VAT focus

To *Longridge* and beyond: the meaning of 'business' for 'relevant charitable purpose'

Speed read

It has long been accepted in the VAT world that 'business' (as used in VATA 1994) has the same meaning as 'economic activity' (as used in the Principal VAT Directive). What has been more controversial is whether UK jurisprudence on what 'business' means is consistent with EU jurisprudence on what amounts to an 'economic activity'. In *Longridge*, a case on what 'business' means when considering 'relevant charitable purpose', the Court of Appeal puts this long running debate to bed. Is this now the end or is there more after the CJEU ruling in *Gemeente Borsele*?

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A charity is planning to put up a new building. A trustee hears that if they could certify that the new building will be used solely for a 'relevant charitable purpose', no VAT would be payable on the construction services. Google tells her that VATA 1994 Sch 8 Group 5 note 6 says:

> 'Use for a relevant charitable purpose means use by a charity in either or both the following ways, namely:
> (a) otherwise than in the course or furtherance of a business;
> (b) as a village hall...'

The charity will not be using the building as a village hall (or similar); it will be using it to run educational courses in line with its charitable objectives. Although it will be charging fees, the fees will be (remarkably) modest. The charity will not be doing anything that, in the trustee's mind, even comes close to commercial. She is confident that they are not carrying on a business, and thinks they will be able to escape VAT on the construction. If only it were that simple...

What 'business' means

The most prominent UK authority on what 'business' means is *Lord Fisher* [1981] STC 238. The case identified six indicia which HMRC still regards as the 'normal questions which need to be considered when determining whether an activity is business for VAT purposes':

1. Is the activity a serious undertaking earnestly pursued?
2. Is the activity an occupation or function which is actively pursued with reasonable or recognisable continuity?
3. Does the activity have a certain measure of substance in terms of the quarterly or annual value of taxable supplies made?
4. Is the activity conducted in a regular manner and on sound and recognised business principles?
5. Is the activity predominantly concerned with the making of taxable supplies for a consideration?
6. Are the taxable supplies that are being made of a kind which, subject to differences of detail, are commonly made by those who seek to profit from them?

(See para 4.1 of the current version of *VAT Notice 701/1: charities*, although the passage above could well be modified in light of the Court of Appeal judgment in *Longridge on the Thames* [2016] EWCA Civ 930.)

What 'business' means in the context of 'relevant charitable purpose' was specifically considered in *Yarburgh Children's Trust* [2002] STC 207. The case concerned a building owned by a charitable trust and let at a rent that was significantly below market to another charity, which ran a playgroup from it, charging flat fees. The question was whether use by each charity constituted use 'otherwise than in the course or furtherance of a business'.

Patten J (as he then was) held that: 'The wider context needs to be looked at in order to determine whether the transaction in question is or is indicative of a business.' He considered that the test whether any activity 'was carried out in the course or furtherance of a business … necessitates an inquiry … into the wider picture … to ascertain the nature of the activities carried on by the person alleged to be in business, the terms upon which and manner in which these activities (including the transaction in question) were carried out and the nature of the relationship between the parties to the transaction'. He regarded it as clear that the 'business' question 'simply could not be answered by reference only to the fact that a service was provided at a price. That is the beginning not the end of the inquiry.'

Meanwhile in Europe...

The 'business' concept is fundamental to how VAT operates in the UK, but what it means is not within the exclusive province of the UK courts. It is (and, if not, should be) synonymous with the 'economic activity' concept used in the Principal VAT Directive. Because of this, it is subject to EU jurisprudence on the subject.

In *Commission v the Netherlands* (Case C-235/85), the CJEU ruled that 'in so far as [a person] provide[s] services … on a permanent basis and in return for remuneration, they carry out an economic activity'.

In most cases, whether an activity is carried out 'on a permanent basis' is reasonably easy to ascertain. Whether it is carried out 'for remuneration' is more difficult, particularly where there is payment, but that payment represents only a fraction of the full cost of the activity (as in *Yarburgh*, where a lease was granted at rent, but rent that was significantly below market).

To determine whether the payment in such cases amounts to 'remuneration', the same test is applied as for the determination of whether a payment is 'consideration' for the purposes of ascertaining whether something is done for a consideration (and is thus a supply of services) within the meaning of VATA 1994 s 5(2)(b).

The CJEU ruled in *Apple and Pear Development Council* (Case C-102/86) that 'the concept of the supply of services effected for consideration … presupposes the existence of a direct link between the service provided and the consideration received'.

That the same test is used to determine whether an activity is carried on 'for remuneration' as for the determination of whether there is 'consideration' for a supply of services begs the question whether finding a supply of services automatically means there is also an economic activity. The CJEU's ruling in *Commission v Finland* (Case C-246/08)

suggests that it does, when the court concludes that 'the link between the [services in question] and the payment … is [not] sufficiently direct for that payment to be regarded as consideration for those services and, *accordingly* [emphasis added], for those services to be regarded as economic activities'.

But if that is correct, where would that leave the *Yarburgh* approach, particularly how it regards 'the fact that a service was provided at a price … [as] the beginning not the end of the inquiry'?

Longridge on the Thames

This was addressed in *Longridge*. The case concerned a charity that provided water-based activities for recreational and educational purposes, and whether VAT was payable on the construction of its new training centre. The charity charged for the use of its facilities – charges which were set by reference to the extent to which the charity's operational costs exceeded its grant and donated income, and which it sometimes reduced even further or waived in pursuit of its charitable objects.

HMRC argued that because the charity 'had an activity which was permanent and which was carried out in return for remuneration … it was to be presumed to have an economic activity'; and that presumption – or, as the Court of Appeal preferred, that 'General Rule' – was not rebutted either by the fact that the charity acted in the public interest or had a charitable (as opposed to a business or commercial) motive, or by how it relied on grants and donations or set its charges.

The Court of Appeal agreed with this argument, and rejected the charity's submission that 'to decide whether a person supplying services is engaged in economic activity one is entitled to take into account those terms and features which lead one to conclude that the manner in which the activities are undertaken is different from that which would be undertaken by someone engaged … in that activity in the ordinary course of the market'. It held that the domestic UK approach of looking at the wider context (as in *Yarburgh*) was not consistent with EU law.

An inconvenient ruling?

Longridge was heard in April. On 12 May, the CJEU released its ruling in *Gemeente Borsele* (Case C-520/14). The case concerned whether, in providing school transport services in return for modest contributions, a Dutch municipality was carrying out an economic activity.

Noting the significant difference between the operating costs of the municipality and the contributions it received, the court held that the 'lack of symmetry [meant] that there is no genuine link between the amount paid and the services supplied', with the result that 'the link between the transport service … and the payment … is [not] sufficiently direct for that payment to be regarded as consideration for that service and, accordingly, for that service to be regarded as an economic activity'.

In this respect, there is little to distinguish the CJEU's approach from the approach it took in *Commission v Finland*. But the 'direct link' test – the test used to determine both whether there is 'consideration' and whether there is 'remuneration', and the bedrock of the Court of Appeal's judgment in *Longridge* – was not the only test the CJEU applied.

It ruled that 'the existence of a supply of services for consideration ... is not sufficient to establish the existence of an economic activity', and considered that all the circumstances in which a service is supplied had to be examined. '[C]omparing the circumstances in which the person concerned supplies the services in question with the circumstances in which that type of service is usually provided may … be one way of ascertaining whether the activity concerned is an economic activity.' The number of customers and the amount of earnings may also be relevant.

Turning to the actual facts, the CJEU held that 'the conditions under which the services at issue … are supplied are different from those under which passenger transport services are usually provided, since the municipality of Borsele … does not offer services on the general passenger transport market, but rather appears to be a beneficiary and final consumer of transport services which it acquires from transport undertakings with which it deals and which it makes available to parents of pupils as part of its public service activities'.

Perhaps the *Yarburgh* approach ... has now to be couched in EU rather than *Fisher* terms

The CJEU ruling in *Gemeente Borsele* does not detract from the Court of Appeal's focus in *Longridge* on 'whether there was a sufficiently direct link between the payment and the service'. Nor does it detract from its finding that the 'differences between the test of direct link and the *Fisher* criteria are material'. Where questions do arise is in relation to the circumstances where the so-called General Rule can be displaced.

The Court of Appeal considered that the approach taken by the FTT and the UT in *Longridge* – applying the 'wider picture' approach laid down in *Yarburgh* – was inconsistent with EU jurisprudence. Query, however, whether, in light of *Gemeente Borsele*, the approach the Court of Appeal took was itself too narrow.

In *Gemeente Borsele*, the CJEU referred to circumstances where the 'direct link' test is met – being circumstances where a supply of service is established – but the activity in question still falls short of an economic activity. This was precisely the scenario in *Yarburgh*. The reference in *Gemeente Borsele* to 'comparing the circumstances in which the person concerned supplies the services in question with the circumstances in which that type of service is usually provided' is also an intriguing echo of the charity's submissions in *Longridge* regarding how 'the manner in which [its] activities are undertaken is different from that which would be undertaken by someone engaged … in that activity in the ordinary course of the market'.

Perhaps reading *Longridge* and *Gemeente Borsele* together, the conclusion is not that the *Yarburgh* approach is no longer applicable, but that it has now to be couched in EU rather than *Fisher* terms, abandoning concepts such as 'predominant concern', for example, and focusing more on the factors discussed in *Gemeente Borsele*. And if one were to carry out such an exercise, would the fact that the charity in *Longridge* was financed by donations and grants rather than its own income have more relevance than it was accorded in the Court of Appeal? ■

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- Beyond *Longridge* (Graham Elliott, 14.9.16)
- Cases: *Longridge on the Thames v HMRC* (6.9.16)
- When are charities' activities within the scope of VAT? (Elizabeth Shanahan, 23.10.14)
- *Capernwray*: the relevant charitable purpose test (Peter Jenkins, 10.9.14)