Food tax
Making a meal of it?

Why certain foods are taxed, and how to negotiate the apparently arbitrary distinctions between zero-rated and standard-rated food.

by Dr Michael Taylor

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Key Points

What is the issue?
The UK's VAT legislation – and the attendant case law – contains any number of peculiar and apparently arbitrary distinctions between zero-rated food and standard-rated food.

What does it mean for me?
'Food of a kind used for human consumption' – within the meaning of the VAT Act – has never been explicitly defined. Rather, the UK courts have tended to use the perception of 'the ordinary man' as to what constitutes food.

What can I take away?
Deciding which rate of VAT should be applied to food products is a persistent problem for businesses, their advisors, HMRC and the courts. The existing legislation is complex and occasionally irrational.

If the man on the Clapham omnibus knows anything about VAT, he probably knows that Jaffa Cakes are zero-rated but that chocolate biscuits are standard-rated as confectionery. If he knows anything else about VAT, he probably knows that the UK's VAT legislation – and the attendant case law – contains any number of peculiar and apparently arbitrary distinctions between zero-rated food and standard-rated food.

The decision of the Upper Tribunal in *Nestle UK* [2018] UKUT 29 (TCC), for instance, has confirmed that banana and strawberry flavoured Nesquik drinks are standard rated, but that chocolate flavoured Nesquik is zero rated because it contains cocoa, or at least a 'preparation or extract thereof'. Fancy a bottle of water? You'll pay VAT on that, but not if you buy a pint of milk instead. At the same time, a packet of salted nuts attracts VAT at 20% but there is no VAT on a packet of nuts which are still in their shells.

So what lies behind the seemingly bizarre legal framework for taxing food?

The origins of VAT food legislation

Upon joining the European Community in 1973, the United Kingdom was obliged to impose VAT in accordance with the terms of the Second VAT Directive of 1967. However, this Directive provided only a skeletal outline of the VAT system, leaving many things up to the member states themselves. The UK therefore enacted VAT by way of the Finance Act 1972, within which Section 12 and Group 1 Schedule 4 provided for the zero rating of food.

When the Sixth VAT Directive was enacted in 1977, thereby creating the first harmonised VAT system, nothing provided explicitly for zero rating. However, member states were allowed to maintain their zero ratings as 'stand-still provisions'; hence food to this day being zero rated by way of the Value Added Tax Act 1994 Sch 8 Group 1.

In terms of 'general items', 'excepted items' and 'items overriding the exceptions', the provisions of VATA 1994 Sch 8 Group 1 are practically identical to the provisions first enacted in Finance Act 1972. The application of zero rating to food products today therefore derives almost entirely from the rationale behind the original 1972 provisions. So what were the reasons for zero rating some food products but not others?

The answer lies in the old purchase tax regime, introduced as a wartime measure in 1940. At the time, the government vowed that there would be 'no purchase tax on food, drink or foodstuffs' in order to 'secure the price of certain essential foodstuffs'.

In 1963, however, the Purchase Tax Act listed 35 groups of items on which the tax would be charged. Once again, the food groups are practically identical to the 'excepted items' in today's VAT Act: ice cream, manufactured beverages (but not milk, tea, coffee or cocoa) and confectionery (but not drained cherries or candied peels); a later measure added potato snacks and salted or roasted nuts (except those in their shells).

The rationale for taxing these items but not others was laid before Parliament in the Budget Statement of 1962. Selwyn Lloyd, the Chancellor of the Exchequer, told the House of Commons that the tax on sweets 'will be welcomed by the medical professions, or ought to be'; in the same breath, he praised the beneficial health effects of 'games, physical, exercise and club facilities'.

The rationale for the tax was clear: it was to deter expenditure on items of food considered harmful to people's health. Yet if this is the underlying purpose of the tax, is there a universal definition of 'food' too?

Defining 'food'

The UK courts have been considering the meaning of 'food' for more than a hundred years. In 1918, in *Hinde v Allmond* (1918) 118 LT 447 at 448, a case which concerned illegal hoarding during the First World War, Avory J held that 'the word "food" must be interpreted in its primary sense – namely, something taken into the system for nourishment and not merely as a stimulant'.

Name: Dr Michael Taylor
Position: Manager, Indirect Tax Disputes
Employer: PwC
Tel: +44 7483 334197
Email: michael.y.taylor@pwc.com

Profile: Michael specialises in technical research in relation to indirect tax litigation. His recent work has focused on the operation of the repayment mechanisms in VATA ss 80 and 81; the concepts of non-business and non-economic activities; the insurance, financial services, education and medical care exemptions; deemed supplies of goods; the zero-rating of food and medical drugs; and landfill tax and the climate change levy.

It remains the case, however, that 'food of a kind used for human consumption' – within the meaning of the VAT Act – has never been explicitly defined. The UK courts have tended to use the perception of 'the ordinary man' as to what constitutes food, a test first articulated by the VAT Tribunal in *Marfleet Refining Company* [1974] V129, a case concerning cod liver oil. But is the 'ordinary man' test still fit for purpose?

In his judgment in *Procter & Gamble* [2009] EWCA Civ 407, Toulson LJ recognised that the 'ordinary man' test was likely defective. 'I rather regret the introduction of the ordinary man in the street into this area,' he held, 'because I do not regard it as necessary and it has led on to a distracting argument about what knowledge should be attributed to that hypothetical person'. Is it time, therefore, to bin this test for good? If so, what could taxpayers, advisers and the courts use as a replacement?

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One possibility is the judgment of the CJEU in the case of *X* (Case C-331/19), which considered whether aphrodisiacs could be regarded as food for VAT purposes. Although in a post-Brexit world the Principal VAT Directive is no longer supreme in post-2020 accounting periods, and though it is a vexed issue whether the terms in the Principal VAT Directive Annex III can be applied across the VAT system, the CJEU in this case arrived at two workable definitions.

First, the court concluded that 'foodstuffs for human consumption' should be defined as 'products which contain nutrients and which are consumed principally in order to provide the human body with those nutrients'. Second, the court considered that food supplements should be defined as 'products which are not foodstuffs but which contain nutrients and are consumed in place of foodstuffs in order to provide the body with those nutrients, and also products consumed with a view to enhancing the nutritional functions of foodstuffs or their substitutes'.

These definitions might be unwieldy, but would their implementation through revised VAT legislation bring greater clarity to the law? Would they better serve the policy goals identified by the UK government in the 1960s and 1970s? Would this not be a prime case for applying the principle of statutory construction known as 'always speaking', so that the meaning of 'food' could change in law as its meaning changes in reality?

Fixing the system

Deciding which rate of VAT should be applied to food products is a persistent problem for businesses, their advisors, HMRC and the courts. The existing legislation is complex and occasionally irrational: why, for instance, should protein drinks be excluded from zero rating when they: (i) satisfy the legislative purpose of delivering nutrition to consumers; and (ii) are derived from milk, which is zero rated?

Moreover, the existing tests available to courts can often bring confusion rather than clarity. The perception of 'the ordinary man' is surely subjective because the opinion of one person on the Clapham omnibus could easily differ from the person sitting next to them. The test of how a food product is 'held out for sale', most recently applied by an appellate court in *The Core (Swindon)* [2020] UKUT 301 (TCC), is surely subjective too: isn't such a thing in the eye of the beholder? An objective alternative is perhaps to assess whether a product is *regulated* as food, and apply the tax treatment accordingly.

Now that the United Kingdom has left the European Union, Parliament and the government – by way of statutory instruments – have the power to expand the scope of zero ratings that, until 2020, had been frozen as stand-still provisions. It would seem an opportune time for a fresh look at how VAT is applied in this area, with an objective of reforming the rules into a more sensible, principled regime fit for the modern world and one which provides increased clarity for all participants.