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Upper Tribunal (Tax and Chancery Chamber)

Hearing venue: Rolls Building
Fetter Lane
London
EC4A 1NL

Heard on: 3 and 4 December 2024
Judgment date: 14 January 2025

VAT – Tour Operators' Margin Scheme – apartments leased to taxpayer and used to provide short term accommodation to travellers – whether supplies of a designated travel service – whether any requirement that the bought-in supply be used for the direct benefit of travellers

Before

MR JUSTICE TROWER
JUDGE JONATHAN CANNAN

Between

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Appellants

and

SONDER EUROPE LIMITED

Respondent

Representation:

For the Appellants: Andrew Macnab, Counsel instructed by the General Counsel and Solicitor for His Majesty's Revenue and Customs

For the Respondent: Jonathan Bremner KC, Counsel instructed by KPMG LLP

DECISION

Introduction

1. This is an appeal by the Commissioners for His Majesty's Revenue and Customs ("HMRC") against a decision of the First-tier Tribunal Tax Chamber ("the FTT") released on 5 July 2023 ("the Decision"). The FTT held that supplies of accommodation made by the Respondent ("Sonder") fell within the scope of the Tour Operators' Margin Scheme ("the TOMS") for the purposes of Value Added Tax ("VAT").

2. We are concerned with supplies made by Sonder in VAT periods 10/17, 01/18 and 04/18. The supplies in question were supplies of accommodation in the UK to corporate and leisure travellers. Sonder leased self-contained apartments from third party landlords for periods between two and ten years. It then granted licenses to travellers to occupy the apartments for periods ranging from a single night up to a month. During the relevant VAT periods the average stay in an apartment by a traveller was five nights.

3. Sonder accounted for VAT pursuant to the TOMS on its margin, that is the difference between the total amount, exclusive of VAT, payable by the traveller and the cost to Sonder payable to the third party landlords. HMRC contended that Sonder's supplies did not fall within the TOMS and Sonder ought to have accounted for VAT at the standard rate on the value of supplies to travellers. HMRC assessed Sonder to VAT in the sum of £252,229 for the relevant VAT periods.

4. The FTT held that the TOMS did apply to Sonder's supplies of accommodation and allowed its appeal.

Legislative Framework

5. It is convenient to start by setting out the EU provisions which establish a special scheme for travel agents and tour operators. Save where the context otherwise requires, we shall refer to such businesses as "travel agents". The provisions are contained in Articles 306 to 310 Council Directive 2006/112/EC (the Principal VAT Directive or "PVD"). The EU provisions were implemented by section 53 Value Added Tax Act 1994 ("VATA 1994") and the Value Added Tax (Tour Operators) Order 1987 ("the TOMS Order"). It is common ground that the TOMS Order must be construed consistently with the PVD, although how the TOMS Order is to be construed is very much in issue. It is also common ground that following the UK's exit from the EU, EU law continues to apply to all the periods under appeal because they pre-date the implementation period completion day.

EU Law

6. Article 26 of Council Directive 77/388/EEC ("the Sixth VAT Directive") introduced the EU special scheme for travel agents. The Sixth VAT Directive was repealed and replaced by the PVD, which re-enacted Article 26 in Articles 306 to 310. The material provisions for the purposes of this appeal are as follows:

> Article 306
>
> 1. Member States shall apply a special VAT scheme, in accordance with this Chapter, to transactions carried out by travel agents who deal with customers in their own name and use supplies of goods or services provided by other taxable persons, in the provision of travel facilities. This special scheme shall not apply to travel agents where they act solely as intermediaries and to whom point (c) of the first paragraph of Article 79 applies for the purposes of calculating the taxable amount.

2. For the purposes of this Chapter, tour operators shall be regarded as travel agents.

Article 307

Transactions made, in accordance with the conditions laid down in Article 306, by the travel agent in respect of a journey shall be regarded as a single service supplied by the travel agent to the traveller.

The single service shall be taxable in the Member State in which the travel agent has established his business or has a fixed establishment from which the travel agent has carried out the supply of services.

Article 308

The taxable amount and the price exclusive of VAT, within the meaning of point (8) of Article 226, in respect of the single service provided by the travel agent shall be the travel agent's margin, that is to say, the difference between the total amount, exclusive of VAT, to be paid by the traveller and the actual cost to the travel agent of supplies of goods or services provided by other taxable persons, where those transactions are for the direct benefit of the traveller.
…

Article 310

VAT charged to the travel agent by other taxable persons in respect of transactions which are referred to in Article 307 and which are for the direct benefit of the traveller shall not be deductible or refundable in any Member State.

7. The FTT summarised the EU special scheme at [8] as follows:

8. It follows from the PVD that the EU special scheme applies to:

(1) transactions carried out by travel agents or tour operators;

(2) dealing with customers in their own name;

(3) using supplies of goods or services provided by other taxable persons;

(4) in the provision of travel facilities; and

(5) where those supplies are for the direct benefit of the traveller.

8. The FTT further noted at [9] that the EU special scheme does not apply to travel agents where they act solely as intermediaries and are merely reimbursed expenditure incurred in the name of and on behalf of a customer.

9. The question of whether the TOMS is only engaged where the supplies received by Sonder had to be supplied for "*the direct benefit of the traveller*" and if so whether they were so supplied lies at the heart of this appeal.

UK Legislation

10. Section 53(1) VATA 1994 provided at the material times:

53 Tour operators

(1) The Treasury may by order modify the application of this Act in relation to supplies of goods or services by tour operators or in relation to such of those supplies as may be determined by or under the order.

(2) …

(3) In this section 'tour operator' includes a travel agent acting as principal and any other person providing for the benefit of travellers services of any kind commonly provided by tour operators or travel agents.

11. The TOMS Order was introduced with effect from 1 April 1988. Articles 2 and 3 define the supplies which fall within the scope of the TOMS:

2 Supplies to which this Order applies

This Order shall apply to any supply of goods or services by a tour operator where the supply is for the benefit of travellers.

3 Meaning of 'designated travel service'

(1) Subject to paragraphs (2) and (4) of this article, a 'designated travel service' is a supply of goods or services –

(a) acquired for the purposes of his business; and
(b) supplied for the benefit of a traveller without material alteration or further processing;

by a tour operator in a member State of the European Union in which he has established his business or has a fixed establishment.

(2) The supply of one or more designated travel services, as part of a single transaction, shall be treated as a single supply of services.

(3) …

(4) The supply of goods and services of such description as the Commissioners of Customs and Excise may specify shall be deemed not to be designated travel services.

12. For present purposes, we are concerned with the question of whether the supplies received by Sonder from third party landlords were supplied onwards for the benefit of travellers "*without material alteration or further processing*" within the meaning of Article 3(1)(b).

13. Article 7 of the TOMS Order makes provision for the VAT on a supply falling within it to be taxed by reference to the margin:

Subject to articles 8, 9 and 9A of this Order, the value of a designated travel service shall be determined by reference to the difference between sums paid or payable to and sums paid or payable by the tour operator in respect of that service, calculated in such manner as the Commissioners of Customs and Excise shall specify.

14. It is also important to note that the supply of an interest in land is an exempt supply by virtue of Schedule 9 Group 1 Item 1 VATA 1994, although a supply of hotel accommodation or similar is excluded from exemption and is therefore a standard rated supply:

Item 1 The grant of any interest in or right over land or of any licence to occupy land, or, in relation to land in Scotland, any personal right to call for or be granted any such interest or right, other than –
…

(d) the provision in an hotel, inn, boarding house or similar establishment of sleeping accommodation or of accommodation in rooms which are provided in conjunction with sleeping accommodation or for the purpose of a supply of catering;
(e) the grant of any interest in, right over or licence to occupy holiday accommodation;

The FTT's findings of fact

15. There was no real issue as to the primary facts before the FTT. It made findings of fact at [26] – [42] of the Decision and we summarise the FTT's findings in the following paragraphs.

16. Sonder commenced its UK operations in 2017. During the relevant VAT periods it rented 40 individual apartments from third party landlords. The leases required Sonder to use the apartments only as serviced apartments for residential occupation. The evidence before the FTT was that leases between Sonder and the landlords were for terms between two and ten years. The landlords were not hoteliers and the case was argued on the basis that the supply bought in by Sonder was not the grant of any interest in, right over or licence to occupy holiday accommodation.

17. Approximately 37.5% of the apartments which Sonder rented were furnished and described as "ready to go". The remaining 62.5% were unfurnished and could not be used in Sonder's business until Sonder had furnished them to its specification. Furnishings provided by Sonder included beds, sofas, armchairs, coffee and side tables, chairs, bookcases and lamps as well as smaller decorative items such as rugs, vases and wall art and basic kitchen utensils. White goods were always provided by the landlords.

18. The FTT found at [30] and [31]:

> 30. Anything Sonder did to the apartments, whether furnished or unfurnished, was only ever purely superficial and cosmetic in nature. Sonder never made any changes which would have altered the fabric or structure of the apartment or building, such as moving a wall or door or changing windows. The agreements with the landlords typically prohibited Sonder from making any alterations or additions to the property…
>
> 31. In a small number of cases, in respect of unfurnished accommodation, Sonder arranged for an accent wall to be painted or for other minor decorating to be done. However, this was not typical and it was more common for any work of that nature to be undertaken by the landlord prior to Sonder entering into the agreement with the landlord.

19. The agreements between Sonder and the landlords were 'internal repairing insuring' leases. Sonder was responsible for keeping the apartments and any furnishings provided by the landlord as they were when the lease was entered into. If any damage was caused to an apartment such as a broken TV or a scratch on the wall, it would be Sonder's responsibility to replace the TV and repair the damage to the wall. The apartments had to be delivered up in their original condition at the end of the lease. Any walls that had been painted had to be repainted and items added had to be removed.

20. Between October 2017 and May 2018 Sonder paid rent to landlords of approximately £1.5m. In the same period it spent approximately £20,000 on maintenance and repairs. There was no finding on how much Sonder spent on furnishing the unfurnished apartments.

21. Sonder used the apartments to provide accommodation to business and leisure travellers, described generally as "holiday accommodation". A traveller would book online with Sonder and receive an access code to access the apartment. The traveller could not book directly with the landlord. Sonder had no staff on site, but would use a third party housekeeping company to provide cleaning and housekeeping services. Apartments were not normally cleaned during a stay, unless requested and paid for by the traveller.

22. Apartments were self-contained with the normal furnishings and features of an apartment. Apartments had kitchens with cooking utensils. Food and beverages were not provided apart from tea and coffee in some rooms.

23. Sonder had a "Hospitality Team" to support guests who had any questions, or who required additional items such as fresh towels or toiletries. Some apartments would have a self-service consumables cabinet. Otherwise, such items would be delivered by Sonder staff.

24. At the end of a stay, there was no check-out procedure as such. The traveller would simply leave the apartment.

The FTT's Decision

25. The FTT referred to various authorities in the European Court of Justice and the Court of Justice of the European Union (both referred to as "the CJEU") as to the scope of the special scheme for travel agents in the PVD. We consider these authorities in due course. The FTT then went on to consider the submissions of the parties and discussed its findings in relation to the issues at [61] – [80].

26. The FTT did not accept HMRC's submission that to fall within the TOMS Order, a trader had to purchase holiday or hotel accommodation which it then used to make onward supplies of such accommodation to travellers. It held there was no such requirement in the PVD or the TOMS Order. Nor was there any requirement that the bought-in supplies, as they are described in some of the authorities, must be identical to the supplies made to travellers. The TOMS Order simply requires that a travel agent acquires the right to use an apartment for the purposes of its business and supplies it for the benefit of a traveller without material alteration or further processing. These findings appear at [61] to [65] of the Decision:

> 61. In essence, HMRC's case was that, to come within TOMS, a trader must have bought in holiday or hotel accommodation which the trader then uses to make onward supplies of such accommodation to travellers. Sonder leased the apartments from the landlords for a term of years with no stipulation that they must be used for the provision of accommodation for travellers. Sonder used the leased apartments to make supplies of short term accommodation to travellers. Mr Macnab's submission was that those supplies did not fall within the TOMS because they were supplies made from Sonder's own resources.
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> 62. I do not accept Mr Macnab's submission that in order for a supply of holiday accommodation to fall within the TOMS, the tour operator must have bought in holiday accommodation. I do not find that requirement in the EU special scheme as set out in the PVD or in the TOMS Order. Nor, in my view, can it be inferred. Article 306 of the PVD simply refers to "supplies of goods or services provided by other taxable persons [which are used] in the provision of travel facilities". The TOMS Order states that goods or services acquired for the purposes of the tour operator's business and provided for the benefit of a traveller without material alteration or further processing are within the scope of the TOMS. In neither case is there any further requirement that the bought-in supplies must be identical to the supplies provided by the tour operator to the traveller.
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> 63. Although it may be that the bungalows in *Van Ginkel* were holiday accommodation or second homes rather than ordinary residential property used for holidays, that fact is not mentioned in the judgment. The ECJ referred to "holiday accommodation" in [24] and [27] but that only referred to what was provided by the travel agent and not by the landlords. In *Alpenchalets*, the Advocate General referred to the properties as "houses" and the CJEU used the term "residences". The only mention of "holiday accommodation" and "holiday rentals" again referred to the supplies made by Alpenchalets Resorts GmbH and not the supplies by the owners. I conclude that whether the bought-in accommodation was

or was not "holiday accommodation" was not a factor in the ECJ's reasoning in *Van Ginkel* and *Alpenchalets*.

64. In my view, the nature or characteristics for VAT purposes of the goods and services supplied by third parties to the tour operators do not determine whether onward supplies fall within the TOMS. The purpose to which the apartments had been put by the landlords was irrelevant to the VAT treatment of the onward supply of those apartments by Sonder.

65. In order to be a designated travel service and come within the TOMS, the TOMS Order only requires that the right to use the apartments was acquired by a tour operator for the purposes of its business before being supplied for the benefit of a traveller without material alteration or further processing.

27. The FTT found that Sonder was a tour operator or travel agent for the purposes of the TOMS Order. It provided accommodation to travellers in self-contained apartments which is a type of service commonly provided by tour operators or travel agents. These findings appear at [66] and [67] of the Decision:

66. The first question is whether Sonder was a tour operator for the purposes of the TOMS. It is clear from *Madgett and Baldwin* and *ISt* that the terms 'travel agent' and 'tour operator' are to be interpreted broadly. Any business that provides services which are the same as or comparable to those provided by travel agents or tour operators within the normal meaning of those terms is itself a travel agent or tour operator for the purposes of the EU special scheme. That is reflected in section 53(3) VATA.

67. The apartments were used by Sonder as serviced apartments for the residential occupation of travellers. There was no suggestion that the apartments were used as permanent or long term accommodation and, during the relevant period, the average length of stay was only five nights. Sonder used the apartments to provide temporary accommodation for persons who did not reside in them as their homes. I conclude that such persons were travellers and the apartments were, therefore, travel facilities (in the terms of Article 306 PVD) and for the benefit of travellers (as required by section 53(3) VATA). I also find that the provision of accommodation in self-contained apartments is the type of service that was commonly provided by tour operators or travel agents. Indeed, I did not understand Mr Macnab to contend otherwise. I conclude that Sonder was a tour operator for the purposes of the TOMS during the relevant period.

28. When the FTT came to consider the test to be applied to Sonder's services it did so firstly by reference to Sonder's supplies generally, and then in relation to Sonder's supplies of unfurnished accommodation where Sonder furnished the apartments before making the onward supply to travellers. In relation to the supplies generally, the FTT held at [72] – [76] that there was no material alteration or further processing of the third party supplies. In relation to the specific supplies of unfurnished apartments, it also held at [77] that there was no material alteration or further processing.

29. The FTT held that the fact Sonder received an exempt supply of land and made a standard rated supply of holiday accommodation did not mean that it had not made an onward supply of an apartment for the purposes of the TOMS Order. Further, a change from leasing the apartments as accommodation for a term of years to supplying them as holiday accommodation did not amount to a material alteration or further processing for the purposes of the TOMS Order:

72. I have already concluded in [62] to [65] that the fact that the terms on which the landlords let the apartments to Sonder and Sonder let them to the travellers and that the VAT treatment of their respective supplies were different did not mean that Sonder had not made onward supplies of the apartments for the purposes of the TOMS. For similar reasons, I consider that a change from letting the

apartments for a term of years as accommodation, to letting them as, as Sonder did, for holiday accommodation did not amount to material alteration or further processing.

73. In my view, the object of the alteration or processing must be the thing supplied, ie the apartment, not the characterisation of the supply for VAT purposes. In *ISt*, the German government submitted that the EU special scheme should not apply to exempt services of language training and education which formed part of the programmes offered. The CJEU rejected this argument in [39] as follows:

> 'There is nothing to suggest that the application of [the EU special scheme] is dependent on such a condition. It should be noted that in respect of operations involving bought-in supplies and services for which traders should be taxed under that article, the only relevant criterion is whether or not the travel service is ancillary.'

74. The CJEU's response in *ISt* shows that the EU special scheme still applies even where an exempt supply to a tour operator changes to a supply chargeable to VAT, albeit on the margin, when supplied by the tour operator as part of travel facilities. It follows that the correct question in this case is whether the apartments themselves, and not the tax status of their supplies, were materially altered or further processed before they were supplied by Sonder to the travellers.

30. The FTT considered that the term "*material alteration or further processing*" refers to more than minor changes or processes which do not affect the fundamental character of the particular goods or services. The alteration and processing must change the goods or services so that what is supplied cannot be described in the same terms as the items acquired. Any changes to the apartments, including furnishing the unfurnished apartments, were "cosmetic or decorative" and could easily be reversed. They could not be described as material and did not amount to processing of the apartment:

76. It seems to me to be clear from the nature of the TOMS that "material alteration or further processing" must refer to more than minor changes or processes which do not affect the fundamental character of the particular goods or services. It would be absurd as well as impracticable if any minor change or processing excluded a bought-in supply from the TOMS. In order to be excluded from the TOMS, I consider that the alteration and processing must change the goods or services supplied so that what is supplied by the tour operator cannot be described in the same terms as the items acquired.

77. I do not consider that it matters whether the apartments were furnished or unfurnished when they were acquired by Sonder. In both cases, Sonder supplied the apartments to the travellers without changing their structure. The evidence shows that any changes that Sonder made to the apartments were cosmetic or decorative, such as painting a wall or providing furnishings and decorative items. In the case of the unfurnished apartments, Sonder additionally acquired the furnishings which were needed to enable it to provide the apartment to the travellers. The nature of the changes that were made were such as they could be reversed simply by removing the items of furniture or re-painting a wall. In my view, such changes cannot be described as material and do not amount to processing of the apartment.

31. The FTT noted that the PVD does not refer to altering or processing the goods or services being supplied. However, given the FTT's conclusion at [76] and [77] it decided at [78] that it was not necessary to consider whether the exclusion of supplies where the goods or services had been materially altered or further processed was consistent with the PVD:

78. The UK notion of alteration and further processing does not appear in Directive. Nowhere in ECJ case law does it say that bought-in supplies that are altered or subject to processing must be excluded from the EU special scheme. As I have concluded that furnishing an apartment did not constitute a material alteration to that apartment or further processing of it, I do not need to consider whether the exclusion from the TOMS of goods or services which have been materially altered or processed by the tour operator is consistent with the EU special scheme in the PVD.

32. In conclusion, the FTT held that Sonder's supplies were designated travel services within the TOMS Order.

The grounds of appeal

33. HMRC has three grounds of appeal, for which the FTT granted permission to appeal. The grounds of appeal may be summarised as follows:

> (1) The FTT erred in law at [62] – [65] and [72] – [76] in finding that Sonder's supplies to customers were designated travel services. The FTT should have held that Sonder's supply to its customers were not supplied "*without material alteration or further processing*" and/or that the supplies were not "*for the direct benefit*" of its customers.
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> (2) Further or alternatively, the FTT erred in law in finding at [76] and [77] that Sonder's supplies of unfurnished apartments were designated travel services.
>
> (3) Further or alternatively, the FTT erred in law in failing to take into account that Sonder carried out significant and meaningful steps to perform obligations to its customers which amounted to a material alteration to the supply. Namely, paying utilities and council tax, and undertaking responsibility for the upkeep of the apartments.

34. At this stage we note that it was Sonder's uncontradicted position in its written argument that it was common ground that it was a tour operator within section 53(3) VATA 1994 because Sonder provided the benefit of serviced accommodation which was of a kind commonly provided by tour operators. Having said that, we note for completeness that when this decision was circulated to the parties for clerical errors and corrections, HMRC stated that this was not in fact common ground. Their position was that Sonder could be a tour operator if it bought in supplies of travel accommodation for the direct benefit of its traveller customers which it resold in its own name to its customers. Whilst Sonder objected to this paragraph being amended, nothing appears to turn on HMRC's apparent change of position for the purposes of our Decision. It is also common ground that Sonder acquired the leases from landlords for the purposes of its business, so Article 3(1)(a) of the TOMS Order is satisfied.

35. There is no dispute that the landlords were taxable persons. This is not a requirement in the TOMS Order but it is a requirement of Article 306 PVD. A taxable person for the purposes of the PVD is simply a person who carries out any economic activity (see Article 9 PVD). There is no requirement for the purposes of the PVD that a taxable person should be making taxable supplies or be registered for VAT.

36. The overarching issue is whether Sonder satisfied Article 3(1)(b) of the TOMS Order which provides that supplies will only be "designated travel services" where they are supplied "for the benefit of a traveller without material alteration or further processing".

37. We shall consider the grounds of appeal in the same order. We are grateful to both parties for their clear and succinct written and oral submissions.

Ground 1

38. Mr Macnab for HMRC says that the FTT erred in law in finding that Sonder's supplies were designated travel services falling within the TOMS Order. A designated travel service for the purposes of the TOMS Order is a supply acquired by a travel agent for the purposes of its business which is supplied onward for the benefit of a traveller without material alteration or further processing. HMRC say that the TOMS Order is not engaged because the bought-in supply of an interest in land from the landlords was not a transaction for the "direct benefit of the traveller" and therefore was not a

designated travel service. It was an exempt supply of land and not a taxable supply of holiday accommodation.

39. In making that submission, HMRC accepted that in determining whether Sonder's supplies were designated travel services within the meaning of Article 3(1) of the TOMS Order, the FTT was required to construe the TOMS Order itself, and that there is no reference in the TOMS Order to any requirement that the bought-in supply should be for the "direct benefit of the traveller". That term does however appear in Articles 308 and 310 of the PVD and Mr Macnab submitted that a supply "for the benefit of a traveller without material alteration or further processing" was simply another way of describing a supply for the "direct benefit of the traveller".

40. Mr Bremner KC on behalf of Sonder submitted that there is no requirement in the TOMS Order that the supply be for the direct benefit of the traveller. The only requirement is that there is no material alteration or further processing of the supply acquired from the landlord. He submitted that Sonder acquired a right to occupy the apartments for the purposes of its business and supplied a right to occupy the apartments for the benefit of travellers. There was no material alteration or further processing and the supply was therefore a designated travel service within the TOMS Order. The FTT applied the correct test and made an evaluative judgment that there was no material alteration or further processing. We should not interfere with the FTT's evaluative judgment. Sonder secured the right to use the apartments and supplied the right to use the apartments. He submitted that HMRC were confusing the legal mechanism by which the rights were acquired and supplied, namely a lease and a short licence, with what was obtained and supplied, namely a right to use.

41. Mr Bremner further submitted that neither the PVD nor the TOMS Order requires the travel agent to acquire a supply of holiday accommodation which is then supplied to customers. The only question is whether Sonder is using supplies made to it in the provision of travel facilities. HMRC are seeking to re-write the statutory test to include such a requirement.

42. It is common ground that the TOMS Order was intended to implement what are now Articles 306 – 310 PVD. It is also common ground that we must construe the TOMS Order in so far as possible to conform with the requirements of the PVD. It is therefore helpful to consider the objectives of the special scheme set out in the PVD. Those objectives were conveniently described in a Commission Staff Working Document published by the European Commission on 17 February 2021.

43. The Sixth VAT Directive in 1977 introduced a special scheme for travel agents and tour operators due to the special nature of that industry. The services offered by such businesses usually consist of a package of services, in particular transport and accommodation acquired from third parties. Those third parties will often be based in different EU member states. The packages are then sold by travel agents or tour operators, acting in their own name, by way of a single supply to their customers. The complexity and location of the services acquired mean that it would be administratively difficult to apply the normal VAT rules on place of supply, taxable amount and deduction of input tax.

44. The special scheme was therefore intended to pursue two main objectives:

> (1) To simplify the normal VAT rules that would otherwise apply so that travel agents do not have to register for VAT in each member state where services are acquired, and
>
> (2) To ensure that VAT revenue goes to the member state in which final consumption of each individual component of the single supply takes place.

45. Case law of the CJEU has confirmed that the special scheme does not only apply where the services acquired comprise multiple services which are packaged together, or only where there is a cross-border element as between the services acquired and the services supplied by the travel agent.

Hence, in *Van Ginkel Waddinxveen BV and others v Inspecteur der Omzetbelasting, Utrecht* Case C163/91 [1996] STC 825 the CJEU held that the scheme applied to a travel agent providing only accommodation to customers which had been supplied by third parties. In *Customs and Excise Commissioners v Madgett and Baldwin* C-308/96 and C-94/9 [1998] STC 1189, the Court of Justice held that the scheme applied to a travel agent acquiring and supplying services within a single member state. We refer to both these authorities in more detail below.

46. It is also worth noting that the special scheme and the TOMS Order are intended in principle to be tax neutral. Hence, over the chain of supplies the VAT accounted for by the travel agent and third parties making supplies to the travel agent will be the same. Ultimately, the burden of VAT will fall upon the purchaser of the package (see Advocate General Sharpston in *European Commission v Spain* Case C-189/11 at [7] and [8]). Having said that, if the purchaser of the travel facilities is a VAT registered business, it will bear the burden of VAT on the travel agent's margin rather than the final consumer because the purchaser will not be entitled to reclaim input tax where the travel agent accounts for VAT pursuant to the TOMS Order.

47. Both parties sought to draw support for their submissions as to the correct test to be applied in construing Article 3(1)(b) TOMS Order from a number of authoritative decisions of the CJEU. In our judgment, those decisions do not support the case of either party. It appears that the issue raised in this appeal is a novel issue which has not previously been considered by the CJEU or in any domestic UK authority to which our attention has been drawn.

48. The first decision of the CJEU is *Van Ginkel*, referred to above. In that case the taxpayer offered 'motoring holidays' in the Netherlands to its customers. Customers used their own vehicles and the taxpayer supplied travel accommodation. Customers were accommodated in bungalows, most of which were owned by third parties.

49. The CJEU held at [27] that the fact that transport was not arranged for the traveller by the travel agent and that the traveller was merely provided with accommodation did not exclude the supplies from the special scheme, at that time contained in Article 26 Sixth VAT Directive:

> 27. … art 26 of the Sixth Directive must be interpreted as meaning that the fact that transport of the traveller is not arranged by a travel agent or a tour operator and that the latter merely provides the traveller with holiday accommodation is not such as to exclude the services provided by such undertakings from the field of application of art 26.

50. Mr Macnab says that it was implicit in the case that what was bought-in by the travel agent was holiday accommodation. It is said to be implicit because of how the Court described the supplies, for example at [3] where it is said that the taxpayer arranged "the travel accommodation" and at [9] where it is said that the taxpayer "lets holiday dwellings".

51. We consider that Mr Macnab is reading too much into such references. The judgment does not identify the nature of the bought-in supply and in our view it is authority only for the proposition at [27] of the Court's judgment.

52. Similarly, Mr Bremner submitted that the present case was indistinguishable on its facts from *Van Ginkel*. We do not consider that is the case, given that the judgment in *Van Ginkel* does not describe the nature of the supplies which the taxpayer bought-in.

53. The next decision of the CJEU is *Alpenchalets Resorts GmbH v Finanzamt München Abteilung Körperschaften* Case C-552/17. In that case, the taxpayer rented residences in Germany, Austria, and

Italy from their owners which it then let to individual customers as holiday rentals. The circumstances are described at [12]:

> 12. In the course of 2011, Alpenchalets rented residences in Germany, Austria, and Italy from their owners and let them, subsequently, in its own name, to individual customers as holiday rentals. In addition to accommodation, the services included the cleaning of the accommodation and, in some cases, a laundry and 'bread roll' service.

54. The CJEU identified the question at [19]:

> 19. By its first question, the referring court asks, in essence, whether Articles 306 to 310 of the VAT Directive must be interpreted as meaning that the mere supply by a travel agent of holiday accommodation rented from other taxable persons or such a supply of a holiday residence combined with the supply of additional ancillary services is covered by the special VAT scheme for travel agents.

55. The Court said as follows in answer to that question:

> 20. It must, first, be observed that, pursuant to Article 306 of the VAT Directive, that special scheme applies only where the travel agent uses for the organisation of the journey supplies of goods and services bought in from other taxable persons (see, to that effect, judgment of 25 October 2012, *Kozak*, C-557/11, EU:C:2012:672, paragraphs 18 and 21).
>
> 21 The request for a preliminary ruling does not include any information as to whether or not the owners or operators of properties, who have leased their residences to Alpenchalets, are subject to VAT.
>
> 22 Accordingly, the Court can only answer the first question on the assumption that those owners and operators of properties have the status of taxable persons for the purpose of VAT, which is a matter to be determined by the referring court.
>
> 23 As is apparent from the wording of Article 306 of the VAT Directive and the case-law of the Court, the special scheme for travel agents applies only where a travel agent uses goods or services supplied by third parties, in the provision of travel, which means that its own services, namely services which have not been bought in from third parties but supplied by the travel agent itself, are not covered by that scheme (see, to that effect, judgment of 25 October 2012, *Kozak*, C-557/11, EU:C:2012:672, paragraphs 18, 21, 23 and 27).
>
> …
>
> 25. As regards the application of that special scheme to the supply of a holiday residence bought in from third parties, it must be noted that, as pointed out by the referring court, the Court held, in paragraphs 23 and 24 of the judgment of 12 November 1992, *Van Ginkel* (C-163/91, EU:C:1992:435), that the mere supply of accommodation by a travel agent can be covered by the special scheme. In order to meet the needs of customers, travel agents offer widely different types of holidays and journeys, allowing the traveller to combine, as he wishes, transport, accommodation and any other services which those undertakings may provide. The exclusion from the field of application of Article 306 of the VAT Directive of services supplied by a travel agent on the sole ground that they cover accommodation only would lead to a complicated tax system in which the VAT rules applicable would depend upon the constituents of the services offered to each traveller. Such a tax system would fail to comply with the aims of the Directive.
>
> …
>
> 35. Having regard to the foregoing, the answer to the first question is that Articles 306 to 310 of the VAT Directive must be interpreted as meaning that the mere supply by a travel agent of holiday accommodation rented from other taxable persons or such a supply of a holiday residence combined

> with the supply of additional ancillary services, regardless of the importance of those ancillary services, each amount to a single service covered by the special scheme for travel agents.

56. We can see from these passages that the CJEU was assuming that the owners of the accommodation were taxable persons who were making taxable supplies. Mr Macnab says that it is clear that the travel agent must have bought-in holiday accommodation. That inference arises from references such as that at [25] to "the supply of a holiday residence bought in from third parties". Although we accept that the language is consistent with Mr Macnab's submission, we do not consider that we can safely draw that inference. In our view the case is simply authority for the proposition stated at [35]. When the CJEU referred to holiday accommodation being rented from other taxable persons we do not consider that it was describing a condition that what was being bought-in must be holiday accommodation. The existence of such a condition did not fall within the scope of the argument before the Court and was not clearly part of the question referred.

57. Similarly, Mr Bremner submitted that Sonder's case is indistinguishable on the facts from *Alpenchalets*. He submits that the following factors were irrelevant to the analysis of the CJEU: 1) the terms on which the taxpayers rented the accommodation; 2) the nature of the owners' businesses; 3) whether the customers could have obtained the accommodation directly from the owners; and 4) the VAT treatment of the supply from the owners to the taxpayers.

58. It is true that the matters identified by Mr Bremner did not form any part of the CJEU's analysis, but that is because the issue before the CJEU was limited to whether the PVD special scheme was applicable in circumstances where the travel agent made a single supply of travel accommodation which was not part of a package of supplies. That is not the same as the issue with which this appeal is concerned.

59. Mr Macnab also relied on the decision of the CJEU in *Madgett*, referred to above. In that case, a hotel in Devon sold packages to customers from the north of England covering half-board accommodation, transport by coach from various pick-up points and a day coach excursion during their stay. The transport services were obtained from third parties. The taxpayer argued that it was not within the TOMS Order on the ground that it was a hotelier and not a tour operator.

60. The CJEU held at [20] that the special scheme applied not only to travel agents and tour operators but also to traders effecting identical transactions, such as hoteliers. It also held at [47] that where the package supplied included transactions consisting partly of services supplied by the taxpayer and partly services supplied by other taxable persons, the special scheme applied solely to the services supplied by third parties.

61. Mr Macnab particularly relied on what was said by the Court at [23] and [34]:

> 23. It must therefore be held that the scheme under art 26 of the Sixth Directive applies to traders who organise travel or tour packages in their own name and entrust other taxable persons with the supply of the services generally associated with that kind of activity, even if they are not, formally speaking, travel agents or tour operators.
>
> …
>
> 34. Finally, it should be recalled that the scheme under art 26 constitutes an exception to the normal rules of the Sixth Directive and must be applied only to the extent necessary to achieve its objective.

62. Mr Macnab submitted that this was authority for a proposition that what is acquired from a third party supplier must be travel services and that the third party supplier must itself be in the business of supplying travel facilities. That was why the Court used the word "entrust" in [23]. He also relied

on what is said at [34], that the special scheme in the PVD should be applied "*only to the extent necessary to achieve its objective*".

63. We do not consider that *Madgett* is authority for Mr Macnab's proposition. In our view he is reading too much into the word "entrust". The questions before the CJEU did not involve consideration of the nature of the supply made by the third parties. The Court was not saying that the special scheme was only engaged when a third party was entrusted by a taxable person with making a supply to the traveller. We agree with Mr Bremner that the Court was not addressing the question of whether the special scheme only applied to services obtained from persons who themselves carry on business in the supply of travel services. It was simply describing the circumstances of that case where the taxpayer had entrusted the supply to a third party.

64. Mr Macnab also referred us to *Dyrektor Krajowej Informacji Skarbowej v C. sp. Zoo* Case C108/22 where the taxpayer was a "hotel services consolidator" which purchased and resold holiday accommodation without any other services. The question referred in that case was set out at [19]:

> 19. By its question, the referring court asks, in essence, whether Article 306 of the VAT Directive must be interpreted as meaning that the service provided by a taxable person, which consists in purchasing accommodation services from other taxable persons and reselling them to other economic operators, is covered by the special VAT scheme applicable to travel agents, even though those services are not accompanied by ancillary services.

65. The Court cited *Alpenchalets* at [28]:

> 28. Consequently, the Court has held that Articles 306 to 310 of the VAT Directive must be interpreted as meaning that the mere supply by a travel agent of holiday accommodation rented from other taxable persons or such a supply of a holiday residence combined with the supply of additional ancillary services, regardless of the importance of those ancillary services, each amount to a single service covered by the special scheme for travel agents (judgment of 19 December 2018, Alpenchalets Resort, C-552/17, EU:C:2018:1032, paragraph 35).

66. The Court answered the question at [30]:

> 30. In the light of the foregoing considerations, the answer to the question referred is that Article 306 of the VAT Directive must be interpreted as meaning that the service provided by a taxable person, which consists in purchasing accommodation services from other taxable persons and reselling them to other economic operators, is covered by the special VAT scheme applicable to travel agents, even though those services are not accompanied by ancillary services.

67. We do not consider that *C Sp zoo* takes HMRC's case any further. A hotel services consolidator is certainly within the special scheme, but it does not mean that the special scheme is limited to similar businesses. The Court was simply concerned with the particular facts of the case.

68. We therefore do not accept that any of the CJEU authorities establish the principle relied on by Mr Macnab to the effect that the special scheme only applies where a travel agent has bought-in travel facilities which are then supplied onwards to travellers. That is not to say that the principle is not correct. It is simply that the issue raised by HMRC is not the subject of previous authority.

69. It is common ground that the TOMS Order must be construed in so far as possible to conform with the requirements of the PVD. We are required to construe what is meant in the TOMS Order when it refers to a supply "for the benefit of a traveller without material alteration or further processing". We must do so consistently with the requirements of the PVD in so far as possible.

70. The thrust of Mr Macnab's submissions on Ground 1 was that the FTT did not take that approach because it failed to consider whether the exempt supply of land to Sonder by landlords was supplied onwards by Sonder for the direct benefit of the travellers. He submitted that this is a condition for the application of the TOMS Order, construed in conformity with the PVD, and that Sonder's supplies did not satisfy the condition because it acquired exempt supplies of an interest in land and then supplied taxable travel accommodation to travellers. Essentially, Sonder was not making onward supplies of bought-in services but was making supplies of what some of the authorities refer to as "in-house" services.

71. In the Decision, the FTT recognised that the PVD contained a requirement that the bought-in services must be for the direct benefit of the traveller, because it identified that requirement in its summary of the PVD at [8]. However, the FTT did not go on to consider whether the requirement in the PVD that a supply be for the direct benefit of the traveller affected how it should construe what amounted to a material alteration or further processing of the bought-in supply for the purposes of the TOMS Order. The question we must consider is whether the FTT correctly construed the TOMS Order in the light of the requirements of the PVD.

72. The FTT did raise the question of whether the TOMS Order was consistent with the PVD at [16] of the Decision:

> 16. It seems to me that section 53 VATA and the TOMS Order are consistent (or can be interpreted conformably) with Articles 306 to 310 PVD save possibly in one respect. That is the requirement in Article 3(1)(b) of the TOMS Order that goods or services acquired for the purposes of the tour operator's business must be supplied to the traveller without material alteration or further processing. Article 306 PVD merely requires that the supplies of goods or services provided by other taxable persons should be used to provide travel facilities. There is no further requirement that the goods of services should be used in their original state. If necessary then I must decide whether that condition in the TOMS can be interpreted conformably with Article 306 PVD.

73. Although the FTT recognised that the phrase "without material alteration or further processing" was not language used in the PVD (see [8]), it is notable that in this paragraph the FTT makes no reference to any requirement of the PVD that the supply must be for the direct benefit of the traveller. It states that the PVD merely requires that the third party supplies should be used to provide the travel facilities. Nor does the FTT make any reference to such a requirement in its discussion at [62] – [65] and [76] – [78].

74. Mr Bremner's first submission was that, despite the FTT's summary at [8], the special scheme in the PVD does not include any requirement that the services bought-in must be supplied "for the direct benefit of the traveller". He argued that the conditions for the special scheme are set out in Article 306 (as is apparent from the language of Article 307) and the only relevant question for present purposes is whether the bought-in supplies were used to make supplies to travellers. If there was a change to the supply that was bought-in then it would not fall within the scheme because it was not being used to make supplies to travellers. It would be the travel agent's own "in-house" supply.

75. Mr Bremner submitted that the only references in the PVD to services being for the direct benefit of the traveller are in Articles 308 and 310. Article 308 is simply concerned with computing the costs that are to be taken into account in calculating the margin on which VAT is payable. It is not setting out any further conditions. He said that the purpose of Article 308 in referring to costs for the direct benefit of the traveller is to exclude from the computation costs which are not sufficiently closely related to the supply, such as advertising costs or office costs. Article 310 is simply concerned with ensuring that there is no input tax deduction in respect of supplies falling within the special scheme. Neither Article imposes requirements or conditions for the application of the special scheme.

76. Mr Bremner also submitted that what the FTT said at [8] of the Decision was consistent with this analysis. The FTT was not setting out the conditions to be satisfied before the special scheme applied. It was simply including within its description of the special scheme how the margin is calculated. If the FTT was in this paragraph setting out conditions for the special scheme to apply, he accepted that it must follow on Sonder's case that the FTT erred in law in that respect.

77. We do not accept Mr Bremner's submissions. We acknowledge that the only references to a transaction being for the direct benefit of the traveller appear in Articles 308 and 310 of the PVD. It is also the case that Article 308 is dealing with the calculation of the margin where the scheme applies and Article 310 blocks the recovery of input tax on bought-in supplies. However, in identifying the circumstances in which the special scheme applies we consider that it is necessary to look at the structure of the special scheme as a whole, as it is set out in Articles 306 to 310.

78. Article 308 describes the margin as the difference between the total amount exclusive of VAT paid by the traveller and the actual cost to the travel agent of supplies provided by other taxable persons. Mr Bremner contends that the special scheme applies to supplies where the bought-in supplies are used to provide travel facilities. However, where those supplies are not for the direct benefit of the traveller then they are excluded when calculating the margin and can be the subject of an input tax deduction.

79. We cannot see any reason why the special scheme would create a separate category of supply which falls within the scheme but outside the scheme calculations. In the present case there is only one bought-in supply. On Mr Bremner's case, if that supply is not for the direct benefit of the traveller then the bought-in supply is not taken into account in computing the margin and there is no restriction on the input tax deduction. Presumably the taxpayer would end up accounting for VAT in the usual way as if the special scheme did not apply. In our view, Mr Bremner's construction of the PVD would add a layer of complexity which would not be necessary or consistent with the objectives of the special scheme.

80. Accordingly, for the reasons given above, we are satisfied that construing Articles 306 – 310 as a whole, for supplies to fall within the EU special scheme the supplies bought-in must be supplied for the direct benefit of travellers.

81. Mr Bremner then submitted that if, as we have found, the PVD contains a requirement that the bought-in supply must be supplied for the direct benefit of travellers, that requirement was not found in the TOMS Order. Further, the TOMS Order could not be construed so as to contain the requirement because that would be to re-write the domestic legislation. He said that the principle set out by the CJEU in *Marleasing SA v La Comercial Internacional de Alimentación SA* Case C-106/89 ("the Marleasing principle") could not be applied to give a conforming construction.

82. The Marleasing principle was set out at [8] of *Marleasing*:

> 8. … in applying national law, whether the provisions in question were adopted before or after the directive, the national court called upon to interpret it is required to do so, as far as possible, in the light of the wording and the purpose of the directive in order to achieve the result pursued by the latter and thereby comply with the third paragraph of Article 189 of the Treaty.

83. We had only brief submissions from the parties on the Marleasing principle. The principle was summarised by the Court of Appeal in *Vodafone 2 v HM Revenue and Customs* [2009] EWCA Civ 446 at [37] and [38] (omitting citations):

> 37. We were referred in the parties' respective written arguments and orally to a number of reported cases on the principles to be observed in looking for a conforming interpretation in either the European Community or Human Rights contexts … The principles which those cases established or illustrated

were helpfully summarised by counsel for HMRC in terms from which counsel for V2 did not dissent. Such principles are that:

> 'In summary, the obligation on the English courts to construe domestic legislation consistently with Community law obligations is both broad and far-reaching. In particular:
>
> (a) It is not constrained by conventional rules of construction …;
>
> (b) It does not require ambiguity in the legislative language …;
>
> (c) It is not an exercise in semantics or linguistics …;
>
> (d) It permits departure from the strict and literal application of the words which the legislature has elected to use …;
>
> (e) It permits the implication of words necessary to comply with Community law obligations …; and
>
> (f) The precise form of the words to be implied does not matter …'

38. Counsel for HMRC went on to point out, again without dissent from counsel for V2, that:

> 'The only constraints on the broad and far-reaching nature of the interpretative obligation are that:
>
> (a) The meaning should "go with the grain of the legislation" and be "compatible with the underlying thrust of the legislation being construed." … An interpretation should not be adopted which is inconsistent with a fundamental or cardinal feature of the legislation since this would cross the boundary between interpretation and amendment; … and
>
> (b) The exercise of the interpretative obligation cannot require the courts to make decisions for which they are not equipped or give rise to important practical repercussions which the court is not equipped to evaluate…'

84. In *Test Claimants in the FII Group Litigation v HMRC* [2012] UKSC 19, Lord Sumption described *Marleasing* as authority for a "highly muscular approach" to construing national legislation.

85. Mr Bremner noted the limitations to the Marleasing principle. We do not propose to embark on a detailed analysis of the authorities, especially when the parties themselves did not do so. We can simply say that we are satisfied that we must endeavour to construe the TOMS Order in a way which conforms with the requirement we have found in the PVD that for the special scheme to apply, the bought-in supply must be supplied for the direct benefit of travellers. In our judgment that is what the TOMS Order meant when it defined a designated travel service as a supply for the benefit of a traveller without material alteration or further processing.

86. HMRC submitted to the FTT that to fall within the scheme a travel agent supplying holiday accommodation must have bought-in holiday accommodation. The scheme did not apply in circumstances where Sonder had not bought-in holiday accommodation. The FTT rejected that submission at [61] – [65]. It held that there was no requirement for the supplies to be identical, although it does not appear that HMRC's submissions went that far. The FTT also held that the purpose to which the apartments had been put by the landlords was irrelevant to the VAT treatment of the onward supply by Sonder. It went on to consider at [70] – [76] HMRC's submission that a change from leasing the apartments for a term of years to letting them as holiday accommodation amounted to a material alteration or further processing. It applied the same reasoning as it had applied in [62] – [65] to find that there was no material alteration.

87. As we have said, it is notable that the FTT did not in these paragraphs seek to construe the TOMS Order in light of the direct benefit requirement found in the PVD. Indeed, it was only in relation to the apartments which were acquired unfurnished and then furnished by Sonder in order to make supplies of holiday accommodation that the FTT considered that any issue of conformity arose. However, at [78] the FTT concluded that it did not need to consider whether exclusion from the scheme of supplies which were materially altered or further processed was consistent with the PVD.

88. We turn now to consider what is meant in the context of the PVD by the requirement that a bought-in supply must be the subject of transactions which are for the direct benefit of the traveller. It seems clear to us that this requirement is reflected in the TOMS Order by the definition of designated travel services as a bought-in supply which is supplied for the benefit of a traveller without material alteration or further processing.

89. Mr Macnab suggested in his skeleton argument and appears to have argued before the FTT that as a matter of principle where a taxpayer acquires an exempt supply and then makes a taxable supply of travel facilities, the supplies cannot fall within the TOMS Order. That is because there must have been a material alteration in the supply merely by reason of the difference in VAT treatment. He also relied on an argument that on a proper construction of the TOMS Order, HMRC should collect VAT on the total consideration charged by Sonder to its customers. That is essentially an argument that where a trader acquires an exempt supply and then makes a taxable supply of travel facilities, the supplies could not fall within the TOMS Order.

90. In oral submissions, Mr Macnab accepted that HMRC's case could not be put that highly. He accepted that exempt supplies could conceivably be included in a package of travel facilities to which TOMS might apply. Whilst we accept that the TOMS is intended in principle to be tax neutral, we accept Mr Bremner's submission that in the context of special schemes, perfect VAT neutrality is not attainable.

91. The more limited submission on which Mr Macnab relied in oral argument was that on the facts of this case there had been a material alteration or further processing in the service supplied because Sonder had acquired interests in land for terms of several years and had supplied short term holiday accommodation to travellers. The supplies could not have been for the direct benefit of travellers because there was no scenario in which a traveller could buy travel accommodation directly from the landlords. The landlords did not supply short term travel accommodation. They were supplying long term interests in land.

92. The FTT held at [73] and [74] that what is altered or processed must be "the thing supplied, i.e. the apartment", rather than the characterisation of the supply for VAT purposes. The FTT referred to *Finanzamt Heidelberg v ISt internationale Sprach- und Studienreisen GmbH* Case C-200/04 [2006] STC 52 in support of that finding. We do not need to consider *ISt* further, given that Mr Macnab no longer contends that a change in the treatment of the supply from exempt to standard rated will in itself amount to an alteration or processing for these purposes.

93. The FTT described the test it was applying to the apartments generally at [76] of the Decision. However, in describing what it considered to be the test, the FTT did not have regard to the need to construe the definition of designated travel services in Article 3 of the TOMS Order consistently with the requirements of the PVD, i.e. that the bought-in supply must be supplied for the direct benefit of the traveller. It is convenient to quote [76] again:

> 76. It seems to me to be clear from the nature of the TOMS that "material alteration or further processing" must refer to more than minor changes or processes which do not affect the fundamental character of the particular goods or services. It would be absurd as well as impracticable if any minor change or processing

excluded a bought-in supply from the TOMS. In order to be excluded from the TOMS, I consider that the alteration and processing must change the goods or services supplied so that what is supplied by the tour operator cannot be described in the same terms as the items acquired.

94. Mr Macnab did not specifically criticise this general formulation of the test in his submissions, and Mr Bremner said that it offered a helpful proxy for testing what was a material alteration. However, we do not consider that it is necessary or desirable to restate the test in a way that goes beyond the language of the TOMS Order and the PVD. That is because all cases will turn on their own facts. It ought to be sufficient to say that the scheme will apply where there has not been a material alteration or further processing of the bought-in supply such that what is bought-in is not supplied for the direct benefit of the traveller. That is the test the FTT was required to apply.

95. In the last sentence of [62], the FTT stated that there is no requirement that the bought-in supplies must be identical to the supplies provided by the tour operator to the traveller. That must be right on any view, and HMRC did not suggest otherwise. Mr Macnab did describe "the scenario envisaged" by the TOMS as being one of "back to back supplies" or "re-supplies" by the trader buying in services from third parties which are themselves carrying on business in the travel sector. Again, we do not consider that these alternative descriptions of the test are very helpful. Indeed, they tend to suggest that the bought-in supplies must be identical to the supplies provided to the traveller which is not the case. The terms used by Mr Macnab are therefore apt to confuse the real issue.

96. Mr Macnab also submitted that the FTT also erred in law at [73] and [74] of the Decision. It described the "thing supplied" as "the apartment" and "the apartments themselves", when in fact what was supplied was an interest in the apartment. Sonder acquired grants of leases for a term of years to occupy the apartments from the landlords. More particularly, it acquired the right to use the apartments as serviced apartments for the residential occupation of one or more occupiers. This was a materially different service from Sonder's supply of short term licences to travellers to occupy the apartments as holiday accommodation.

97. The FTT repeated what we consider to be a misdescription of the service supplied at [77] when it came to consider the unfurnished apartments. It refers to the apartments being supplied "without changing their structure" and notes that any changes "to the apartments" were cosmetic or decorative and did not amount to processing of "the apartment".

98. In our view, a focus on alterations to the apartment as the thing supplied, without sufficient regard to alterations in the rights granted in relation to the apartment as the service supplied, was an error of law. Although the FTT refers at [72] to letting the apartments for a term of years and then letting them as holiday accommodation, and concludes that the change did not amount to a material alteration or further processing, the question of materiality is only analysed by reference to the physical changes made to the apartment itself. Although the paragraph also cross-refers to [65] where the FTT states that the TOMS Order requires that the "right to use the apartments" was acquired and supplied without material alteration or further processing, there is no explanation as to why that is the case in relation to the totality of the right rather than the later explanation of the alterations made to the physical thing.

99. Mr Bremner correctly submitted that we should read the Decision as a whole and adopt a realistic analysis of the Decision. However, looking at the Decision as a whole it appears to us that at [73], [74] and [77] the FTT fell into error in focussing on the apartments themselves as the service supplied and the physical changes to the apartments themselves as the applicable alterations. In particular, at [77] the FTT ought to have been considering whether there was any material alteration or further processing of the term of years in an unfurnished apartment supplied by a landlord in circumstances where what was supplied to the traveller was a short term licence to occupy furnished holiday accommodation. We accept that the nature of the physical changes to the actual apartments are

relevant to the test which the FTT ought to have been applying, but the FTT did not compare the alterations to the full bundle of rights and interests supplied to Sonder with those which were supplied by Sonder to travellers in order to assess the materiality of those alterations.

100. For these reasons, we are satisfied that the FTT fell into error in the test which it applied pursuant to Article 3(1)(b) of the TOMS Order because it failed to have regard to the requirement that the bought-in supply must be for the direct benefit of the traveller, and mischaracterised the precise nature of the supplies to which the test is to be applied. These were material errors of law and we must allow the appeal and set aside the Decision.

Grounds 2 and 3

101. Grounds 2 and 3 do not therefore arise because we have allowed the appeal on Ground 1. We shall however say a little about Grounds 2 and 3.

102. HMRC say on Ground 2 that the FTT erred in law in finding that Sonder's supplies of unfurnished apartments were supplies of designated travel services within the TOMS Order. In particular, it is said that Sonder could not have made onward supplies without furnishing the apartments. The FTT ought to have found that furnishing the apartments constituted a material alteration or further processing of the supply received from the landlords.

103. HMRC say on Ground 3 that the FTT erred in law in failing to take into account that Sonder carried out significant and meaningful steps to perform its obligations to customers which amounted to a material alteration in the supply. It did so by paying utilities and council tax, and undertaking responsibility for the upkeep of the apartments. It did not merely entrust or sub-contract to a third party the performance of its contractual obligations to customers.

104. We have found that the FTT applied the wrong test in considering whether the TOMS Order was engaged. In those circumstances, we do not consider it would be helpful to address Grounds 2 and 3 in detail on the hypothetical basis that the FTT had applied the right test. Ground 2 challenges an evaluative judgment of the FTT. In relation to that challenge we must exercise the caution described by the Court of Appeal in *re Sprintroom Limited* [2019] EWCA Civ 932 at [76] and [77]. In short, if the FTT had applied the right test we would not have been persuaded that we should interfere with an evaluative judgment of the FTT as to whether the supplies of unfurnished apartments had been made without material alteration or further processing.

105. In relation to Ground 3, we would have adopted the principles described by the Court of Appeal in *Volpi v Volpi* [2022] EWCA Civ 464. The FTT was not required to set out every aspect of the evidence which it took into account in concluding that there was no material alteration or further processing of the supply, nor was it required to set out every aspect of its reasoning. If the FTT had applied the right test, we would not have been persuaded that the absence of any reference to the matters identified in Ground 3 amounted to an error of law.

Re-making the decision

106. We have allowed the appeal on Ground 1 and set aside the Decision. HMRC invited us to remake the decision and Mr Bremner did not suggest that the matter should be remitted to the FTT. In the circumstances we consider that it is appropriate for us to re-make the decision.

107. We have described under Ground 1 the error which the FTT made in considering whether Sonder's supply to travellers of holiday accommodation involved a material alteration or further processing of the interests in land supplied by landlords for a term of years, because it did not have regard to the question of whether what was bought-in by Sonder was supplied for the direct benefit of the traveller.

108. Mr Bremner simply submitted that, if there was such a requirement, in light of the FTT's findings at [62] – [67] and [71] the services acquired by Sonder were clearly for the direct benefit of travellers.

109. Mr Macnab simply submitted that Sonder acquired interests in land which were supplied for the indirect benefit of all travellers throughout the term of years for which Sonder's interest subsisted. There was therefore no direct benefit to individual travellers.

110. The FTT had been referred to a number of decisions of the VAT and Duties Tribunal, but at [75] it stated that it did not find those decisions particularly useful because cases will all turn on their own facts. We were also referred to those cases and have similarly concluded that they do not provide any real assistance. In particular, we do not accept Mr Bremner's submission that the present case is no different from *Independent Coach Travel v HM Customs & Excise* [1994] 2 CMLR 257. In that case, the taxpayer made block bookings of ferry crossings and hotel accommodation. The ferry bookings were made for the carriage of a particular number of people travelling by coach. The hotel bookings were made for a particular number of people for stays of varying lengths. The block ferry bookings were then sold to coach travel businesses, with or without appropriate hotel block bookings. On occasion the hotel block bookings would be sold on their own. The term "block booking" therefore referred to blocks of specific individual bookings on specific ferry passages or of specific hotel rooms for specific nights.

111. One argument on appeal to the VAT Tribunal was whether the taxpayer was a travel agent. The tribunal rejected an argument of the taxpayer that it was not a travel agent because it was not selling to individual travellers. An alternative argument that the taxpayer was not making supplies of designated travel services because the bought-in supply was being further processed was also rejected. In rejecting that argument, the tribunal stated at p265:

> In our judgment what ICT does by buying in in bulk supplies of accommodation and ferry crossings and supplying on the same services in quantity, although smaller quantity, as required by its customers does not constitute "further processing" as that expression is to be understood in this legislation. It seems to us that in relation to the supplies of services acquired and supplied on this operation where it is not identical is in fact less extensive than that commonly carried out by tour operators putting together packages and thus supplying travel services which without question are intended to be within the ambit of the Order. To hold that that kind of operation was enough to take services outside its scope would be largely to deprive the Order of any effect.

112. We have no reason to doubt the correctness of the decision of the tribunal in that case. However, the reasoning does not in our view apply to the facts of the present case. The bought-in supply in that case was a supply of travel facilities from ferry and hotel operators. In the present case, Sonder was acquiring rights to use and occupy apartments for a term of years. Sonder was therefore acquiring rights in land from which it could then make its own in-house supplies. That was the economic reality. Sonder was not acquiring specific nights (whether in bulk or individually) which were then supplied on to travellers.

113. Looking at the facts as a whole, we are satisfied that the service which was supplied by Sonder to the traveller was materially altered from that which was supplied by the third party landlord to Sonder having regard to the direct benefit requirement. Sonder acquired an interest in land for a term of years. The terms on which it did so were described by the FTT at [28] to [35] of the Decision which we have summarised above. We have taken into account all those terms, and give particular weight to the fact that Sonder entered into internal repairing and insuring leases for a term of years between two and ten years.

114. The supply which Sonder then made was a short term licence to the traveller to occupy property it had leased as holiday accommodation. We have summarised the FTT's findings above, although

the FTT does not describe in any detail the terms on which Sonder entered into licences with travellers. The evidence before the FTT included an overview of the "customer journey" which included signing up to Sonder's terms and conditions. The material terms and conditions simply required payment by the traveller including authorisation to charge a credit card in the event that any damage was caused to the apartment in consideration of the grant of a temporary right of occupation to the traveller. Overall the way in which the traveller's licence to occupy is described indicates that there is no reason to think that those terms would be any different to the basis on which a hotel or similar establishment might offer accommodation for the benefit of travellers, which is the basis on which the TOMS Order is said to apply in the first place. It is a very different bundle of rights from those which were granted to Sonder by the landlords.

115. The services received by the traveller in consequence of the grant of a licence to occupy are described in [36] to [42] of the FTT's decision and are markedly different to the services which Sonder itself acquired on entering into the leases with the landlords. In our view, it is relevant even if not determinative, that these marked differences were themselves reflected in the difference in the VAT treatment of the supply to Sonder and Sonder's supply to the traveller. The fact that both Sonder's rights under its leases with the landlords and a traveller's rights under its licence from Sonder both gave rights of occupation does not mean that what Sonder acquired was supplied to the traveller without material alteration or further processing such that it was supplied for the direct benefit of the traveller. In our view the services supplied by the landlord to Sonder were not for the direct benefit of Sonder's own customers and the services were not supplied by Sonder for the benefit of the traveller without material alteration and further processing. In short, the services supplied by Sonder to the traveller were its own in-house supplies, which therefore fall outside the ambit of TOMS.

116. It is not necessary for us to deal with Mr Macnab's submission that the bought-in supply must in the present context be a supply of travel accommodation. On the present facts we can simply say that the term of years purchased by Sonder was not supplied without material alteration or further processing such that it was for the direct benefit of the traveller.

117. The position is even clearer in relation to the unfurnished apartments. Sonder acquired an interest in land for a term of years in an unfurnished apartment. It furnished the apartment and then supplied a short term licence to a traveller to occupy as holiday accommodation. What was supplied to the traveller was materially different to what was supplied to Sonder.

Conclusion

118. For the reasons given above, we allow the appeal on Ground 1 and set aside the decision of the FTT. We re-make the decision so as to dismiss Sonder's appeal against the assessments.

MR JUSTICE TROWER
JUDGE JONATHAN CANNAN

Release date: 14 January 2025