but because it pursued an appeal in relation to payment rather than repayment at a time when repayment was barred by UK law. That is why the scheme of the UK legislation gave rise to excessive difficulty in establishing RCL's EU law right.

72. A particular problem with the workability of the section as proposed by HMRC is that it still contains s4(4) which refers to the application for a repayment taking such form as the Commissioners may direct. The only form in existence at the relevant time was one which clearly applied only to a manufacturer and therefore did not apply to RCL. Mr Beal points out that the section also refers to HMRC having the power to direct an appropriate form in a particular case. That is so but it does not help since at the time HMRC were seeking to apply the Three Conditions as they stood.

73. Mr Beal says that the appeal brought by RCL was in effect a challenge to the implementation of Art 27 and that the result of that appeal was that any EU law right was given effect by treating the Three Conditions as deleted. He argues that *Metallgesellschaft* does not assist RCL and contends that the FTT assumed, rightly, that the offending parts of the domestic law were to be disapplied, and then properly required the Appellant to comply with that portion of the domestic law which had not been case into doubt by the CJEU's preliminary ruling. But that "assumption" seems to us to be the stumbling block. The UK's legislation and administrative practice indicated in clear terms that this course was not available: making the assumption avoids confronting the difficulty which existed.

74. A Member State which makes it practically impossible or excessively difficult to exercise a community law right does not give effect to that right. The effect of Art 27

is to give the taxpayer a right to exemption. A refund procedure which would deprive the taxpayer of the ability of exercising the right to exemption without making a challenge to the domestic legislation and domestic practice in circumstances where the correct path is uncertain because of the way the State implemented the Directive, is a procedure which makes it excessively difficult to exercise the right.

75. In our judgment reading section 4 in the manner proposed by HMRC does not give effect to the EU law rights of parties such as RCL. Deleting this sort of limitation from this sort of provision has the effect of widening its scope after the event. The Manufacturer's Condition excluded from the UK refund scheme an entire class of persons. Those excluded persons (such as RCL) were still obliged by the legislation as a whole to pay the duty. It is the disapplication of that exclusion which creates the *Metallgesellschaft* problem. Conversely, reading in to section 4 an implicit exception for persons who do not satisfy that Condition gives full effect to the principle of Effectiveness.

76. A further reason why we prefer to read in an implicit exception into the legislation is that to take that approach "goes with the grain" of the legislation much more than simply disapplying whole parts of provisions enacted by Parliament. The repayment regime is a workable regime for anyone who satisfies the Three Conditions. For a manufacturer who makes the claim within the appropriate time and for an appropriate sum of money, the scheme works and gives effect to Art 27. At most one might need to disapply the second and third conditions, leaving a scheme for refunds for manufacturers, which is what Parliament unquestionably intended. In a case in which the State had a choice how to give effect to the exemption right under Art 27, it risks usurping the function of Parliament for the court to assume that it intended to give refunds to anyone else.

77. Finally, we note that the section 4 scheme as enacted gives effect to the exemption where a manufacturer imports and claims a repayment. Section 4 speaks of the duty paid on the goods, not the duty paid by the claimant. Thus if duty is paid by the importer who sells the goods to a manufacturer it seems to be the manufacturer who can make the repayment claim. Considerations of this kind were discussed by the Advocate General at paragraphs 102-108. If the manufacturer is to claim the repayment, the scheme would not want to provide that the importer could claim a refund as well. For this reason the intention of the UK scheme (even if not comprehensively implemented) may well be to exclude the non-manufacturing importer from obtaining repayment, and give effect to the exemption by permitting the refund to be made by only one person, the user (who would be better able to certify use in any event). This is another way of addressing the previous point. If Parliament never intended a repayment scheme to be available to a wider class of persons and if the court can find a way to apply section 4 in a manner consistent with EU law which does not make the repayment scheme available to a wider class, then that is the right way to go.

Error of law by the FTT

78. The FTT made its decision by considering whether "the UK could properly require the payment of excise duty on the cooking liquors in issue pursuant to section 4, FA 1995". Section 4 merely confers exemption, but the FTT's use of that phrase was clearly merely shorthand for "the payment and refund regime which includes section 4".

79. The FTT concluded that a "Member State may give effect to the exemption … by means of a refund of excise duty paid, depending on how the products in question are used" and that "[n]o 'reading down' of the guidance given by the Court of Justice into section 4, FA 1995, or invocation of the direct effect of Article 27(1)(f) of the Excise Directive can avail RCL on this point. The establishment in the UK of a system of exemption with refund of excise duty paid is, in our judgment, immune to either of these attacks.".

80. In other words it concluded that the refund scheme adopted by the UK (modified to take into consideration the CJEU's doubts) gave effect to RCL's rights under the Directive, and as a result it had an obligation to pay the duty (with a right of refund on proof of use).

81. For the reasons set out above, we have concluded that the UK did not give effect to RCL's rights. As a result we conclude that the FTT were wrong in concluding that RCL's rights arose under the UK's refund scheme. We have therefore set aside the decision and shall remake it.

82. We have found as a fact that RCL is entitled to exemption from duty in relation to the larger assessment. Since the legislation has to be read as implicitly subject to the EU law right of a person entitled to exemption from duty who is not within the Three Conditions, RCL does not owe any duty for that consignment of cooking liquor. Accordingly we will allow the appeal on the larger assessment.

MR JUSTICE BIRSS

CHARLES HELLIER

(Signed on original)

UPPER TRIBUNAL JUDGES
RELEASE DATE: 26 FEBRUARY 2016