[2019] UKFTT 0748 (TC)

TC07505

Appeal number: TC/2018/03379

VALUE ADDED TAX – children's activity boxes - whether single standard rated supply or mixed separate supplies of zero rated and standard rated goods

FIRST-TIER TRIBUNAL
TAX CHAMBER

DODADINE LIMITED T/A TOU-CANBOX **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S **Respondents**

REVENUE & CUSTOMS

TRIBUNAL: JUDGE MARILYN MCKEEVER

MRS JO NEILL

Sitting in public at Taylor House, 88 Rosebery Avenue, London EC1R 4QU on 18 November 2019

Ms Charlotte Brown, Counsel for the Appellant

Mr John Nicholson, an officer of HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This is an appeal against four assessments issued by HMRC under section 73(2) Value Added Tax Act 1994 ("VATA") in respect of VAT which it says the Appellants underpaid in the VAT periods from 01/14 to 07/17. The Appellants contend that their activity boxes for children, which contain a book or magazine and craft activities should be regarded as a mixed supply of zero rated and standard rated items for VAT purposes. They accounted for VAT on this basis for the period to which the assessments relate. HMRC, following a review, conceded that the Appellant's "Super" and "Grande" boxes, which included books, were indeed mixed supplies but that the "Petite" box, which included a magazine was a standard rated supply

2. The assessments were for the following amounts.

Date of Assessment	VAT Period(s)	Amount (£)
20 September 2017	01/17	106,989.93
6 October 2017	04/17	105,616.73
6 October 2017	07/17	101,714.45
10 October 2017	01/14-10/16	383,335.00

3. The total assessed VAT was £697,656.11. This figure needs to be revised as, on review, HMRC accepted that some of the supplies had correctly been treated as mixed supplies. The assessments were made on a "best judgement" basis. Revised assessments have not yet been produced and the Appellants reserve their position on the quantum of the assessments and whether they were to HMRC's best judgement. The present hearing is concerned only with the characterisation of the supplies. The goods in question are the "Petite" toucanBoxes produced by the Appellant.

4. We had before us a bundle of documents including a witness statement from a customer of the Appellant. As HMRC did not wish to challenge the witness statement, it was unnecessary for the witness to attend the hearing. We also heard oral evidence from Ms Virginie Charles-Dear who is the founder and CEO of the Appellant, toucanBox. The Appellant also provided us with two samples of the Petite toucanBoxes on the themes of dinosaurs and kings and queens respectively.

The facts

History of the toucanBoxes

5. ToucanBox is an online retailer of children's activity boxes which are designed to be educational and entertaining and are aimed at 3-8 year old children.

6. Customers subscribe to receive toucanBoxes on a regular basis, either monthly or fortnightly. A prospective customer, typically a parent or grandparent of a child within the target age group, can apply online for a free toucanBox. The company describes them as "triallists". If the triallist continues to subscribe for the toucanBox, they become a customer. An important point is that a triallist knows exactly what they can expect to receive as they will already have sampled the product.

7. In April 2012, the Appellant launched the first toucanBox, the Super box, which contained a book and four craft activities. The book and activities were themed. The books were a key part of the product designed to extend learning and to help parents and children explore the theme further. Initially, the books were hardbacks but these were superseded by paperbacks. The Super box sold at £19.90.

8. In November 2013, the Appellant introduced a "taster" box which was the forerunner of the Petite box. It was initially intended as the free sample to encourage triallists to convert to customers and was designed to fit through a letter box.

9. Ms Charles-Dear indicated that the company regularly sought customer feedback and that the products evolved in line with that feedback.

10. The feedback on the taster boxes was positive and led to the introduction of the Petite boxes as a discrete product line. An important feature of the Petite box was that it could fit through a letter box, which imposed size limitations on the contents. The craft activities used smaller, thinner materials. The Appellant wanted to include a book with the package. As noted, this was regarded as a key part of the product. It proved difficult to source a book which was small enough to fit into the box. The company was keen to begin selling the Petite box in order to generate revenue and so initially, they were launched with craft activities only. The cost of the Petite box was originally £3.95, increasing to £5.95 in February 2017 in order to reflect increasing prices and to align the company's pricing better with that of competitors. All the prices mentioned included postage and packing.

11. The Appellant found that the price of the Super box was a barrier to purchase for many prospective customers and in December 2013 it launched the Grande box which included two craft activities and a book which retailed at £12.90.

12. In January 2014, the Appellant concluded that it would not be practicable to source a suitable book for the Petite boxes and decided to develop a magazine which could be included in the box and which would contain separate content, designed to extend the thematic learning in the same way as the books did in the larger boxes.

13. In the course of 2015, after raising funds from investors, toucanBox began to develop a magazine for inclusion in the Petite box which was produced (along with the books for the larger boxes) by a new, in-house, editorial team. The magazines had 12 pages containing activities separate from the crafts. The possibility of selling the magazines separately was discussed, but not pursued at the time. The magazines were, however designed to allow that in future.

14. In August 2015, the first magazine was published and included in a Petite box.

15. Initially, the box contained various other pieces of paper, besides the magazine, and in particular:

- A four page instruction booklet for making the crafts
- A further cardboard instruction sheet
- Promotional material from other retailers
- Refer-a-friend leaflets.

16. The Appellant received negative feedback from customers that there were too many pieces of paper in the box and things got lost as the box contents were spread out on the table.

17. In response, toucanBox reduced the amount of paper by omitting the advertising material and including the craft instructions as a separate fold out which was attached to the magazine, but which could be detached. Underneath the fold out page, was the magazine's front cover. The intention was that the magazine should appear as a separate entity.

18. In the course of 2016, the magazines were translated into French and Italian.

19. From October 2017, the fold out craft instructions included a perforation mark showing that they could be detached from the magazine. The magazine was also redesigned at this time, with the intention of being able to sell the magazines separately from the crafts. The front cover, editorial and back pages were changed, the Appellant obtained an ISSN number for the magazine and registered it with the British Library and with the relevant authority in France as a magazine.

20. We find in relation to both the pre-October 2017 magazines and the post-October 2017 magazines that although the instructions were attached to the magazine, they did not form part of it. The physical attachment did not constitute an "obvious link" as Mr Nicholson put it so as to make one part of the other.

21. The magazines are now sold separately from the craft boxes. They are available on the company's website as packs of 12 back copies. Ms Charles-Dear indicated that it would not be economic to sell them singly.

22. The Appellant has discontinued the Super and Grande boxes in order to focus on the Petite boxes.

23. Mr Nicholson, rightly, cautioned us about taking account of matters which occurred outside the VAT periods in question. Whilst we note that caveat, we consider that it can be helpful to look at circumstances before and after the period in order to identify the correct treatment of the Petite boxes during the periods from 01/14 to 07/17.

The contents of the Petite boxes

24. We were provided with two sample Petite boxes, one from the July 2016-September 2016 period and the second in the current format.

25. The product arrives in a cardboard box. The boxes are addressed to the child and are personalised with the child's name.

26. The magazine is on the top of the contents and is the first thing one sees on opening the box. It is A5 in size and printed on good quality paper. Each of the sample magazines had 14 pages.

27. The 2016 box had a dinosaur theme. The craft instructions consisted of a folded A4 sheet which continued as the back cover of the magazine but could be easily removed and retained as a separate item. The magazine itself contains no reference to the craft activities. HMRC's review letter of 23 April 2018 acknowledges this and that the instructions can now be removed.

28. The instructions contain simple diagrams and show colourful images of the finished crafts. The first page is headed "Let's get making" and on a banner underneath (in this case) "Dinosaur Tail & Mask".

29. Underneath the instructions is the front page of the magazine with a colourful illustration of dinosaurs and the title "Let's Visit the Land of the Dinosaurs". The back page is also illustrated with dinosaurs and includes a bar code and social media information and the branding "toucan Box".

30. Inside, the magazine contains information on the theme and a number of activities as follows:

- Dinosaur time line
- Find the hidden T-rexes
- Colour the dinosaur (with "did you know" facts) and a larger picture to colour
- Match the picture of the dinosaur to its description
- A recipe to cook
- Maze type activities

32. All the materials needed to complete the craft activities were in the box. They were:

- A fabric "tail" that could be tied round a child's waist

- Foam spikes and sticky tape
- Foam decorations
- A pre-cut dinosaur mask and lolly stick (for holding the mask)
- Felt tip pens to decorate the mask
- Stickers.

33. The magazine did not refer to the crafts/instructions in any way and vice versa.

34. The 2017 box which was on the theme of kings, queens and dragons was very similar in format. The craft activities were a "royal crown" and finger puppets with all the materials needed to make and colour them included in the box.

35. The only difference in the style of the instruction sheet is that the sheet now has a dotted line to indicate where it can be cut to remove it from the magazine.

36. The magazine has a redesigned front page which now has a title "toucanBox Arts and crafts magazine" and at the bottom of the page "The Kings, Queens and Dragons Issue". The back page is similar in format to the earlier version but now includes the ISSN number and a cover price, in this case, £5. This has been reduced to £3.95. The first inner page consists of an editorial introducing the theme.

37. The content consists of:

- A maze
- A sequencing activity
- Match the "famous royals" to their descriptions
- Design a castle colouring activity
- A picture story
- A cooking activity
- A creative story writing/drawing activity.

38. Again there was no link between the magazine and the crafts, other than the theme.

Ms Charles-Dear's evidence

39. Ms Charles-Dear gave evidence about the evolution of the Petite box concept and the magazine itself (which we have summarised above) and the impact of the introduction of the magazine on the business. There were three key exhibits to Ms Charles-Dear's witness statement which provided an insight into these matters and which were explored extensively at the hearing. They were: a customer survey conducted in August 2018 (the "survey"), the sales figures before and after

the introduction of the magazine and figures for the "conversion rate" of triallists into customers, following the introduction of the magazine.

40. We heard from Ms Charles-Dear that toucanBox regularly conducted customer surveys in order to obtain feedback from customers and, as we have seen, the products evolved in response to that feedback. The August 2018 survey was called "toucanBox magazine survey". It covered a number of areas including questions about which pages the customer's child had most enjoyed, the age of the child, whether the magazine was age appropriate, possible additional content and, most importantly in the present context, "How important is having a magazine or activity book to your overall toucanBox experience" and "If the magazine was available to purchase separately, how much do you think it could retail for?". For the former question, customers could choose "very important", "important" or "not at all important". They also had the opportunity to add comments explaining their answer. For the second question, customers could state a price and add comments.

41. The survey was sent to 16,305 recipients as part of a regular online newsletter. Of these, 2,856 recipients opened the survey, 655 clicked on it to start it and 161 replied to the survey, that is, about 1%. Although that might sound a small percentage, Ms Charles-Dear gave evidence, which we accept, that this is in line with industry norms and was considered a good level of response given that no incentive was offered for the response. She went on to explain that statistical models indicated a 95% confidence level that the survey answers represented the true views of the customer base. That is to say, applying these principles, the confidence that these responses provide a representative sample of customers' views is between 88% and 96%.

42. In response to the question "how important is the magazine" a total of 91.3% said that it was "important" or "very important" and only 8.7% said that it was "not at all important". The survey results included four A4 pages of additional comments/explanations which expressed a range of views. Of the 161 people who had responded, 120 had made additional comments. Unsurprisingly, each of the parties highlighted the comments which best supported their own case. There are too many to set out in full, but we set out some examples below:

> Fun but the main event is the activity
>
> The box is great fun by itself. So is the book. They are not interdependent.
>
> It's a nice adjunct to the box
>
> Just extra things to do
>
> Makes the box much more than one and done as he's little my son and I do bits from the magazine each day so we can kinda drag out the experience til the next one arrives (sic)
>
> Nice extra
>
> My granddaughter looks through the book before doing any of the activities

I think it's a nice addition. Something that can be looked at after the initial crafting is done.

It's fun. But the box would be great without it as well. It does add to the experience but it's not essential.

We don't always have time to do the crafts as soon as he's opened the box. But we can read the magazine and do the puzzles over a few mealtimes which is great.

It expands the themes involved in the craft activity and promotes reading, problem solving and introduces ideas that are from all around the world.

It's a nice addition but the box and craft activity is the focus.

My boy likes doing the other activities, possibly more than the craft.

Otherwise end up buying a magazine as well as or instead

It's an essential element

The craft activities are the highlight of the package

When themed with the box they bring the whole box together, allowing the child to learn as well as to develop creativity.

We love the magazine, we make the craft and then work our way through the magazine. Extends the time we spend with the Toucan box.

It's an extra thing for him to do another time.

43. Although a variety of views are represented by the comments, it remains the fact that over 91% of respondents regard the magazine as "important" or "very important".

44. We had in our bundle, a witness statement by a "typical consumer", a Mrs Janet Braithwaite who subscribes for the Petite box and who set out how her daughter uses it. Mrs Braithwaite was not required to attend the hearing. Her statement indicates that her daughter engages first with the magazine when she opens the box. If there is time she will do the craft when she receives the box and look at the magazine later the same day. Otherwise she will work he way through the magazine on her own.

45. Her daughter always makes the crafts and keeps them to play with. She keeps the magazine and goes back to it regularly eg for ideas for baking. She keeps the magazine in a box along with other standalone magazines which have been bought for her.

46. We cannot attach much, if any, weight to Mrs Braithwaite's statement. At most, it is an extended comment explaining why she and her daughter value the magazine as an independent element, but on its own, it does not add anything to the survey.

47. There were a wide range of responses to the survey question about how much subscribers would pay for the magazine if it were available separately ranging

from "I wouldn't buy it separately" to £5. The average price which customers were prepared to pay was £2.50 which is about half of the price of the toucanBox.

48. Ms Charles-Dear stated that one on the main key performance indicators is the "activation rate", that is, the proportion of triallists who go on to become subscribers after receiving their free taster box. We were provided with a graph which showed activation rates between Q1 of 2015 and Q2 of 2016. In Q2 of 2015, before the introduction of the magazine, the activation rate was 54%. In Q3 2015, when the magazine was introduced, the activation rate increased by 13% to 67% and remained fairly stable, at the higher rate for the remainder of the period for which we had figures.

49. The final piece of key evidence is the gross revenue figures for the periods from January to June 2015 ie before the introduction of the magazine and from July to December 2015, after its introduction. The gross revenue in the second half of the year was almost double that in the first half year. Ms Charles-Dear stated that there were no other changes in the business (apart from the introduction of the magazine) which could account for this.

Procedural history

50. The Appellant had, from the outset, treated the Super and Grande boxes as mixed supplies of standard rated craft materials and a zero rated book. The Petite boxes did not initially include the magazine and the Appellant accepts that during that period, the Petite box consisted of a standard rated supply of craft activities. From August 2015 when the magazine was included in the box, the Appellant treated the boxes as a mixed supply.

51. On 7 February 2017 the Appellant's accountants, Accordance, wrote to HMRC seeking agreement to the method which it had used to apportion the VAT on the boxes between the standard rated supplies and the zero rated supplies. As the craft activities and magazine were produced in-house for the Petite box, the apportionment method was based on staff salaries and the time spent on the different components. This resulted in an apportionment of 70% to the Activity Book (as it was described) and 30% to the craft items giving a VAT rate of 6.04% on the box. As the components for the Grande and Super boxes were bought from third parties, the apportionment was carried out based on costs.

52. HMRC replied on 16 June 2017. The officer Mrs Hill stated that in her view, the booklet was an instructional aid to the main purpose of the craft set and she was going to raise assessments on the basis there was a single standard rated supply of a craft set. HMRC had only seen a sample of the Petite box. Mrs Hill sent a decision letter dated 20 September 2017.

53. Accordance requested a review of the decision on 31 January 2018 setting out a great deal of information and analysing the VAT treatment in the light of the case law which we refer to below. Accordance also sent HMRC samples of the Super and Grande boxes.

54. HMRC's decision on review, issued on 23 April 2018 was that the Grande and Super boxes were mixed supplies, but the Petite boxes were standard rated. The

reasons were broadly those that Mr Nicholson submitted and which are discussed below, so we need not set them out here.

55. The Appellant filed a Notice of Appeal on 22 May 2018.

56. There followed an ADR process after which the Appellant was invited to submit arguments for a further review which Accordance did on 28 September 2018. The further review upheld the the 23 April 2018 review letter by a letter dated 19 November 2018.

The law

57. The VATA sets out the circumstances in which a supply of goods or services will be subject to the standard rate of VAT. Section 30 and Schedule 8 VATA provide for certain categories of goods to be zero rated. Group 3 of Schedule 8 provides for the zero rating of books and magazines.

58. It is common ground that the craft activities, if supplied on their own, as was the case until August 2015, would be standard rated. Also that the magazine, if supplied on its own, which it now is, would be zero rated. It is further common ground the the VATA does not assist in determining whether a supply of two items together constitutes a mixed supply, in which case, the relevant VAT rate applies to each item or whether there is a single supply, so that both items must be taxed at the rate applicable to the dominant supply.

59. The principles to be applied are set out in a number of leading cases which both Mr Nicholson and Ms Brown relied on to support their respective contentions.

60. The first case is *Card Protection Plan Ltd v Commissioners of Customs and Excise* Case C-349/96, a case of the CJEU which was referred by the House of Lords ("*CPP*"). This case concerned the provision of insurance services to credit card holders to protect them in the event of the fraudulent use, theft or loss of their cards. As part of the service, CPP also maintained a register of customers' cards, provided a 24-hour telephone "helpline", assistance in obtaining replacement cards and certain other services.

61. Ms Brown took us to paragraphs 29 to 31 of the CJEU decision where the Court set out the salient principles to be applied:

> "…it follows from Article 2(1) of the Sixth Directive that every supply of a service must normally be regarded as distinct and independent and, second, that a supply which comprises a single service from an economic point of view should not be artificially split, so as not to distort the functioning of the VAT system, the essential features of the transaction must be ascertained in order to determine whether the taxable person is supplying the customer, being a typical consumer, with several distinct principal services or with a single service.
> 30. There is a single supply in particular in cases where one or more elements are to be regarded as constituting the principal service, whilst one or more elements are to be regarded, by contrast, as ancillary services which share the tax treatment of the principal service. A service must be regarded as ancillary to a principal service if it does not constitute for customers an aim in itself, but a means of better enjoying the principal service supplied (Joined Cases C-308/96 and C-94/97 *Commissioners of Customs and Excise v Madgett and Baldwin* [1998] ECR I-0000, paragraph 24).

> 31. In those circumstances, the fact that a single price is charged is not decisive. Admittedly, if the service provided to customers consists of several elements for a single price, the single price may suggest that there is a single service. However, notwithstanding the single price, if circumstances such as those described in paragraphs 7 to 10 above indicated that the customers intended to purchase two distinct services, namely an insurance supply and a card registration service, then it would be necessary to identify the part of the single price which related to the insurance supply, which would remain exempt in any event. The simplest possible method of calculation or assessment should be used for this (see, to that effect, Madgett and Baldwin, paragraphs 45 and 46)."

62. This indicates that the starting point is that each supply should be treated as an independent supply, but if the essential features of the transaction show that there is a principal supply to which another supply is ancillary, there is a single supply for VAT purposes. The single supply would be taxed in accordance with the treatment of the principal supply.

63. Mr Nicholson took us to paragraph 49 of the Advocate-General's opinion which emphasised that one should seek to avoid complex arguments about the cost of different elements of a single supply.

64. He also referred to the House of Lords decision in applying the CJEU decision, where the Court said:

> "**[22]** It is clear from the European Court of Justice's judgment that the national court's task is to have regard to the "essential features of the transaction" to see whether it is "several distinct principal services" or a single service and that what from an economic point of view is in reality a single service should not be "artificially split". It seems that an overall view should be taken and over-zealous dissecting and analysis of particular clauses should be avoided.
>
> **…**
>
> **[25]** If one asks what is the essential feature of the scheme or its dominant purpose, perhaps why objectively people are likely to want to join it, I have no doubt it is to obtain a provision of insurance cover against loss arising from the misuse of credit cards or other documents. That is why CPP is obliged to, and does, arrange, through brokers, with an insurance company like Continental for that cover to be available."

65. Lord Slynn indicates that in order to avoid "artificially splitting" a single service, one should ask why, objectively, people are likely to want it. In other words, what is it they are buying. In this case, the Court held that the customers were buying an insurance service and the other services provided were services which were useful, but merely ancillary services.

66. The meaning of ancillary was considered in the case of *Harley-Davidson Europe Limited v HMRC* [2017] UKFTT 973 (TC) ("*Harley-Davidson*"). That case related to the Harley Owners Group, where owners and aficionados of the motorcycles could pay for membership. Membership came with a series of additional benefits including a magazine, badges, maps and so on. The question arose whether this was a single supply of membership (including the benefits) or mixed supplies of membership and other products. The Tribunal said:

> "In order to succeed in his primary argument Mr Hill would need to persuade me that all the benefits provided were simply "ancillary" to the status of membership. In *College Estate Management v Customs & Excise* [2005] STC 1597 Lord Walker approved the description of that term by Ward L J in the court of Appeal as meaning subservient, subordinate and ministering to something else (paragraph [30]). My view is that this is simply not a correct description of the individual benefits provided. For example…the receipt of the hard copy magazine is important. The sample magazine provided clearly indicates it can be enjoyed by itself, and by any owner or lover of Harley-Davidson motorcycles."

67. Further guidance can be derived from the CJEU case of *Levob Verzekeringen BV v Staatssecretaris van Financien* Case C041/04 ("*Levob*"). That case concerned the supply of computer software by an American company to a Dutch Insurance business. The software was in English and could not be used by the Dutch company as it stood. The US company also undertook to provide customisation of the software, translating the program into Dutch and modifying it to be capable of dealing with certain features of the Dutch insurance market. The US company was also to install the software and provide training for the Dutch company's staff.

68. The CJEU held that the "principle/ancillary" supply test set out in *CPP* was not applicable here and proposed an alternative test; that there was a single supply where the components are so closely linked that they are not of benefit to the average consumer if they are supplied in isolation. The Court said:

> "68. In the present case, neither of the two main supplies (the supply of the standard software and the customisation thereof) is subsidiary to the other in such a way that it clearly represents an ancillary supply. However, it cannot be concluded on this basis that the two supplies cannot be regarded as a single comprehensive supply for VAT purposes. The principal/ancillary supply arrangement is only *one* scenario already recognised in case law.
> 69. The essential issue is still to determine the substance of the supplies, taking all the circumstances into account. In this connection, it is important whether both supplies are so closely linked that, in isolation, from the perspective of the average consumer, they do not have the necessary practical benefit for customers."

69. In *Levob* it was clear that neither component of the supply was of any use to the Dutch company without the other component. When one asks, "what was supplied", the practical answer from the company's point of view was "software that works for our staff in our industry". Neither the software on its own nor the customisation on its own was of any use at all to the purchaser. From their perspective they needed, and were buying, a single, combined package of software which could meet their needs only as a package.

70. In *Honourable Society of Middle Temple v Revenue and Customs Commissioners* [2013] UKUT 0250 (TC) ("*Middle Temple*")the Upper Tribunal set out the principles to be derived from the CJEU cases about how to analyse whether supplies are a single composite supply or separate supplies of different elements for VAT purposes. In that case, Middle Temple supplied leases of premises , subject to an option to tax, together with the provision of cold water. At paragraph 60, the Tribunal said:

"Principles derived from CJEU cases
[60] The key principles for determining whether a particular transaction should be regarded as a single composite supply or as several independent supplies may be summarised as follows:

(1) Every supply must normally be regarded as distinct and independent, although a supply which comprises a single transaction from an economic point of view should not be artificially split.

(2) The essential features or characteristic elements of the transaction must be examined in order to determine whether, from the point of view of a typical consumer, the supplies constitute several distinct principal supplies or a single economic supply.

(3) There is no absolute rule and all the circumstances must be considered in every transaction.

(4) Formally distinct services, which could be supplied separately, must be considered to be a single transaction if they are not independent.

[2013] STC 1998 at 2014(5) There is a single supply where two or more elements are so closely linked that they form a single, indivisible economic supply which it would be artificial to split.

(6) In order for different elements to form a single economic supply which it would be artificial to split, they must, from the point of view of a typical consumer, be equally inseparable and indispensable.

(7) The fact that, in other circumstances, the different elements can be or are supplied separately by a third party is irrelevant.

(8) There is also a single supply where one or more elements are to be regarded as constituting the principal services, while one or more elements are to be regarded as ancillary services which share the tax treatment of the principal element.

(9) A service must be regarded as ancillary if it does not constitute for the customer an aim in itself, but is a means of better enjoying the principal service supplied.

(10) The ability of the customer to choose whether or not to be supplied with an element is an important factor in determining whether there is a single supply or several independent supplies, although it is not decisive, and there must be a genuine freedom to choose which reflects the economic reality of the arrangements between the parties.

(11) Separate invoicing and pricing, if it reflects the interests of the parties, support the view that the elements are independent supplies, without being decisive.

> (12) A single supply consisting of several elements is not automatically similar to the supply of those elements separately and so different tax treatment does not necessarily offend the principle of fiscal neutrality."

71. Although a lease and a supply of cold water could, outside the Inn, be obtained from different suppliers and would be separate supplies, a lease of premises could not be obtained within the Inn separately from a supply of water. Both supplies were held to be indispensable to the use of the premises; neither could be properly enjoyed without the other. The Tribunal said at paragraph 69:

> "**[69]** The Middle Temple provides the right to occupy the premises in the Inn and also provides cold water to those premises. We acknowledge that the two elements supplied by the Middle Temple to the tenants may be provided separately in other circumstances. A tenant of a landlord (including the Middle Temple) outside the Inn may obtain a supply of water directly from the water company. However, the tenants of premises in the Inn have no choice but to obtain water from the Middle Temple. As both accommodation and water are essential if they are to occupy and use the premises, the tenants must be assumed to require a combination of those two elements if the premises are to fulfil their economic purpose. We consider that the leasing of the premises and the supply of the water to those premises under the lease form a single economic supply which it would be artificial to split because, from the point of view of the typical tenant, both the premises and the water are equally indispensable and inseparable. It cannot be disputed that the right to occupy the premises is an indispensable part of the supply to the tenants. The FTT accepted that water was indispensable when it found, at [51], that it was required for human life and, at [52], that the lease would not have any practical utility without the supply of water. Likewise, a supply of water would be pointless without the premises. As both premises and water are required in order for the tenants to occupy and use the premises, we consider that the two elements are not only indispensable but also inseparable. Applying the analysis of the CJEU in *Deutsche Bank*, our view is that the provision of the premises and the cold water is an indivisible supply which it would be artificial to split."

72. When characterising supplies one must consider the viewpoint of the "typical consumer". The recent Upper Tribunal decision in *HMRC v the Ice Rink Company* [2019] UKUT 0108 (TC) clarified what this means. The Tribunal referred to *CPP*, and commented on it:

> "[29 (of *CPP*)]… the essential features of the transaction must be ascertained in order to determine whether the taxable person is supplying the customer, being a typical consumer, with several distinct principal services or with a single service.
>
> …"
>
> **[19]** The 'typical consumer' is mentioned in para 29, not as an arbiter of whether it would be artificial to split a single service into constituent parts, or whether one element of a supply is ancillary to another but rather as an aid to identifying precisely what has been supplied and whether that amounts to a single composite supply or several separate supplies. It therefore necessarily follows that the 'typical consumer' must be a recipient of the package of supplies whose characterisation is in dispute, and not simply a general customer of the business."

73. So the "typical consumer" is a person who receives the actual goods or services in question and not merely a person who receives other goods or services from the supplier or who receives similar goods and services from other suppliers. In the *Ice Rink* case, a customer could pay for admission to the ice rink only, hire skates only or buy admission with the hire of skates. The "typical consumer" in this context is the person who buys the "skating with skates" package and not any other type of customer. In *Middle Temple* the typical consumer was a person taking a lease in Middle Temple, not someone taking a lease outside the Inn. In our case, the typical consumer is a subscriber who, having received their free taster box signs up to receive regular deliveries of the Petite box.

The Appellant's submissions

74. The Petite toucanBoxes constitute a mixed supply of a zero rated magazine and standard rated craft activities. The typical consumer of Petite boxes were buying both the magazine and the craft activities as separate activities designed to promote themed learning in different ways as well as entertain young children.

75. Each activity could be enjoyed on its own separate from the other and it would not be artificial to split the supplies for VAT purposes.

The Respondent's submissions

76. Mr Nicholson argued that the Petite boxes constituted a single standard rated supply as the main supply was of craft activities to which the magazine was merely ancillary and the two elements were indivisible and it would be artificial to split them.

77. We noted that HMRC had accepted that the Super and Grande boxes were mixed supplies and asked what distinction HMRC drew between the larger boxes and the Petite box. Mr Nicholson erroneously thought the books and crafts in the larger boxes were on different themes, but this is not the case. All the boxes were themed. The main difference appears to be that the books are more substantial than the magazine and can stand alone and be sold separately. HMRC argue that because the magazine is smaller and less substantial than a book, it is subservient to the craft activity and so ancillary to the main supply which is of the craft activity.

Discussion

78. Both parties used the list of principles set out in *Middle Temple* as a framework for their submissions and we shall adopt that as a convenient approach, although there is a certain amount of overlap between the principles. It is important to note that in applying those principles we must conduct a balancing exercise, taking account of all the circumstances and giving appropriate, not necessarily equal, weight to all the relevant factors. Principle (3) in *Middle Temple* confirms that there is no absolute rule and all the circumstances must be considered in every transaction.

79. The starting point is that every supply must normally be considered distinct and independent.

80. Despite this general principle, a supply which comprises as single transaction from an economic point of view should not be artificially split.

81. In HMRC's view, the craft and, what Mr Nicholson described as a "pamphlet" were "obviously linked". He relied upon the fact that the pamphlet is deliberately themed to work hand in hand with the craft activity and provides instructions on how to complete the craft activity (ie the instructions are part of the magazine as they are attached to it). The pamphlet is integral to the craft activity and therefore the pamphlet cannot be seen as independent of the craft exercise. During the period under appeal, the magazines were not available separately and the fact that they are now is irrelevant. Mr Nicholson's position is that there is a single supply which it would be artificial to split.

82. Ms Brown submitted that one has to consider whether supplies are dependent on each other so that it would be artificial to split them. Ms Brown took us to paragraph 98 in *Harley-Davidson* where the Tribunal said:

> "…supplies that comprise a single supply from an "economic point of view" (*CPP* at [29], described in *Stock 94* at [27] as supplies that are "not independent") should not be artificially split. The test is an objective one. It is necessary to consider the characteristic elements of the transaction (*Stock 94* at [28]): in essence, what is acquired? In doing this the focus is on the typical consumer rather than any individual consumer, and on their economic objective (*Stock 94* at [29])."

83. In Ms Brown's submission, the magazine and crafts are independent of each other. The customer survey shows that the two elements are not dependent on each other. The crafts and magazine are used separately and at different times and many customers considered that their children derived different benefits from each of the items.

84. When one asks, "what is acquired?", Ms Brown's answer is that the typical consumer of Petite boxes were buying both the magazine and the craft activities as separate activities designed to promote themed learning in different ways as well as entertain young children.

85. She submits that it would not therefore be artificial to split the supplies. Each item is capable of standing alone.

86. Mr Nicholson disputed that a 1% response rate to the survey produced a representative sample and considered that a "typical consumer" was one who did not complete the survey and that customers who completed the questionnaires were not typical. On the other hand, Mrs Bishop of HMRC, who made the review decision in her letter of 23 April 2018 appears to have based her conclusion that "I do not consider that there is a realistic prospect that the magazines would be sold separately, even if they were available…" on the basis of conversations with two of her colleagues with young children. We prefer the statistics based approach of the Appellant.

87. Mr Nicholson also submitted that the "essential feature" of the boxes are the crafts which he argues are the main activity.

88. We recognise that the magazine and crafts are sold as a package. Ms Brown submitted that this was merely a marketing strategy and as set out in paragraphs 103 and 104 of *Harley-Davidson*, marketing is not the test. The question is, what is really being acquired, not what motivates individual consumers to make the purchase. In this case, Ms Brown contends, customers are acquiring a magazine and a craft activity.

89. We have found as a fact that the instructions for the crafts, although attached to the magazine, were not part of it.

90. We note that the Super and Grande boxes, which were accepted by HMRC as constituting separate, mixed supplies were also themed and were also sold as a package of book and crafts.

91. Whilst the crafts are not at present available on their own, and at the time in question the magazines were not available separately, the crafts were originally supplied on their own, before July 2015 and the magazines are now available separately on the website. This indicates that each item *can* "stand alone" and they are not so inextricably linked that it would be artificial to split them.

92. It is clear from *Levob* and *Middle Temple* that the sort of linked supplies which should not be artificially split are those where the different components of the supply are of no use to the typical consumer on their own and are only economically viable if provided together. One cannot take a lease of premises without a water supply. A water supply is no use on its own to a person who wants premises for their business. Software written in English cannot be used by the staff of a Dutch company. The customisation is useless without the basic software. As it was put in *Middle Temple*:

> "(5) There is a single supply where two or more elements are so closely linked that they form a single, indivisible economic supply which it would be artificial to split.
>
> (6) In order for different elements to form a single economic supply which it would be artificial to split, they must, from the point of view of a typical consumer, be equally inseparable and indispensable."

93. That is far from the position here. At various times the crafts and magazines have, in fact, been available separately and there is a market for each element on its own. This illustrates that it would not be artificial to split the supply. We examined the sample toucanBoxes and it was clear that the craft activities and the magazine are not dependent on each other. Each element can be used at different times without reference to the other items in the boxes. The customer feedback reinforces the view that each component is a welcome resource in its own right and each supports different learning objectives. It is clear that the crafts and magazine can be, and are, used and enjoyed separately by the children/grandchildren of the typical consumer. The typical consumer in this case is a parent or grandparent with children/grandchildren aged between 3 and 8 years who is a subscriber (and not a triallist) to toucanBox.

94. Accordingly, we find that the supply of the crafts and magazine are distinct and independent supplies. We conclude that it would not be artificial to split the supply and that the essential features of the boxes (both the crafts and magazine) constitute several distinct principal supplies rather than a single economic supply from the point of view of the typical consumer. (Principles (1), (2), (5) and (6) of *Middle Temple*).

95. Principle (4) of *Middle Temple* applies equally to goods.

96. Mr Nicholson argues that the magazine could not, in HMRC's view, be sold separately as it stands.

97. As we have seen, the magazines are in fact sold separately, albeit in a bundle of 12. Although this was not the case at the time to which the assessments relate, the test is not whether they were in fact sold separately but whether they are *capable* of being supplied separately. We have already found that the crafts and magazine are independent.

98. Further, the survey indicates that typical consumers would, on average, be prepared to pay £2.50 for the magazine if sold separately which is approximately half of the cost of the Petite box.

99. Before the magazines were introduced, the crafts were in fact sold separately, and the crafts only toucanBox was a successful product.

100. This points to there being separate supplies.

101. Principle (7) is neutral.

102. Principles (8) and (9) are derived from *CPP* and articulate the distinction between principal and ancillary supplies, even where the supplies are separate.

103. Mr Nicholson submits that the craft activities are the principal activities. He argues that customers subscribe for the boxes in order to receive the crafts, regarding them as the main activity and that the magazine is merely ancillary. In HMRC's view, the magazine complements the crafts and, by continuing the theme is simply a "means of better enjoying the principal service supplied". The magazine is not a substantial item and is not an "aim in itself". It is an add-on to the craft activities and subservient to them.

104. Ms Brown submits that the evidence shows that the Petite Box does not contain a principal and ancillary supply but two independent, principal supplies. They are physically and economically dissociable.

105. We are satisfied that the fact that the books supplied in the Super and Grande boxes are more substantial than the magazine cannot determine the matter. The size and degree of substance of the item is not the test. It is a question of how the boxes are perceived and used by the typical consumer. Nor does the fact that the boxes are themed affect the analysis. The whole point of the toucanBox concept is that the boxes provide themed learning through different media.

106. In order to be an "ancillary" supply in accordance with Lord Walker's test in *College of Estate Management*, the magazine must be "subservient, subordinate and ministering to [the craft activities]". That is simply not borne out by the evidence. When one examines the boxes, they present as two separate items. The magazine is on top. One does not need the magazine to enjoy the crafts and *vice versa*. They serve different educational purposes.

107. It is clear from the survey that they are indeed used separately and at different times. The magazine has greater longevity than the crafts. A child will often keep it and read it repeatedly. It cannot be said that the magazine is subservient to the crafts or that it is just a means of better enjoying the crafts. It is something which is used and enjoyed separately and in its own right, without reference to the crafts and, indeed, is used for longer than the crafts.

108. It is also our view that the evidence shows that the magazine is an "aim in itself". Over 90% of respondents to the survey regarded the magazine as important or very important. As noted above, the magazines are used independently, without reference to the crafts.

109. Following the introduction of the magazine the activation rate increased by 13% and gross revenue doubled. The survey showed that respondents were, on average, prepared to pay £2.50 for the magazine on its own-half the price of a Petite box. This is compelling evidence that subscribing customers, the typical consumers, regard the magazine as a desirable and useful resource for their children in its own right.

110. We conclude that the magazine is not ancillary to the craft activities but is a principal supply.

111. Principle (10) suggests that the ability of the customer to choose whether or not to be supplied with an element is an important factor in determining whether there is a single supply or several independent supplies. Although a consumer can choose to buy the magazines only, they cannot choose to buy the crafts only, so in the present case, this principle points to a single supply.

112. Separate invoicing and pricing (principle (11)) supports the view that the supplies are independent but is not decisive. Similarly, if the customer buys a package of items, both of which they wish to have, the fact that they are charged a single price is not decisive. Crafts and magazines from other suppliers are available separately. Customers of toucanBox choose to buy them together and they are designed to be bought together to reinforce the themed learning concept. Although a single price points towards a single supply, we do not give this factor a great deal of weight.

113. Principle (12), which relates to fiscal neutrality, is not applicable here.

114. We have considered all the evidence, written and oral, examined samples of the Petite boxes and taken into account all the other circumstances of the case. We have weighed the various factors and principles which may be drawn from the authorities. We consider that the most important factors to which we should have regard are the "principle/ancillary supply" test derived from *CPP* and the test from *Levob* that we should consider whether there is a single economic supply

which should not be artificially split. We have also given appropriate weight to the other factors identified and set out in *Middle Temple*.

115. Having performed the required balancing exercise we conclude that the magazine is not ancillary to the supply of the craft activities but is a valued resource in its own right and that it is not artificial to split the supplies.

Decision

116. For the reasons set out above, we have concluded that the Petite toucanBoxes are a mixed supply of a zero rated magazine and standard rated craft activities.

117. Accordingly we allow the appeal.

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

MARILYN MCKEEVER

TRIBUNAL JUDGE

RELEASE DATE: 13 DECEMBER 2019