Tribunal ref: UT/2014/0013

[2016] UKUT 19 (TCC)

VALUE ADDED TAX — zero rating — construction of building for educational use — VATA Sch 8, Group 5 Item 2(a), Note (6) — whether building used in course or furtherance of business — supplies of education to students paying less than cost of provision of course —* Commission v Finland *considered — supplies made in course or furtherance of business — appeal allowed

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS — **Appellants**

- and -

WAKEFIELD COLLEGE — **Respondent**

Tribunal: The Honourable Mr Justice Barling
Judge Colin Bishopp

Sitting in public in London on 27 and 28 July 2015

James Puzey, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the appellants

Kevin Prosser QC, instructed by Deloitte LLP, for the respondent

CROWN COPYRIGHT © 2016

DECISION

Introduction

1. This is an appeal by the Commissioners for Her Majesty's Revenue and Customs ("HMRC") against a decision of the First-tier Tribunal ("the FTT") (Judge Barlow), released on 6 December 2013. The appeal represents the latest stage of a lengthy dispute between HMRC and Wakefield College ("the College") about the supply to the College of construction services relating to a new building for the College, known as the SkillsXchange ("the Building"), at Glasshoughton. The College maintains that the supply should be zero-rated for VAT purposes, but by a ruling communicated by a letter dated as long ago as 23 May 2007 HMRC refused to authorise the issue by the College to the builders of a zero-rating certificate. It is that refusal which is the subject of this appeal.

2. Group 5 of Sch 8 to the Value Added Tax Act 1994 provides for the zero-rating of various supplies made in the course of construction of certain buildings. The part of that Group relevant here is Item 2:

> "The supply in the course of construction of—
>
> (a) a building … intended for use solely for … a relevant charitable purpose …
>
> of any services related to the construction other than the services of an architect, surveyor or any person acting as a consultant or in a supervisory capacity."

3. That provision has to be read together with Note (6) to Group 5:

> "Use for a relevant charitable purpose means use by a charity … —
>
> (a) otherwise than in the course or furtherance of a business …".

4. It is common ground that the College is a charity, and that the use it intended to make of the Building following its construction (and has made of it since it opened in 2009), namely the provision of further and higher education, is capable of amounting to a relevant charitable purpose. HMRC's position, however, and the reason why they consider that the construction cannot be treated as zero-rated, is that some of the College's relevant supplies of further and higher education have been made in the course or furtherance of a business. If that is right, the use made of the Building has not been solely for a relevant charitable purpose, as Item 2(a) requires.

5. The 1994 Act contains no definition of "business", and it is necessary instead to turn for guidance to the Principal VAT Directive (2006/112/EC). The parties agree that the relevant provision is art 2(1)(c), which provides that

> "The following transactions shall be subject to VAT: …
>
> (c) the supply of services for consideration within the territory of a Member State by a taxable person acting as such."

6. A "taxable person" is defined by art 9 as

> "any person who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity."

7. It is also common ground that the College is a taxable person within the meaning of that definition. The question which divides the parties is whether the fees paid by certain students to the College in return for supplies of education made from the Building amount to consideration, so as to bring those supplies within art 2(1)(c).

The history of the appeal

8. The College appealed against HMRC's May 2007 ruling to the FTT, at that time arguing that none of the supplies made from the Building were made in the course of business and, moreover, that it was acting as a public body and was not taxable at all. The essence of the former argument at that stage was that, as those of the College's supplies which might otherwise be regarded as business supplies were entirely dependent and parasitic upon its core activity of making what were agreed to be non-business supplies, they could not amount to a separate activity; taken alone, they would be wholly uneconomic. In its decision released on 20 January 2011 ("FTT(1)") the FTT dismissed the College's appeal, holding that it was not a body governed by public law, and that the use of the Building "was not restricted to use for non-business purposes".

9. The College appealed to the Upper Tribunal (Arnold J). It did not pursue the argument that it was a body governed by public law, and it now accepted that some of its supplies were made in the course of business. It argued instead that the extent of the business use made of the building was of such a limited scale that it should be regarded as *de minimis*, and ignored. Arnold J recorded that, by virtue of an extra-statutory concession, ESC 3.29, and a Business Brief issued on 1 July 2009, HMRC accepted that the word "solely", as used in Item 2(a), could accommodate a *de minimis* margin of up to 5% business use. The accepted margin had been mentioned to the FTT, but it had been led to believe that, because it was dependent on an extra-statutory concession, it had no jurisdiction to take it into account. However, by the time the appeal reached Arnold J the parties agreed that the effect of the Business Brief did bring it within the FTT's power to determine whether or not the extent of the business use of the Building came within the 5% margin.

10. In a decision released on 20 December 2011 Arnold J allowed the appeal. He accepted at [15] that, through no fault of its own, the FTT "had wrongly proceeded on the basis that Wakefield's appeal should be dismissed if the Building was put to any business use at all, however small, whereas the Tribunal should have gone on to decide whether in the light of its subsequent findings the extent of the business use was *de minimis* or not". He accepted also that the FTT had not reached a conclusion on one important question, that is whether the supplies made by the College to certain of its students were supplies made in the course of business, and rather than decide the point himself he remitted the appeal to the FTT in order that it could reconsider those two issues.

11. When the case returned to the FTT in March 2013 the College did not seek a determination of the *de minimis* point, on the basis that if the second remitted issue was determined by the FTT the parties would themselves be able to resolve the question whether any business use of the building was or was not *de minimis.* In its decision of 6 December 2013 ("FTT(2)") the FTT found in the College's

favour on that second issue, holding that the provision of education to the relevant students was not a supply "in the course or furtherance of a business" because the link between the tuition fees paid by the students and the courses they received was insufficiently direct for the former to amount to consideration for the latter. On 20 February 2014 the FTT granted HMRC permission to appeal to this Tribunal against that conclusion, accepting without elaboration that the grounds of appeal advanced raised arguable points of law.

12. We were told by Mr James Puzey, who appeared before us on behalf of HMRC, that FTT(2) has been relied upon by other taxpayers seeking to argue that the provision of services by publicly funded bodies for a charge that amounts to less than the cost of providing the service is not a supply in the course of business, and that there are nearly 50 cases (involving VAT of about £121 million) awaiting the Tribunal's decision in this appeal. He added that the issues here also potentially affect sectors beyond that of further and higher education.

Factual background

13. Although by the time this appeal reached us most of the relevant facts were no longer in dispute the parties were not wholly agreed on some matters, and on what the FTT decided about them. We take the following from its two decisions and from the decision of Arnold J, but will need to add some comments about those points on which the parties disagree, or at least disagree about the FTT's findings.

14. The College provides a substantial range of courses, some of an academic but most of a vocational character. The Building is only one of several which together make up its campus. Altogether the College has about 10,000 students, some full-time and others part-time. At the material time the College's primary source of income was the grant funding it received from the Learning and Skills Council ("the LSC") or the Higher Education Funding Council for England ("the HEFCE"). The LSC is responsible for further—essentially vocational—education, and the HEFCE for higher, equivalent to university, education. We are concerned in this appeal only with further education. The grant income is supplemented by fees charged to students or their employers, by contributions from other public sources, such as local authorities, and by some miscellaneous income. The public funding the College received represented, it seems, about 81% of its total income.

15. The grant funding rules within which the College operates and its own fee structure are rather complicated but the features relevant to this decision can we think, be fairly shortly summarised. As we explain below, the majority of the College's further education students were wholly grant-funded and paid no tuition fees at all; the cost of their education was met from a block grant from the LSC. Others were only partially funded by the block grant, and they or their employers were required to pay some fees, although the amount payable might be wholly or partially remitted in certain circumstances. The amount of the grant the College received for each course which attracted only partial grant support was determined by way of a formula which assumed a base cost for the provision of the course (a cost which varied depending on the nature of the course and which was determined by the LSC) and that the student or his or her employer would pay a percentage of the base cost so determined. That percentage was assumed to be

37.5% in 2007-08, rising incrementally to 50% in 2010-11. A further group of students, mainly but not exclusively those from overseas, attracted no grant support at all and were required to pay fees which were not eligible for remission.

16. The College was not formally required to limit the fees charged to partially grant-funded students to the amount which the formula assumed would be received and could, if it wished, charge more. However, as FTT(1) mentioned at [22], the LSC did not expect colleges to charge more than the assumed fee to students whose courses were partially grant-funded because it was anxious to ensure that there was no adverse impact on the supply of suitable affordable education and, in practice, the College was obliged by reason of the perceived difficulty in payment some of its potential students would encounter—Wakefield, we were told, is in a deprived area—to charge rather less than the assumed fees. The amount it charged to these students or their employers was set by the College alone, without consultation with other colleges in the area or the LSC, and it was possible that other colleges, even those nearby, might offer the same course for a different tuition fee. The fee payable for each course was set out in an annual prospectus published by the College. It was, no doubt, because of the constraints on what it could charge that the fees the College received made up no more than 6 or 7% of its total income.

17. Arnold J said at [5] that the College's students all fall into one of three primary groups. The first group comprises those who pay no tuition fees but are wholly supported by grant funding; they are aged between 16 and 19 and pay nothing for their education for that reason. Arnold J recorded that they represent about 73% of the College's total student population. The second comprises about 11% of the student population; as he put it they are those "who qualify for a reduced grant … These students or their employers are expected to pay a proportion of the fees for their courses." The third group consists of those who qualify for no grant support at all and pay the full fee charged by the College. Those fees are set at a level which the College judges the students or their employers will be prepared to pay, generally above the cost of provision in order to make up some of the shortfall in the College's income from grants and the fees paid by the other students. We should add that there were some students who did not fit into one of those three groups but there were so few of them that the parties agreed they should be disregarded.

18. It has always been accepted by HMRC that supplies to the first of Arnold J's three groups are outside the scope of VAT and, therefore, that no supplies in the course of business are made by the College to those students. Despite its initial argument to the contrary, the College accepted before Arnold J, and accepts now, that its supplies to the third group of students are made in the course of business, although Mr Kevin Prosser QC, representing the College before us, pointed out that the concession was immaterial for present purposes because at the relevant time all of these students were taught elsewhere on the campus. The College accepts that it makes some further, relatively minor, business supplies (of catering and of hairdressing, as part of hairdressing students' training) which make up or contribute to the miscellaneous income we have mentioned, but we are not concerned with those supplies in this appeal.

19. The disagreement between the parties focuses on the second group of students, as they were identified by Arnold J. Between [18] and [23] FTT(2) embarked on a more elaborate taxonomy of the groups, based on five categories. Of these, category 1 can be ignored for present purposes, and category 2 coincides with Arnold J's first group. Categories 3, 4 and 5 subdivide the second group; category 3 is further subdivided, at [21], into six sub-categories. FTT(2)'s categories did not extend to the third of Arnold J's groups, but that group is now immaterial to the appeal. The six sub-categories at [21] ("the para [21] students") have in common that, for one reason or another, they qualify for partial or, more commonly, total remission of tuition fees—in other words, they did not pay the subsidised fee determined by the College in the manner described at para 16 above, but rather less. The reason why they were entitled to remission related to their personal circumstances, for example that they were in receipt of certain state benefits or had already achieved a particular educational level. A few who did not meet those conditions but were on low incomes benefitted from a separate, discretionary, remission scheme administered by the College itself, and paid a flat fee of, we understand, £150; they made up FTT(2)'s category 4 and were described at [22]. By this process of elimination FTT(2)'s category 5 captured a residual class of students, described at [23] as "students over 19 who are not otherwise entitled to remission of tuition fees [and] who are not overseas students" ("the para [23] students"): these students, or their employers, were required to pay the tuition fee specified in the prospectus.

20. HMRC say that this more elaborate approach led the FTT into confusion since it did not, as it should have done, focus only on the para [23] students, but instead treated them as similar to, and therefore to be considered together with, the category 3 and 4 (or paras [21] and [22]) students. The parties also disagree about the meaning and significance of the additional statement, also within [23], that the para [23] students "pay £896 per annum for BTEC courses, which is a reduced fee compared with what overseas students pay" (BTEC is the Business and Technology Enterprise Council) and the observation, at [24], that:

> "None of the relevant students pays a fee that is enough to amount to a full payment of the cost of putting on the courses in question and the College is dependent upon grants to cover its costs."

The reasoning in FTT(2)

21. After setting out the relevant facts as he saw them the judge went on to compare the College's position with that described in *Commission of the European Communities v Finland* (Case C-246/08) [2009] ECR I-10605 ("*Finland*"), in which the question was whether Finland could legitimately treat as non-taxable (that is, outside the scope of VAT) supplies of legal aid provided by the public legal aid office while taxing similar supplies made by lawyers in private practice. The amount a recipient of legal aid was required to contribute to the cost of the legal aid with which he was provided was dependent upon his income and capital: some were required to pay nothing, some were disqualified because their income or capital, or both, exceeded certain thresholds, and others in between paid an amount up to 75% of the cost of the service. In most cases the public legal aid office, acting by its employed lawyers, provided the relevant service but it was possible for a recipient of legal aid instead to engage a lawyer in

private practice. In the former case the contributions supplemented the office's income, most of which was derived from public funds. In the latter, the State paid for the lawyer's services, which were subject to VAT. It made no difference to the recipient's contribution if he instructed a private lawyer rather than the public office. The court's conclusion was that the public office did not engage in an economic activity. The reasoning was as follows:

> "[47] … it is established that the payment concerned is only a part payment since it does not cover the whole amount of the fees set by the national legislation, by reference to the nature of the dispute, in respect of remuneration for legal aid services provided by public offices and private advisers. Indeed … the payment consisting in the basic contribution is a percentage, ranging from 20% to 75%, of that amount. Admittedly, that payment may, depending on the recipient's assets, be supplemented by an additional contribution. Nevertheless, the Commission does not maintain – and … it is unlikely, in view of the income ceilings fixed by the national legislation for the grant of legal aid, – that the additional contribution could result in the recipient making a payment corresponding to the full amount of the fees set by the legislation concerned for the supply of legal aid services.
>
> [48] Although this part payment represents a portion of the fees, its amount is not calculated solely on the basis of those fees, but also depends upon the recipient's income and assets. Thus, it is the level of the latter – and not, for example, the number of hours worked by the public offices or the complexity of the case concerned – which determines the portion of the fees for which the recipient remains responsible.
>
> [49] It follows that the part payment made to the public offices by recipients of legal aid services depends only in part on the actual value of the services provided – the more modest the recipient's income and assets, the less strong the link with that value will be.
>
> [50] … that finding is borne out by the fact that, according to the data provided by the Finnish Government in the present proceedings, the part payments made in 2007 by recipients of legal aid services provided by the public offices (which relate to only one third of all the services provided by public offices) amounted to EUR 1.9 million, whilst the gross operating costs of those offices were EUR 24.5 million. Even if those data also include legal aid services provided other than in court proceedings, such a difference suggests that the part payment borne by recipients must be regarded more as a fee, receipt of which does not, per se, mean that a given activity is economic in nature, than as consideration in the strict sense.
>
> [51] Therefore, in light of the foregoing, it does not appear that the link between the legal aid services provided by public offices and the payment to be made by the recipients is sufficiently direct for that payment to be regarded as consideration for those services and, accordingly, for those services to be regarded as economic activities for the purposes of Article 2(1) and Article 4(1) and (2) of the Sixth Directive."

22. At [27] FTT(2) mentioned the two principles which the court had in mind: that it was necessary for a legal relationship to subsist between the supplier and the recipient requiring the reciprocal obligations of, respectively, supply and payment; and that there must be a direct link between the service provided and the consideration paid. At [29] the judge summarised the three factors which the court

had taken into account: that the contribution represented only part payment; that it was set in part by reference to the recipient's means; and that the aggregate of the contributions represented only a small proportion of the operating costs of the public offices. At [30] to [32] he set out his conclusions:

> "[30] In this case the College does not set a scale of fees against which the part-payment can be compared in the way the Finnish Government had set a scale of fees payable from which the part-payments could be calculated.
>
> [31] I hold that the varying factors such as age, previous academic achievements, receipt of benefits, low income and personal factors … are factors that are analogous to the income levels in the *Finland* case in their effect on the directness of any postulated link between the fees payable and the services provided. The effect of the variations in income levels was sufficient to make the link between the payments and the services 'insufficiently direct' in the *Finland* case. In this case the variations between what students pay is affected by factors other than income levels in most cases but they are factors applicable to individual students and with varying consequences so far as the amount of payment is concerned. I hold that those variable factors are closely analogous to the income levels in the *Finland* case and have the same effect namely that the part-payments are not 'sufficiently direct' to amount to consideration in the relevant sense and so the supplies of services to the students who make part-payment are not to be included in any calculation of the level of business use.
>
> [32] The overall contribution the students make to the cost of running the College is also small and so the [third of the factors taken into account by the court in the *Finland* case] also applies."

23. Thus, although he did not expressly say so, he determined the second of the two remitted issues in the College's favour.

24. HMRC appeal to this tribunal on the grounds that the judge was wrong in treating the students described at [23] of FTT(2) as if they were in a similar position to the recipients of legal aid in *Finland* and in concluding, in consequence, that they were not receiving a supply in the course of a business pursued by the College. We were invited by both parties to re-make the decision, should we allow the appeal in whole or part, rather than remit it again.

The parties' submissions

25. Mr Puzey's first argument was that the judge failed, in FTT(2), to provide a properly reasoned decision. That was a failing criticised by the Court of Appeal in the well-known case of *English v Emery Reimbold & Strick Ltd* [2002] 1 WLR 2409, where the court made the point, at [19], that "… if the appellate process is to work satisfactorily, the judgment must enable the appellate court to understand why the Judge reached his decision." At [25] the court went on to suggest that, on receipt of an application for permission to appeal on the ground of inadequate reasons, the judge should consider whether the reasons he has given are sufficient and, if not, he should remedy the defect. HMRC had invited the judge to adopt that course, but he had instead simply granted permission to appeal.

26. The particular error of this kind of which Mr Puzey complained is that the decision contains only brief and inadequate reasoning—paragraphs [31] and [32], set out above—and says nothing at all about HMRC's case or of the evidence

which the FTT had read and heard. In substance, he said, the judge had summarised the College's skeleton argument and taken account of the judgment of the Court of Justice in *Finland*, without any reference to, let alone analysis of, HMRC's argument that the case could and should be distinguished, and had failed to deal with their submissions about the evidence and other relevant authorities.

27. Mr Prosser accepted that FTT(2) was not entirely adequate, and that it contained little of HMRC's case before the FTT. However, he said, it also did not do full justice to the College's case, and he produced a summary of relevant facts designed to make up for what he recognised to be shortcomings in the FTT's recitation of them. Nevertheless, he said, these failings were not a sufficient basis on which we should set aside the decision. For example. Mr Puzey had observed that four of the authorities cited by him at the second FTT hearing had not been dealt with. They related, however, to the proposition that a payment may amount to consideration even though it does not cover the cost of providing the supply, and as that proposition was common ground there was no need for FTT(2) to deal with it. The essence of the remainder of HMRC's argument was that *Finland* was to be distinguished because the amount the students and the recipients of legal aid paid was determined differently. But even if the argument was not specifically described, FTT(2) dealt with it, and it is implicit in its conclusions that HMRC's argument was rejected. Similarly, there was no need to recite much of the evidence, since it was undisputed; FTT(2)'s exposition of the relevant facts is sufficient without identification of the sources from which they had been drawn.

28. Mr Puzey's second point was that the statement at [23] that all the relevant students paid £896 for the BTEC course was wrong: the amount a student of this kind had to pay differed depending on the nature of the course. The amount identified was the fee for one particular engineering course; the College's own prospectus showed that there were many different courses attracting different tuition fees. Any of the relevant students who was undertaking one of those other courses was required to pay the published fee for that course, and it followed that it was the course, and not the student's personal circumstances, which determined how much was paid. FTT(2) was also wrong to contrast the relevant students with overseas students. It is true that the overseas students were required to pay substantially more for the same course, but the College's own case was that it was targeting two different markets, that is for local students who, it was assumed, would not be able to pay a greater amount, and overseas students who were assumed to be willing to pay a premium—the College's evidence was that there was no upper limit when fixing the fees of overseas students and that they generally paid significantly more than the cost to the College of providing the course. It was, therefore, incorrect to say that £896 was a reduced fee. It was not; it was the fee the College charged to its residual class of local students.

29. This error, Mr Puzey continued, led the FTT into a misunderstanding of what was said in *Finland*. At [31] the judge dealt with a disparate group of students, both those who paid reduced fees because of their personal circumstances—the paras [21] and [22] students—and the residual group, the para [23] students. They could not be lumped together in that way; the paras [21] and [22] students all had in common the fact that they paid less than the published fee because of their personal characteristics, whereas the para [23] students paid the

full published fee applicable to local students. It was plain that the judge had misunderstood what was required of him from what he said at [16] of FTT(2): that he was required to consider "the question of how part-payment of fees affects the calculation of the non-business receipts". The focus should have been on the para [23] students alone, and had the FTT adopted that course it would have realised that these students were not comparable to the recipients of legal aid discussed in *Finland*.

30. Mr Prosser's response was that, despite the apparently all-embracing nature of what it said at [23], the FTT was well aware that the BTEC civil engineering course for which the students with which that paragraph dealt paid £896 was merely an example. At the second hearing before Judge Barlow he had the written and oral evidence of Mr John Foster, the deputy principal of the College. He was cross-examined by Mr Puzey, but for clarification only—there was no challenge to his evidence. He described the fees and funding received by the College in running a BTEC course in civil engineering, and explained that he had chosen that particular course because it was reasonably typical, and attracted fee-paying students. The FTT could not be criticised for taking that same course, as it had, as an example.

31. Mr Prosser submitted that it was likewise not possible to criticise FTT(2) for its having taken the students described at paras [21] to [23] together, and for its comparison of them with the overseas students. The former all paid reduced tuition fees, substantially lower than the cost of putting on the course, whereas the latter paid as least as much as that cost, and usually more. The statement at [23] that £896 was a "reduced fee" was plainly correct; it was less than the overseas students paid, and it was less than the cost of putting on the course. FTT(2) was also right to point that fact out at [24]; it was an observation that reflected the evidence that, at the material time, the College received a grant of £1,994 for the BTEC civil engineering course so that the student's payment of £896 represented only 31% of the total amount received. It was quite reasonable to describe £896 as "reduced" by comparison with what the overseas student paid for the same course, about £5,000.

32. HMRC's attempt to draw a distinction between the paras [21] and [22] students and the para [23] students did not stand up to scrutiny, in his submission. All of the students in these categories paid less than the cost of their courses for different personal reasons, which might be because of their income, because of their educational attainments, because of the fact that they were offenders undertaking community service or, in the case of the para [23] students, because they were adults (so did not qualify for free education), and were UK residents so not liable to pay the full fee for the course as the overseas students were required to do. For these reasons too the analogy drawn by FTT(2) between this case and *Finland* was properly drawn. The para [23] students paid less than the overseas students—therefore a reduced fee—because of a personal characteristic, the fact that they were UK-resident. In fact, the students in any particular classroom could all be paying different fees, or none, because of their personal characteristics.

33. HMRC's third argument was that FTT(2) was also wrong at [24] and [32] to treat as significant the fact that the fee paid by such students, whether £896 or some other amount, did not cover the cost of the course, and that the College

made up the difference from the block grants it received from the LSC and others. It is immaterial that the payment made falls short of the cost of providing the service: see *Hotel Scandic Gåsabäck AB v Riksskatteverket* (Case C-412/03) [2005] STC 1311 at [22]: "the fact that the price paid for an economic transaction is higher or lower than the cost price is irrelevant to the question whether a transaction is to be regarded as a 'transaction effected for consideration'." In addition, as the Advocate General observed in *Finland* (see [38] of the opinion), it is not necessary for an activity to be carried on with a view to profit in order to qualify as an economic activity within the meaning of art 9 of the Principal VAT Directive (set out at para 6 above), referring as it does to an economic activity "whatever the purpose or result of that activity".

34. Mr Prosser retorted that, contrary to HMRC's argument, it could be seen from *Finland* that the disparity between what was paid by the recipients of the service and the cost of providing it was a relevant factor. HMRC's argument did not reflect what was said by the court at [50] (set out at para 21 above), namely that the difference between the contributions of 1.9 million euros and the operating costs of 24.5 million euros "suggests that the part payment borne by recipients must be regarded more as a fee … than as consideration in the strict sense". In *Revenue and Customs Commissioners v Longridge on the Thames* [2014] UKUT 504 (TCC), [2015] STC 672 ("*Longridge*"), too, Rose J, sitting in this tribunal, had rejected HMRC's argument that the FTT in that case had been wrong to focus on the disparity between the cost of the service and the price charged. Nothing could be drawn from *Hotel Scandic* in this context since in that case it was assumed that an economic activity was being carried on whereas that was the question in *Finland*, and the court had not thought it necessary even to refer to *Hotel Scandic*. That could not be an oversight as the same Advocate General participated in both cases.

35. At para [47] of his opinion in *Finland* Advocate General Colomer said:

> "If subsidised legal aid is provided by a private lawyer, it is easy to find that direct relationship, since, irrespective of whether the client pays nothing or pays only a fraction of the fee, the full amount is paid by the State. The professional always obtains true consideration, the amount of the legally appropriate remuneration, which is therefore subject to VAT. Whether it comes in whole or in part from public funds, the price depends solely and exclusively on the nature of the work carried out."

36. If HMRC's argument was right, Mr Prosser said, it would follow from that observation that the grant element of the College's income would amount to consideration for a taxable supply, yet HMRC accept, correctly, that such payments are outside the scope of VAT. The focus has to be solely on what the student pays just as, in *Finland*, the focus was on what the recipient paid. Although there are some factual differences between the two cases there are no differences of principle.

37. Mr Puzey's next complaint was that the FTT's analysis of the relevant law was also inadequate. The first question to address is whether there is reciprocity of obligation, in that the remuneration received by the provider of the service constitutes the value actually given in return for the service supplied: see the judgment of the Court of Justice in *Tolsma v Inspecteur der Omzetbelasting*

Leeuwarden (Case C-16/93) [1994] STC 509. The second is whether there is a direct link between the service provided and the consideration received: see *Apple and Pear Development Council v Customs and Excise Commissioners* (Case C-102/86) [1988] STC 221. The Court of Justice referred to both of these cases in its judgment in *Finland*, but on the way to reaching the conclusion that the services provided by the lawyers in private practice, who received payment in full for those services, were taxable. This point had been made by HMRC at both of the hearings before the FTT, but it had been ignored.

38. He submitted that neither of those two principles is difficult to apply. In *Finland* it was regarded as immaterial that payment to the private lawyers might come in part from the contribution and in part from the State because the lawyer always received the full amount, representing the price due for the work carried out. Thus there was reciprocity of obligation, and a direct link between the service rendered and the price paid for it. Here too the requirements were satisfied: the relevant student paid the prescribed fee, and the College provided the course in return. At [31] of FTT(2) the judge referred to "varying" or "variable" factors, meaning their individual personal characteristics, which affected what the students paid, and came to the conclusion that they were sufficiently analogous to the income levels which dictated the amount of the contribution in *Finland* to negate a direct link between the payment and the supply. The factors which FTT(2) identified were, however, relevant only to the paras [21] and [22] students; it was their lack, rather than possession, of any relevant characteristic which led to the payment, by the para [23] students, of the full fee.

39. It followed therefore that the two conditions identified by the court in *Finland* which led it to the conclusion that the private lawyers' fees were the consideration for a taxable supply made in the course of business were also met here. There was reciprocity of obligation between the para [23] students and the College; and there was a direct link between the payment and the supply. The only proper conclusion is that the College was making its supplies of education to those students in the course of business.

40. Mr Prosser's response was that the comparison drawn in FTT(2) between *Finland* and this case was one the judge was entitled to draw. The court took particular account of the fact that the payment by the recipient of legal services was only a part-payment, and that the proportion payable by the recipient was partly dependent on the recipient's income. Thus the value of the service provided was not the factor which determined what the recipient paid, and the aggregate of all part-payments made amounted to only a small proportion of the gross operating costs of the public offices. What the judge said in FTT(2), at [30], showed that he was conscious that the parallel between this case and *Finland* was not exact, yet the relevant students, he found, made part-payments of the fees. He then drew an analogy between the varying personal factors relevant in this case and the income levels in *Finland*. The analogy was a proper one, and it was right to lead him to the conclusion that the part-payments were not sufficiently direct to amount to consideration.

41. A similar point had been made by Rose J in *Longridge*, in which the question was whether a charitable organisation providing facilities for training in water-based and other activities was carrying on a business. The organisation

charged fees which differed by reference to the characteristics of the payer: young people might pay less, while adults might pay more, than the economic cost of providing the supply, and in some cases the charges were waived altogether. The charges did not contribute to the organisation's capital costs, which were met from donations and grants. The FTT in that case concluded that although the organisation charged for the supplies it made, its doing so was incidental to its main purpose of advancing its charitable objectives, and it was therefore not carrying on a business.

42. At [32] Rose J observed that *Finland* indicates that when deciding whether activities are economic, the test to be applied is a "nuanced one". At [34] she added that there is a dividing line to be drawn between a situation "where the activities do amount to the furtherance of a business even though they are not aimed at making a profit, and a situation akin to that in *Finland* where the activity is not conducted as a business even though payment is made by the recipient for the services provided." In *Longridge* the FTT decided that the activities were not economic, and Rose J held that "that is precisely the kind of evaluation of the facts that the FTT is well placed to make and with which the appellate court should not interfere."

43. Mr Prosser recognised that a different tribunal might have come to a different conclusion but the fundamental question is whether the decision reached in FTT(2) was one open to the tribunal. In essence, HMRC were inviting this tribunal to do precisely what Rose J said was not permissible, namely to interfere with FTT(2)'s findings of fact.

44. Mr Puzey, in reply, argued that this case could not be compared, as the College had suggested, with *Longridge*, since the activities of the two organisations were quite different. In addition, as Rose J said at [15], "The Tribunal found that by far the greater part of Longridge's activities are 'directly by way of carrying out its charitable objectives' and a limited part was 'seemingly for the purpose of raising funds' to subsidise the charitable activities." Here, the fees charged to the para [23] students were directly linked to the supplies they received. Moreover, the question in *Longridge* was not whether some of what it did amounted to a business, but whether any of it did so; here, the College accepted that it was carrying on a business and the question was whether its supplies to the para [23] students formed part of that business. There was, he said, no true analogy between the cases. The better comparison is with *Hotel Scandic*.

Discussion

45. We agree with Mr Puzey that FTT(2) is not altogether satisfactory. In particular, we accept his argument that what the judge said at [31] does not address the distinction HMRC were seeking to draw between the paras [21] and [22] students, liable in principle to pay the fee published in the College's prospectus but who were eligible for partial or total remission on the one hand, and the para [23] students, liable to pay the published fee and who were not eligible for any remission, on the other. At the very least, he has failed to explain why he rejected the argument (if he did reject it) that a distinction was there to be drawn. It is, instead, unclear whether he rejected HMRC's argument in his own mind but failed to explain why, or overlooked it.

46. That failure amounts, in our view, to a material error sufficient to require intervention by this tribunal: see *Pendragon plc v Revenue and Customs Commissioners* [2015] STC 1825 at [44] *ff* and *Weymont and another v Place* [2015] EWCA Civ 289 at 4 *ff*. It does not, of course, necessarily follow that the conclusion in FTT(2) is wrong.

47. There is, we think, a clear analogy between the legal aid recipients in *Finland* and the paras [21] and [22] students in this case. They all paid less than the ordinary cost—in *Finland*, the fee set by national legislation, here the fee set by the College—by reason of their possession of certain personal characteristics which entitled them to a measure of remission. HMRC do not disagree with what FTT(2) said about those students at [31]. The question which remains, therefore, is whether the fee published in the College's prospectus is to be regarded, as the College maintains, as itself a rebated or remitted fee such that there is in reality no distinction to be drawn between the para [21] and [22] students, and the para [23] students who were entitled to no further remission.

48. It is, of course, true that the published fee is less than the cost of the course—in the case of the BTEC course used as an example, the published fee represented only about a third of the total amount received by the College, which is itself not necessarily equivalent to the cost. The court made it clear in *Hotel Scandic* that it is not a determining factor that a supply might be made for consideration less than cost although it seems from what was said in *Finland* at [50] that it also takes the view that there must come a point at which the disparity between the value of the payment and the cost of the supply becomes so great that the direct link between supply and consideration to which the *Apple and Pear Development Council* case referred is lost.

49. However, what was said at [50] follows from the observations at [48] and [49], in which the court addressed the fact that the amount the recipient paid was determined by reference to two factors, the cost of the supply and the extent of his resources. In our view the conclusion that the supply was not taxable is dependent upon that combination: without the overlay of variation of payment according to means the link between supply and payment would not be broken. In the case of the para [23] students there is no such overlay; they must pay the published fee irrespective of their means, and the direct link remains in place.

50. We do not accept Mr Prosser's argument that the absence of a personal characteristic entitling the student to some remission is itself to be treated as a relevant personal characteristic; but even if we did accept it, it would not help him. It was the fact that the fee which would otherwise be payable was abated by reference to the recipient's personal characteristics which was determinative in *Finland*; but in the case of the para [23] students there was no abatement for that reason. If the published fee is to be treated as abated, as Mr Prosser argued, it was abated by reason of its being subsidised by a grant, without regard to the circumstances of the individual ultimately receiving the supply. It also cannot be treated as the fee charged to overseas students abated for those resident in the UK, since the College's own evidence, as we have described it above, was that the two fees were determined independently of each other, and on quite different criteria. In our judgment the reasoning in *Finland* cannot be applied to the para [23] students.

51. We do not find anything in *Longridge* which undermines that conclusion. That was, as Rose J said, a case in which the FTT was required to undertake a fact-sensitive evaluation of the organisation's activities as a whole in order to determine whether or not it was carrying on a business at all. The question was not, as here, whether the organisation was making supplies in return for consideration—it was accepted that it was—but whether what it did, overall, amounted to an economic activity. Here, it is not in dispute that what the College does is capable of amounting to a business activity, and that in the case of its supplies to overseas students does in fact amount to a business activity. The only question here is whether the published fees amount to consideration for what the para [23] students receive, with the consequence that the supplies to them are also made, as Note (6) puts it, in the course or furtherance of a business.

52. In our judgment the fact that the fees charged to the para [23] students represented less than the cost of the supply, because that cost was in part defrayed by grant funding, does not have the consequence that the fees did not amount to consideration for the supply. There was a direct link between the payment and the supply, and there was reciprocity of obligation: as Mr Prosser accepted, the fees were determined on a course-by-course basis by operation of the formula we have described, and a student accepted on a course who, or whose employer, paid the fee became entitled to receive the tuition. Thus both the *Apple and Pear Development Council* and *Tolsma* requirements were satisfied, with the consequence that the fee must be regarded as the consideration for the supply.

53. It follows that the College's supplies to the para [23] students were made in the course or furtherance of a business.

Disposition

54. For those reasons, the appeal must be allowed and the decision of the FTT is set aside.

55. We invite the parties to agree and submit to us for approval an order reflecting this decision, including any consequential orders or directions.

56. We cannot leave this appeal without expressing some disquiet that it should have reached us at all. It is common ground that the College is a charity, and that the bulk of its income is derived from public funds. Because that public funding does not cover all of its costs it is compelled to seek income from other sources; but its doing so does not alter the fact that it remains a charity providing education for young people. If, by careful management or good fortune, it can earn its further income in one way rather than another, or can keep the extent of the income earned in particular ways below an arbitrary threshold, it can escape a tax burden on the construction of a building intended for its charitable purpose, but if it is unable to do so, even to a trivial extent, it is compelled to suffer not some but all of that tax burden. We think it unlikely that Parliament intended such a capricious system. We consider it unlikely, too, that Parliament would consider it a sensible use of public money for the parties to litigate this dispute twice before the FTT and now twice before this tribunal. We do not blame the parties; the College is obliged to maximise the resources available to it for the pursuit of its charitable activities, just as HMRC are obliged to collect tax which is due. Rather, we think the legislation should be reconsidered. It cannot be impossible to relieve

charities of an unintended tax burden while at the same time protecting commercial organisations from unfair competition and preventing abuse.

5

The Honourable Mr Justice Barling
Judge Colin Bishopp
10 **Judges of the Upper Tribunal**

Release date 20 January 2016