

EUROPEAN COMMUNITY - Exemption with right to repayment - Appellant provides telecommunications network services for members - Whether Appellant's supplies meet the direct needs of aircraft - No - EC Sixth Council Directive article 15.9

ZERO RATING - Transport supplies - Passenger aircraft - Making arrangements for such supplies - Appellant operates telecommunications network system for member of air transport community - Whether Appellant makes arrangements for supplies of passenger aircraft related supplies - No - Whether Appellant's supplies meet "direct needs" of passenger aircraft - No - Appeal dismissed - VATA Sch 8 Gp 8 item 10 - EC 6th Council Direction Art 15.9

ISSUE ESTOPPEL - Res judicata - Decision given by tribunal in 1973 - Whether Commissioners estopped in present appeal from disputing 1973 decision on its merits - No

LONDON TRIBUNAL CENTRE

SOCIÉTÉ INTERNATIONALE DE TÉLÉCOMMUNICATIONS AÉRONAUTIQUES SC ("SITA") - Appellant - and - THE COMMISSIONERS OF CUSTOMS AND EXCISE - Respondents

**Tribunal: STEPHEN OLIVER QC (Chairman)
PRAFUL DAVDA FCA**

Sitting in public in London on 16-18 December 2002

Francis Fitzpatrick, counsel, instructed by Maxwell Batley, solicitors, for the Appellant

Peter Mantle, counsel, instructed by the Solicitor for the Customs and Excise, for the Respondents

© CROWN COPYRIGHT 2003

DECISION

1. Société Internationale de Télécommunications Aéronautiques SC ("SITA"), the Appellant, appeals against a ruling made by the Commissioners on 18 November 1997 that the relevant supplies should be standard rated. The ruling relates to the VAT treatment of supplies of telecommunication services by SITA to its members who are airlines and other members of the air transport community throughout the world.

2. The relevant supplies have been treated as zero-rated. The treatment of the supplies as zero-rated was endorsed by a decision of the VAT Tribunal given in 1973 ("the 1973 Decision") following the agreement between SITA and the Commissioners as to its terms.

3. In brief, the three issues in this appeal are:

(i) whether, as SITA contends, its services are zero-rated by item 10 of Group 8 of Schedule 8 of VAT Act 1994 ("the Act") as being "the making of arrangements" for the supply of the aircraft-related services referred to in the item;

(ii) whether, as SITA contends, the Commissioners are estopped by reason of the prior judicial decision on the same matter between the same parties (i.e. the 1973 Decision) when disputing the VAT treatment of SITA's supplies to its members and

(iii) whether, as SITA contends, the supplies qualify for exemption (with repayment of tax) under paragraph 9 of Article 15 of the Sixth Directive.

We shall deal with issues (i) and (iii) in Part I of this Decision. Issue (iii) will be convened in Part II.

4. We heard evidence from three witnesses for SITA. Bryan Wilson MA, now SITA's senior vice president of application services, was in 1997 BA's general manager of network development in charge of designing its route network. Jean-Pierre Gaudard, now SITA's executive vice president, major programme development, was until 1997 vice president engineering, in overall charge of the technical design and development of the network. From 1997 to 2000 he was on secondment by SITA to work as managing director of SITA-Equant SC which, following the establishment of a joint venture between SITA and Equant, controlled the operational and technical aspects of the network. Jean Roworth is SITA's vice president taxation.

PART I

Findings of relevant facts

5. SITA has at all times been a non-profit making co-operative company established with limited liability under Belgium law. It was formed in 1949 by 11 airlines. The founding airlines had in those early days operated their own network centres using SITA as an overall network manager. By degrees the airlines transferred to SITA the responsibility for operating the network centres. SITA now operates in 220 countries.

6. SITA's current main objects are, so far as is relevant:

(a) to foster all telecommunication and information processing matters directly or indirectly connected with the transmission and processing of all categories of information required in the operation of the air transport industry and to study the problems relating to them with the aim of promoting in all countries safe and regular air transport;

(b) to develop, acquire, use and operate in all countries telecommunications and information processing means, and to provide efficient telecommunications, data processing and information transmission services;

(c)-(e) ..."

7. The share ownership varies each year, the shares being redistributed on the basis of each member's use of the facilities in the preceding year; the use that each member makes will have equated with its share in the overall cost of SITA's services. The shares carry voting rights but no rights to dividends or participation in liquidation.

8. Membership is open to anyone operating aircraft for the transport of passengers, mail or cargo. Members are charged for SITA's services at cost according to their use of the service or otherwise on the basis of an agreed tariff.

9. SITA is governed by a board of 30 directors, 20 of whom represent the 20 most extensive users. The chairman is appointed from among the airline members. SITA is managed by a director general and committees comprising specialist individual employees of member airlines. The committees are "the Infrastructure Development and Solutions Committee" and "the Finance Committee". The top executive management of SITA include many specialists from the airlines industry. SITA's activities are conducted on a regional basis.

10. SITA consults the air transport community in order to develop solutions to their networking and data processing requirements. It liaises with international organizations such as IATA, the International Telecommunications Union (of which it is senior member), the UN Conference on Trade and Development (with which it has a special consultative status) and the International Civil Aviation Organization (with which it has a special organization observer status). The Infrastructure Development and Solutions Committee manages these consultations and representations; it has a brief to review major projects and to prioritize them according to the requirements of its members.

11. The current membership of SITA is 728 of which 581 are airlines and 147 are other organizations within the air transport community. The 14 UK members of such other organizations include travel companies, aircraft systems businesses, engines and landing gear companies, an airport authority, an airport, a courier company and companies that provide airline schedules.

SITA's Activities

12. SITA operates as a single lessee of leased circuits (leased in from the public telecommunications organizations). It acts as the single provider providing a permanently available telecommunications network to its members, all of whom are participators in the air transport community. At the time of the Commissioners' decision (1997) and now, the network has been managed as a joint venture, the parties to which have been SITA and Equant (a company controlled by SITA's members and financed by outside capital). Under that joint venture agreement Equant has been free to sell its network services commercially while SITA has made available the features specifically required for the air transport community on a non-profit making basis.

13. The telecommunications network services supplied by SITA to members enable members to transmit messages either within the particular member's organization or between different members. (The messages will typically relate to passenger and freight reservations, baggage handling enquiries, aircraft handling and maintenance and associated administration matters. A great majority of them will be concerned with passenger and freight reservations.) SITA's role as

network provider includes the manipulation, routing, conversion and switching of data to enable the safe, secure and efficient transmission of these.

14. The older service, "Type B", developed from the teletype message service. The format of the message was relatively flexible, with headers and footers to ensure safe and reliable transmission. Type B messages are based on "store and forward" technology. The technology involves a one-way message, but with the possibility for multiple deliveries. The main feature of the Type B messaging service is that it links the members of the air transport community quickly and reliably. It handles regularly over 10 million messages a day. It is used for "mission critical" (the expression used by Mr Gaudard) applications such as aircraft movement, seat booking, cargo tracking, flight operations and for the management of aerospace parts and repairs. The service includes features designed specially for the air industry to ensure the delivery, fast retrieval, and tracking and audit facilities.

15. The other service is called "Type A" depends on newer technology. This system enables the transmission of data in certain set formats It enables interactive transactions including both question and response. It has been designed to enable members managing seat reservations to use their computers to make the enquiry linking up to the host computer; the response is automated and the booking records updated in the host computer following the transactions.

16. Both Type B and Type A services were developed using specific protocols specially developed for the air transport community by IATA. These are known as airline protocols and are still widely in use today.

17. The Type A transactions are based on the use of compatible technology which minimizes human involvement. These permit real-time booking of passenger seats through the query-and-response delivery over the SITA network to the airline's host computer.

18. In 1981 a new "Data Transport Network" was implemented. The basis for the technology was essentially similar to earlier technology known as "High Level Network" but with improved performance, traffic volumes and fault identification through the use of the new "Network Control System". One benefit of the Network Control Centre is that it allows the "lowering" of technology by enabling different generations of technology to co-exist and to be linked, so that centres with older technology may be linked to those with the latest developments.

19. In the early 1990s the Mega Transport Network (MTN) was introduced. The benefit of this was that it enabled the use of both older and newer protocols thereby facilitating the transmission of messages between different centres without being required to upgrade to the new technology. The MTN was designed to increase throughput capacity tenfold. By the end of 1995 there were 900 MTN network connection centres in 156 countries. The MTN response times improved to under one second, and the network availability reached 99.99%. However, while the volumes, speed and reliability had increased by 1997, the essential characteristics of the network have at all times (and since before 1973) remained the same. It has been based around leased circuits, with network equipment to control and monitor the reliable transmission of the messages and to support the diagnoses and correction of faults.

20. Cost efficiencies have played an important part in SITA's network developments in the 1990s. The establishment of the joint venture with Equant

(see paragraph 12 above) has enabled the costs of the facilities to be shared between general commercial use and the air traffic community.

21. A further feature of SITA's telecommunications network is the "frame relay access". This provides a data networking service for the interconnection of geographically dispersed local area networks. This service is available in nearly 200 countries. SITA's regulatory status as a "closed user group" enables it to provide the services to the air transport community worldwide and, without it, the airlines would be unable fully to access the service.

22. SITA also offers a fully managed global intranet solution, using the Transmission Control Protocol/Internet Protocol range of protocols, enabling the connection of global locations. SITA's special regulatory status enables the air transport community to use this service in a wider range of countries than would otherwise have been possible. SITA also provides special services enabling the conversion of airline protocols to the new technology; by this means airlines are able to retain older technology while at the same time taking advantage of the new.

23. Precisely what use members make of the network is unknown to SITA. SITA does not initiate the messages and does not read them. SITA will know the generic nature of the message from the system that has been used. There are different systems that handle respectively reservations, baggage arrangements and flight networks. The system with the "big pipe" is the one which handles reservations and transmits the highest volume of messages. Non-aircraft related transmissions, such as messages dealing with financial information, are accepted as relatively small.

24. SITA invoices members monthly. The amounts charged are based on their actual connections and usage. The charges are either agreed between SITA and individual members or based on a general pricing structure. The invoice sent to the member reveals the location of connections and the destination of messages. The invoices summarize the charges by "product group" to which we now refer.

25. The first product group, "managed data network services" (which are mainly for Type A transactions), are the method used for effecting passenger and freight reservations as well as other operational transactions such as passenger seat allocations. The charging calculations are made respectively under connection charge and transmission charge headings. The former are charges for access to the network. The latter are usage charges based on the amount and length of traffic sent over the network.

26. The product group "New Network Services" relates to use of later technology such as frame relay and intranet. The group "messaging services" breaks the charges into the different types of messaging services. The largest type is Type B. These are for SITA's person to person message system based on Type B technology and there is a fax service by which messages are delivered as faxes. The groups "Local Network Access Services" and Supplies to Companies covers SITA's provision of an end-to-end service to and from each user's premises. Most of the costs required to provide this are shared, but linked to the fixed network connection will be a tail circuit at the end of which will be local network access equipment, such as a modem or routes to link the tail circuit to the user's own equipment. These costs, being dedicated to one user, are recharged on an ad-hoc basis.

27. SITA's activities in the UK are conducted through a branch. This provides one of the main access points to switching centres within the global network. Through these the major users can obtain access to the central switching centre. The UK switching centre site is linked to others worldwide by leased circuit through which the members' transmissions are routed. Other UK activities, which do not relate to the supplies with which this appeal is concerned, are certain airports services, VHF air-communication services and a data processing centre for airline applications (such as cargo and flight planning). We will refer to these briefly later.

The use made by members of SITA's services

28. SITA's members are all members of the air transport community. They are all connected to SITA's network using compatible systems. They are competitors within their particular spheres of activity. They nevertheless have to co-operate. They have certain common requirements. These requirements include the need for a quick, reliable and cost-efficient transmission of messages and data, the ability to communicate with different parts of their own businesses as well as with other members of the air transport community, a network coverage that covers all destinations served by airlines and a neutral service provision to all members of the air transport community.

29. "Interlining" is one essential function that makes use of SITA's facilities. Different airlines serve different routes and different countries. Passengers' journeys often require the use of different airlines, different ticketing and reservation facilities, baggage handling facilities and customs and immigration handling activities. This calls for a system by which airlines, agents, freight forwarders and other members of the air transport community can communicate so as to co-ordinate, for example, bookings and reservations, dealings between airlines and their agents, baggage and passenger handling at airports, emergency procedures, catering and freight arrangements and baggage and passenger transfers. SITA's facilities are also used to enable co-operation between members in the use of limited airport, air terminal and air space facilities. There is a priority message system operated by SITA that enables safety messages to be given priority. The telecommunications system is also used to give members access to spare parts pools which are located in different parts of the world.

30. We turn now to the use made by members of the particular services provided by the network operated by SITA.

31. For passenger seat reservations each airline maintains, or subcontracts to a service company, its own database of future flights and availability of seats. This is distributed throughout the world, via the telecommunication network system offered by SITA, to all the sales channels that the airlines wished to deploy. Travel agents obtain access to the airlines' databases through the SITA network and airlines used the network to receive information about bookings and to update their own availabilities.

32. To cope with airport services, those airlines which do not have their own dedicated terminals use the network to process the management of passenger transportation; this covers last-minute sales, checkings, seat reservations, special meals, flight connections, interline transfers, bag management and departure control. The reconciliation system in SITA's network confirms that bags and passengers are matched. And the network system passes messages about each bag from airline to airport and onto the loading agent. The network also provides

a cargo function and supports the sales and operational activities. It is used to communicate lost property enquiries.

33. The airlines use the SITA network when carrying out their back office support procedures for flight operations activity. The airline in question obtains flight plans and communicates weather and flying notifications through the network. It receives advice about in-bound and connecting flights through the network. In all cases it uses the range of specialized protocols and message formats designed by SITA for the air transport community.

Conclusions on the facts

34. SITA provides and maintains a telecommunications network system. All supplies with which this appeal is concerned are to SITA's members. The structure and capacity of the network system have been designed for SITA's members with whom it is continuously consulting. As things are SITA's telecommunications network meets the needs of its members for, for example, interlining, making shared use of airport facilities, safety procedures, making passengers and baggage reservations and handling arrangements and dealing with maintenance and associated administrative matters. It meets those needs by providing the means for transmission and receipt of messages and other information. The system processes the messages and other information transmitted through the network and does so to the highest standards of accuracy, speed and reliability. Moreover we can safely infer that the great majority of the messages passing through SITA's network deal with the transportation of passengers and their baggage on commercial airlines. Without SITA's system its members would not, save for the local activities of some large airlines, be able to carry out their air transport businesses; they would have to find some acceptable alternative. We conclude that SITA provides an essential facility with which its members carry on their air transport and air transport-related businesses.

35. At the same time it is evident that SITA has nothing to do with the content of the messages, data and information transmitted and received through the network. Those matters are confidential to the users. The content of particular messages is not disclosed to SITA nor does SITA generate the information or messages transmitted on the system.

36. We heard no evidence that the services in issue in this appeal are used in the communications with or navigation or flight operations of aircraft.

37. For completeness we refer to the three categories of telecommunication and extended telecommunication services provided by SITA which are not the subject matter of this appeal. These are CUTE AND CUBES, Voice and Aircom. The CUTE (Common Use Transportation Enterprise) service was created in the mid 1980s in response to a shortage of space at airports. It enables the airlines to check in passengers at the check-in desk, to print out the required boarding cards and tags and to check passengers through the gate into the aircraft. CUBES (Common Use Baggage Enterprise System) provides a variety of centralized and airport-based applications which enable baggage-handling agents and airports to manage baggage locally and airlines to manage their own on a global basis.

38. The Voice service is based on the Mega Transport Network. It is a "virtual private network" that members can use to obtain voice services through core centres to enable them to contact SITA support functions for queries about the data network functions, e.g. Types A and B services.

39. The Aircom service relates to the requirements of the aircraft in flight. SITA's aircom service combines the worldwide ground coverage of the SITA network with specific VHF or satellite communication services to meet the in-flight requirements of the aircraft. Airline applications for these services include monitoring, maintenance, flight operations and logistic support. Examples of these are automatic dependence surveillance that enables ground control systems to receive reports of aircraft positions, heading and other related information, controller pilot data link communications used for air traffic services clearances and instructions (normally communicated by voice), oceanic clearance which enables the aircrew to request, receive and acknowledge oceanic clearance messages and weather reports.

The statutory provisions

40. The provisions relevant to the question of whether SITA's services are zero-rated under the UK VAT law are in item 10 of Group 8 in Schedule 8 to the Act. So far as is relevant, item 10 of Group 8 provides as follows:

"10. The making of arrangements for -

(a) the supply of, or of space in, in a ship or aircraft;

(b) the supply of any service included in items 1 and 2, 3 to 9 and 11; or

(c) the supply of any goods of a description falling within items 2A or 2B, or paragraph (d) of item 3."

As for (b), there are a number of items relevant to air transport. The principal items comprised:

"(2) The supply, repair or maintenance of qualifying aircraft or the modification or conversion of any such aircraft provided that when so modified or converted it will remain a qualifying aircraft.

(2A) The supply of parts and equipment, of a kind ordinarily installed or incorporated in, and to be installed, or incorporated in -

(a) the propulsion, navigation or communication systems; or

(b) the general structure

of a qualifying ... aircraft.

(4) Transport of passengers -

(a) in any ... aircraft ... designed or adapted to carry not less than 10 passengers ...

(c) on any scheduled flight ...

(6) Any services provided for -

(a) the handling of ... aircraft in a ... customs and excise airport or outside the United Kingdom; or

(b) the handling or storage -

(iii) in a customs and excise airport, or

(iv) in a transit shed,

of goods carried in a ... aircraft.

(6A) Air navigation services.

Contentions

41. SITA, represented by Francis Fitzpatrick, contends that its supplies fall within item 10 on the ground that it makes arrangements for supplies falling within each of paragraphs (a), (b) and (c) of item 10. It makes arrangements because it does things antecedent to and directly leading to the result sought to be achieved by doing those things: that result is the provision of supplies falling within those paragraphs. In this respect SITA satisfies the test adopted by the Court of Appeal in *Customs and Excise Commissioners v Civil Service Motoring Association* [1998] STC 111 at 118g-j. Its supplies, SITA argues, amounts to the making of arrangements notwithstanding that it is not either the agent for, for example, the airlines or the intermediary between the airline and its own customer. It is enough for these purposes, where the result to be obtained is of a general rather than a specific nature, that the arrangements have, as here, been planned and designed by the joint efforts of SITA and the airline in question; the critical thing is that there should be a nexus between the service supplied and the supply in question (see the tribunal decisions in *Barclays Bank* [1991] VATTR 466 and *Countrywide Assurance* [1993] VATTR 277). Here there is a nexus between SITA and the supplies that fall within item 10 because the whole purpose of the network services are to enable SITA's members to deliver the zero-rated supplies.

42. Thus, it is argued for SITA, it makes arrangements for the supply of -

- space in any aircraft : item 10(a) :
- services of supply, repairs or maintenance of qualifying aircraft or the modification or conversion of such aircraft : item 10(b):
- the transport of passengers (by e.g. transmitting messages relating to seat reservations) in aircraft that satisfy the conditions in item 4:
- the handling of baggage and goods within item 6.

43. The response for the Commissioners, represented by Peter Mantle, is that SITA's provision of telecommunication network services does not amount to the making of arrangements for any of the supplies covered by item 10. The expression "making of arrangements for" should not be given a wide construction; it should be confined to the activities of agents or like persons "acting" for a principal who himself makes or receives the supply within the relevant category in item 10. Here SITA does not make the arrangements for such supplies even though the relevant information and messages are

transmitted and received through SITA's network. SITA neither initiates those messages nor knows their content.

Conclusions on item 10

44. No authority that has any real bearing on this issue has been cited to us. However, if we were asked whether in the ordinary use of the English language SITA's supply amounted to the making of arrangements for, for example, the transport of passengers, our answer would be unreservedly - no. We would say that instead SITA was supplying something quite different, namely a purpose-designed telecommunications network for the use of its members. In making that supply SITA is providing the facility with which its members carry on their air transport related businesses.

45. In reaching that conclusion we recognize that the shared telecommunications network provided by SITA is essential to the operations of the air transport community most, if not all, members of which could not provide such a network for themselves. We recognize that it meets the needs of the air transport community arising from the requirements for interlining, sharing limited facilities at airports etc, safety, and to enable interaction between different systems. We accept that the services have been designed for the essential requirements of the air transport community following consultation with SITA's members. We accept that messages sent over the network relate to passenger and freight reservations, baggage handling enquiries, aircraft movements, maintenance and associated administrative matters; and the great majority of these relate to passenger and freight reservations. But those features cannot disguise the fact that SITA really functions as a facilitator. It neither initiates messages nor generates the information transferred nor receives them nor takes any action on receipt. Its function is to process the information fed into the system by its members. It does so accurately and effectively without in any way altering the content of the messages or its information. Shortly stated, it makes no arrangements for any of the supplies referred to in item 10.

46. Do the decided cases lead to a different conclusion?

47. The only decision on this particular item is *BAA v Customs and Excise Commissioners* [1975] VATTR 43. There BAA granted a retailer, in return for monthly payments, the right to sell merchandise in a departure concourse and the right to sell merchandise duty free in an international departure lounge. BAA sought to argue that it was thereby making arrangements for the supply of services for the handling of goods carried on aircraft : see item 6(b) and item 10 of Group 8 to Schedule 8. The tribunal dismissed BAA's appeal, rejecting its argument on this point. Relevant to the present situation, the tribunal (Kenneth Suenson-Taylor QC) observed (on page 49) that the words "the making of arrangements for" -

"... should not be construed widely but restricted to the making of arrangements by an agent or like person for a principal who himself makes, or is the recipient of, a supply falling within the relevant items 1-9".

If that test were applied to SITA and its services, SITA would not be regarded as making arrangements for, for example, the transport of passengers in qualifying aircraft. It supplies the telecommunication network service as principal to its members who use that service to make their own supplies. It is not their agent nor does it function in like manner for its members.

48. The Association, the appellant in the *Civil Service Motoring Association* appeal to the Court of Appeal, *supra*, was a non-profit making body that provided motoring, leisure, financial and related services to its members. It received consideration from a bank in return for its providing a credit card scheme to its members. The Association contended that its supplies to the bank were to be exempt because they consisted of the making of arrangements for the granting of credit. The Commissioners argued that this was neither the negotiation of credit within Article 13B(d)(1) or (2) nor the making arrangements for the granting of credit. The Court of Appeal (at 118g-j) saw the critical question in that case as being whether the expression "negotiation of credit" and "making of arrangements" are to be construed as implicitly restricted to activities in relation to particular transactions for the specific grant of credit. This they answered in the negative in favour of the Association. They observed that -

"Both the 'negotiation of credit' and 'the making of arrangements' for the granting of credit referred to the doing of things antecedent to, and directly leading to, the results sought to be achieved by the doing of those things. The result to be attained is of a general rather than a specific nature, namely the 'granting of any credit'. In some cases intermediaries between principals will be involved in achieving that result. In others they will not. It is neither expressly nor impliedly necessary that they should be involved as a condition of the application of the exemption to those who do not actually grant credit."

That case was concerned with a different provision and the EC counterpart hardly corresponds with Article 15.9. The Court of Appeal concluded that the activities of the association, in respect of which the bank paid commission, could reasonably and sensibly be described as negotiation of, or making arrangements for any transaction for, the granting of credit. What the association was doing by offering its members the facility of a credit card scheme in return for the bank's commission was implementing arrangements which sought to achieve the actual granting of credit. They were introducers. Here by contrast SITA's supplies begin and end with affording access to its telecommunications network. SITA's supplies, as we have already observed, were essential to the running of the business of its members and they were supplies made antecedent to SITA's members' supplies of air transport services. But that is not the same thing as to say that SITA were making arrangements for supplies referred to in Group 8. Unlike the association, SITA does not seek to achieve the supply of the particular services referred to in item 10. That is the objective of the airlines, their agents and intermediaries and other members of the air transport community.

49. *The Barclays Bank plc* decision, *supra*, was concerned with an insurance broker that carried on a direct marketing activity, sending mailshots to selected customers offering insurance services and sending out further advice and information. The broker obtained a commission based on the premiums received. The question for the tribunal was whether the broker was "making arrangements for the provision of any insurance". The tribunal concluded that the broker was making such arrangements : on page 472 at C-E D C Potter QC said:

"Upon reflection it seems to us that the correct interpretation of the words extends the exemption to services, not in themselves

broking, which have a clear connection or nexus with insurance broking activities, are similar to such activities, and are carried on by insurance brokers otherwise than as a distinct and different activity.

In the present circumstances the direct marketing activities must be considered in their context. They meet the statutory test; are not themselves broking, they are performed by insurance brokers; or importantly, they are a sort that can be performed by insurance brokers without losing the overriding character of insurance brokers - they are something that an insurance broker might do. They are not mere publicity. They are services related to insurance transactions in that they are the first step towards the making of arrangements for insurance. We are on balance of the view that the disputed activities qualify for exemption from VAT. We allow the appeal."

Here the nexus that SITA's services has with the service referred to in item 10 is that they facilitate those latter services. But that is not a nexus that can, we think, be properly described as a first step towards the making of arrangements for, for example, "the supply of space in an aircraft" or "the transport of passengers".

50. *Countrywide Insurance Marketing Ltd, supra*, again raised the question whether the services of an insurance intermediary operating its business for its members amounted to the making of arrangements for the provision of any insurance. The Appellant negotiated terms of insurance products with insurers and made them available for sale by its own members. The Tribunal concluded that the Appellant's services were exempt: at page 290A-B, Dr A N Brice concluded:

"On the facts and evidence before us we consider that the activities of the Appellant Company in devising insurance products, in negotiating with insurers, and in making those products available for sale by its members do constitute the "making of arrangements for the provision of any insurance by a permitted insurer" within the meaning of the exemption. The activities of the Appellant Company are a necessary part of the chain of supply whereby the particular policies of insurance are provided by the insurer to the insured. Those activities are not ancillary to the supply ..."

Here the services supplied by SITA were undoubtedly necessary to the business of its member who themselves made supplies of the sorts referred to in item 10. SITA's services are a cost-ingredient of those members' supplies. But they are not part of the chain of supply whereby, e.g. the supply of transport in an aircraft is provided by the airline to the passenger.

51. It follows that the decided cases relied on by SITA do not support its contention that it is making arrangements for the supplies of the categories set out in paragraphs (a)-(c) of item 10.

Article 15.9

52. Article 15.9 exempts the supply of services "to meet the direct needs of aircraft .. and their cargoes". The aircraft in question are limited to those used "by airlines operating for reward chiefly on international routes": see article 15.6.

The exemption includes services supplied "by brokers and other intermediaries where they form part of transactions" within Article 15.9.

53. It is not in dispute that article 15.9 has direct effect. The present dispute revolves round the expression "direct needs". SITA says that this expression covers the operational and logistical requirements of aircraft required for their safe and efficient operation and the management and loading of cargo. SITA's services, it is argued, meet those direct needs by achieving the well-coordinated, efficient, reliable and hence safe operation of aircraft: they include the transfer, management and guaranteed delivery of information regarding passengers and their baggage, air movements, the locality of planes and freights; and all of those features make the service an indispensable pre-requisite to, and an essential part of the actual operation of, aircraft. The Commissioners say that the facts do not support SITA's contention. In the circumstances the telecommunications network services satisfy the needs of the airlines rather than those of the aircraft and their cargoes. The Commissioners concede that SITA's services, or a great majority of them, involve the transmission of messages that have to do with services falling within article 15.9; nonetheless, they say, the provision of the telecommunications network is at least one step removed from the direct needs of the aircraft. Those direct needs can only be met by telecommunications that provide transmissions to a receipt of signals by an aircraft. On that basis the only services of SITA that could rank as exempt are the Aircom services referred to in paragraph 39 above; (these are not in issue here and whether or not they did qualify would depend on an examination of their particular facts). So far as concerns aircraft cargoes these, say the Commissioners, have no "direct needs" of telecommunication services.

54. Before addressing the "direct needs" issue, there are two points to be made. First, Article 15.14 is, as we read it, the provision that widens the net and enables the inclusion in the UK zero-rating Schedule of services that amount to the making of arrangements for the supply of aircraft-related services. The net is nonetheless limited to brokers and intermediaries whose services form part of aircraft-related services. SITA is neither a broker nor an intermediary. It operates as a principal providing the telecommunications network services to its members. Second, we (the tribunal) did advance as a possible construction of Article 15.9 together with paragraph 6 that the exempted services covered all those that met the direct needs, not just of aircraft, but of aircraft that had to earn their keep because they were operated by commercial airlines; on that basis the direct need included passenger booking arrangements and cargo handling facilities. On reflection we doubt if this is a good point. The expression "by airlines operating for reward" imposes a condition that the aircraft have to fulfil; it does not however widen the scope of the exempted services.

55. The only relevant ECJ decision on Article 15 is *Berkholz v Finanzamt Hamburg-Mitte-Altstadt* [1985] 3 CMLR 667. This was the decision on the scope of Article 15.8 which concerns the supply of services to meet the direct needs of sea-going vessels or of their cargoes. In that case the issue was whether the installation of gaming machines on a ship, the purpose of which was to amuse passengers, fell within Article 15.8. The Court held that the installation of such machines was not within Article 15.8 saying (in paragraph 21) -

"... the only services exempted under Article 15.8 are those which are directly connected with the needs of sea-going vessels or their cargoes, that is to say services necessary for the operation of such vessels."

56. We have examined the evidence in the context of the wording of article 15. The essential quality of the services supplied by SITA is, as we have already observed, that of a telecommunications network facility for use by its members. The recipients of the supplies are the airlines, the ticket sales businesses, the baggage handlers, the airports, the spare parts depots and so on. It is their needs that are being met by SITA. The members may or may not use them to meet the direct needs of the aircraft or their cargoes; and if they do use them for those purposes, it is at the members' initiation and not at SITA's. Only at one remove, at the least, are the needs of the aircraft and baggage being met. The connection is too remote for us to be able to say that SITA provides for their "direct" needs. For that reason we are against SITA on the article 15 point.

57. We turn finally to the decision of the ECJ in *Sparekassernes Datacenter (STC) v Skatteministeriet* [1997] STC 932 on which both parties relied. *Sparekassernes* is a case where some banks formed a jointly owned operating centre (Sparekassernes) and "outsourced" some of the services previously provided by them. These services included the provision of advice on and trade in securities and the actual implementation of security transactions as well as the management of deposits, purchase contracts and loans. Sparekassernes performed these transactions entirely by electronic means. They were performed for the banks and Sparekassernes had no legal relations with the banks' customers. A question was whether Sparekassernes' services were "transactions, including negotiation, concerning deposit and current accounts, payments, transfers, debts, cheques and other negotiable instruments ..." within Article 13B(d)(3) or "transactions ... in shares ... debentures and other securities ..." within (d)(5). Relevant to the present question is the conclusion of the Court that it is the nature of the services provided that engages the exemption, not the type of legal persons supplying or receiving them. That is equally applicable to Article 15.9. The court went on, in paragraph 66, to observe that for services to be characterized as exempt under paragraphs (d)(3) and (d)(5) they must "viewed broadly, form a distinct whole fulfilling in effect the specific essential functions of a service described in those two points". Thus "for a 'transaction ... concerning ... transfers' the services provided must ... have the effect of transferring funds and entail changes in the legal and financial situation". Taking that approach with Article 15.9, one has to ask whether the services supplied by SITA, e.g. the provision of the service of electronic transmission of a message from a member, form a distinct whole fulfilling the essential functions of meeting the direct needs of aircraft or their cargoes. The answer, we think, is bound to be "no" whatever the direct needs that are sought to be met. SITA's transmission services, essential though they are, are merely the means by which the airline meets the direct needs of its aircraft. The message which may cater for those direct needs is not SITA's message, and anyway SITA will probably be unaware of it. Borrowing the words of the Court, SITA's services do not effect the "specific essential functions of the services described in" Article 15.9. SITA's services do not meet the direct needs of aircrafts or their cargoes. As already explained, our view is that SITA's service facilitate the provision of services by its members who in their turn may use them to provide for the direct needs of aircraft and their cargoes.

PART II

Estoppel

58. SITA contends that the matter is covered by "issue estoppel". The issue of the zero-rating of telecommunication services supplied to those of its members who are airlines was, it was argued, determined by the 1973 Decision. The question before this tribunal is the same and there has been no material change between

1973 and now. Such changes as there have been to the technical nature of the network are not material for these purposes. Such changes as there have been to the statutory wording are, it is argued, immaterial. The Commissioners say that there is no estoppel here, indeed there is no public interest for having an estoppel. Even if there were, the 1973 Decision should not create an estoppel. This is because, say the Commissioners, the services and the law have changed since then. Moreover, the issue in the 1973 Decision covered services in 1972/73 and that was the limit of the tribunal's jurisdiction as regards those services.

Facts relevant to the estoppel issue

59. The following are taken directly from the witness statement of Jean Roworth.

60. On the introduction of VAT in the UK in 1972, SITA wrote to the Commissioners asking for their early advice concerning the VAT liability of its services. Discussions with the Commissioners ensued. A letter of 21 December 1972 enclosed a formal registration form (VAT 1) applying for zero-rating on the grounds that SITA formed "an integral part of the air transport industry in operating on a cost-sharing basis the communications which the member airlines would otherwise operate on their own behalf." The letter went on to describe SITA communications service as "a worldwide system of message switching centres linked by a network of private circuits leased from the telecommunications administrations of the countries concerned." A meeting was held on 8 February 1973 following which the Commissioners wrote to SITA stating that as the Post Office had agreed to charge VAT on supplies within the UK - "... the activities of SITA relating to the provision of telecommunications facilities within the UK is therefore taxable at the standard rate, and you should account for output tax on those services."

61. SITA disputed this treatment in letters of March and April 1973. It appears that SITA made or was treated as having made an appeal against the Commissioners' decision. The Commissioners appeared to have agreed to allow the appeal and, in accordance with rule 15 (appeal or application allowed by consent) of the VAT Tribunal Rules, 1972/1344, submitted agreed terms to the Tribunal for the determination of the appeal.

62. On 6 July 1973 the VAT Tribunal (Neil Elles) determined the appeal in accordance with the parties' agreed terms and the decision reads as follows:

"That for the purposes of the Value Added Tax the telecommunications services of SITA as described in detail in correspondence between SITA and the Commissioners of Customs and Excise during the period from 26 October 1972 and 10 April 1973 and in the "Constitution-Articles of Association" of SITA fall within the zero-rating provision of item 10 of Group 10 of Schedule 4 to the Finance Act 1972".

63. The correspondence apparently referred to the tribunal describes the telecommunications services covered by the Commissioners' ruling as communications necessary for the efficient and economical transmission of airline members' messages relating to passenger and freight reservations, baggage handling, lost property enquiries, aircraft handling, maintenance and associated administrative matters.

64. As appears from paragraphs 18-22 above, changes to the service provided by SITA and to the technology of the network have taken place since 1973. For

example, the Data Transport Network provides improved performance and facilities through its Network Control System. The Mega Transport Network has given members more flexibility in their use of protocols and it has improved response times, capacity and reliability.

65. The recipients of the supplies have changed since 1973. Originally only a company operating aircraft for transport of passengers, mail or cargo was entitled to become a member of SITA. However, in 1989 the category of persons eligible for membership was extended to include (in addition to those already mentioned), other organizations whose primary business is within the air transport industry. The wording of the revised articles of association set out the criterion for qualification for membership as -

"Any company operating aircraft for the transport of passengers, mail or cargo, or any organization whose primary business is related to the air transport industry ..."

This change, Jean Roworth explained, was largely made in response to changes in the air transport industry itself. Competition law throughout the European community and the USA required airlines and their passenger reservation companies to operate separately. The reservation companies still needed to have access to the SITA network and therefore to become members.

66. Another change has been in the computerization of functions of the air transport industry. Communications technology now plays a prime function in the building of an aircraft to the requirements of an airline. In the early 1990s SITA established an "Aero Net" internet community network service, enabling all participants in the design and building of an aircraft to be connected. Other changes were made to enable different types of participants in the air transport community to become SITA members. After 1989, airports, ground handling organizations, certain travel companies and courier companies have become SITA members.

Conclusion on estoppel issue

67. The principle of "res judicata estoppel" is stated in Chapter 1 of Spencer Bower, Turner and Handley's edition of "The Doctrine of Res Judicata", third edition, 1996. Paragraph 9 states as follows:

"It may thus be stated: Where a final judicial decision has been pronounced on the merits by an English or (with certain exceptions) a foreign judicial tribunal with jurisdiction over the parties in the subject matter, any party to such litigation, as against any other party (and in the case of a decision in *rem*, any person whatsoever, as against any other person) is estopped in any subsequent litigation from disputing such decision on the merits, whether it be used as the foundation of an action, or as a bar to any claim, indictment, affirmative defence or allegation, provided the party entitled raises the point at the proper time."

For present purposes there are two forms of estoppel, "cause of action estoppel" and "issue estoppel". The cause of action leading to the 1973 Decision was the tax status of SITA's supplies between 26 October 1972 and 10 April 1973. That has no application because here we are concerned with the tax status of SITA's supplies in 1997. Issue estoppel is relied upon by SITA. This may operate where the decision relied upon did not determine the cause of action litigated in later

proceedings; in that situation it may be invoked as determining, as an essential step in its reasoning, some issue in those later proceedings. Diplock LJ defined it in *Thoday v Thoday* [1964] P 181 at 198:

"... 'issue estoppel' is an extension of the same rule of public policy. There are many causes of action which can only be established by proving that two or more different conditions are fulfilled. Such causes of action involve as many separate issues between the parties as there are conditions to be fulfilled by the plaintiff in order to establish his causes of action; and there may be cases where the fulfilment of an identical condition is a requirement common to two or more causes of action. If in litigation upon one such cause of action any of such separate issues as to whether a particular condition has been fulfilled is determined by a court of competent jurisdiction, either on evidence or on admission by a party to the litigation, neither party can, in subsequent litigation between one another upon any cause of action which depends upon the fulfilment of the identical condition, assert that the condition was fulfilled if the court has in the first litigation determined that it was not, or denied that it was fulfilled if the court in the first litigation determined that it was".

68. Here we are concerned with the application of a taxing provision (Schedule 8 item 10) to the facts as they existed in 1997. The question is whether the Commissioners have been correct in their decision that for 1997 onwards SITA's supplies of its telecommunications network services to its 800 or so members are standard-rated as being outside the scope of item 10. The public policy behind the general application of issue estoppel is to ensure the finality of litigation. In taxation and rating cases, however, that aspect of public policy has been overridden by a different element of public policy. Recurring business transactions, which fall to be assessed period by period, as is the case of supplies of a VAT registered trader, are involved here. Administrative flexibility is needed to enable the even-handed management of the revenue. To impose on a trader the unalterable privilege or disadvantage of a particular tax treatment of his supplies as the result of a decision of a tribunal or court might lead to inequity as between him and other traders making similar supplies the liability of which had been determined at a later date. The principle of public policy that applies in that situation, and in particular through the taxation of business transactions, is that of ensuring that the tax operates uniformly. We refer to the decision of the US Supreme Court in *US v Stone & Downer Co* 274 US 224 and to paragraph 303 of *Spencer Bower* (page 161).

69. Here SITA and its services are unique. Nonetheless there can, we think, be no real public policy in securing finality in litigation on the strength of a decision reached with the consent of both parties some 30 years ago. Moreover, to regard the 1973 Decision as ensuring zero-rating in perpetuity for SITA while the supply of other telecommunications outlets are either exempt or standard rated could lead to inequality of treatment. This is all the more so when it is recalled that the 1973 Decision was a tribunal decision produced without pleading, without argument, and without any reasoning.

70. A different, but related, feature of VAT cases is that the jurisdiction of this tribunal is limited to determining the taxability of past supplies. See *Odhams Leisure v Customs and Excise Commissioners* [1992] STC 332. That is the effect of section 83(b) of VAT Act 1994 which limits the tribunal's jurisdiction to "the tax

chargeable on the supply of any goods or services". That provision reflects the rule that issue estoppel has no place in a VAT litigation of this nature.

71. But supposing we were wrong and issue estoppel were available to SITA and the 1973 Decision were relied upon; would it actually establish an estoppel? Here it will be recalled that Diplock LJ in *Thoday v Thoday*, in the passage quoted above, stressed that both causes of action should depend on identical conditions if an estoppel is to be established. A more relaxed approach was adopted by the Employment Appeal Tribunal in *McLoughlin v Gordons (Stockport) Ltd* [1978] ICR 561. There a woman's claim for equality of pay with a male colleague had been dismissed by an industrial tribunal. The woman made a second claim for equality of pay with the same colleague. She argued that issue estoppel did not apply to the second claim. The Tribunal (chaired by Kilner Brown J) decided against her. While the doctrine of issue estoppel did not apply in circumstances where there was a change in situation, a mere potential for change was not sufficient to exclude it. Thus, the Tribunal concluded (on page 564) that unless it could be shown that there was an appreciable difference in the facts at the time of the second hearing, issue estoppel applied to a claim for equal pay and the industrial tribunal had correctly held that they had no jurisdiction.

72. One significant change since 1973 is the alteration to the articles of SITA that has enabled it to admit to membership members of the air transport community who are not airlines. If the issue relied upon as determined by the 1973 Decision is that SITA makes arrangements for the supply of transport services, the nature of the arrangements will have significantly changed since 1973. Its supplies to the new class of non-airline members will be arrangements of the different nature to those made in relation to its airline members of 1973. Another change since 1973 is the technological change in the nature of SITA's supplies. These are summarized in paragraph 12-27 above. Those two features may on examination amount to appreciable differences that, on the *McLoughlin v Gordons* reasoning, exclude the operation of issue estoppel. They certainly, and without examination, demonstrate that the issue behind the 1973 Decision was not based on identical conditions as that now in detention.

73. Another factor is that the law has changed. There have been some minor changes in the domestic legislation. These are not of themselves material. But in 1973 there was no Sixth Directive and nothing of comparable effect. Would Mr Elles, the 1973 Tribunal, have construed the expression "making arrangements for" differently had he had the 1997 facts and the text of the Sixth Directive before him and known the implications of the *Marleasing* decision of the European Court of Justice? There is quite sufficient doubt about this to exclude the operation of issue estoppel in relation to the 1973 Decision.

74. For all those reasons we would not, were we free to do so, regard the 1973 Decision as creating an issue estoppel that precluded us from dealing with the present appeal on its merits.

PART III

75. For the reasons given above we dismiss the appeal.

76. We were not asked to make an award of costs. We leave it to the parties to agree the amount of the Commissioners' costs. If this cannot be agreed, the matter should be referred back to this tribunal.

STEPHEN OLIVER QC

CHAIRMAN

RELEASED:

LON/00/1142

© Crown copyright 2005. All rights reserved