TC04247

Appeal number: TC/2013/06233

VALUE ADDED TAX – exemption for sporting supplies – Group 10, Schedule 9, VATA – whether two subsidiaries of the Appellant (itself an "eligible body" within Note (2A) to Group 10) were themselves "eligible bodies" within Note (2A) – held no 'non-profit-making aim' was discernible from the constitutions of the subsidiaries and that no other 'specific facts' suggesting that the subsidiaries had a 'non-profit-making aim' obviated the necessity of such an aim being discernible from their constitutions – **Kennemer Golf & Country Club v Staatssecretaris van Financiën** ***(Case C-174/00) [2002] STC 502 applied – appeal dismissed***

FIRST-TIER TRIBUNAL
TAX CHAMBER

ST ANDREW'S COLLEGE BRADFIELD **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE JOHN WALTERS QC
MRS SHAMEEM AKHTAR

Sitting in public at the Royal Courts of Justice, London on 17 and 18 December 2014

Roger Thomas QC, instructed by Crowe Clark Whitehill, for the Appellant

Philip Shepherd, HMRC, for the Respondents

DECISION

1. The Appellant in this appeal, St Andrew's College, Bradfield ("the College") is a charity, incorporated by Royal Charter and registered with the Charity Commission as a co-educational boarding school.

2. The College is registered for VAT and is the representative member of a VAT group of companies. The other companies in the VAT group are the College's two wholly owned subsidiaries, Bradfield College Developments Limited ("Developments") and Bradfield College Enterprises Limited ("Enterprises").

3. The College appeals against a decision of the Respondent Commissioners ("HMRC") to refuse a claim for the refund of the excess of output tax charged and accounted for by the College in the quarterly VAT periods 11/08 to 08/12 inclusive over associated input tax deducted. The claim totals £427,166. It relates to VAT charged by the College, as representative member of the VAT group in respect of supplies actually made by Developments, and later Enterprises (but treated as made by the College pursuant to section 43 VAT Act 1994 ("VATA") – Groups of companies) for the provision of services closely related to sport or physical education.

4. The basis of the claim is that Developments and Enterprises are each of them an "eligible body" within the meaning of Group 10 of Schedule 9 to VATA (exemptions related to sport, sports competitions and physical education), and that therefore the supplies in issue were properly exempt pursuant to section 31 and Schedule 9 VATA. Section 43(1AA) VATA makes it clear (and it was common ground) that whether or not the supplies were exempt as claimed turns on whether Developments or Enterprises, as the case may be, was an "eligible body" and not on whether the College was an "eligible body" (if there is a difference). It is common ground that the College, as an educational charity, is a non-profit making body and an "eligible body".

5. We heard oral evidence from Mr Kester Russell, a director of Enterprises, and Mr Trefor Llewellyn, who until very recently was the Bursar of the College and, although he retired from that post on 1 September 2014, remains employed by the College on a part-time basis. Both witnesses had also provided Witness Statements.

6. From the witnesses' evidence and the documents which were before us we find the facts stated above and below.

7. The supplies with which the appeal is concerned are (as was common ground) supplies of services to unconnected individuals, which services are closely linked with and essential to sport or physical education. They are mainly the making available of the facilities of a Sports Centre built at Bradfield in the early 1990s, and other sporting assets, such as a golf course and tennis courts. Developments formerly carried on the management of the Sports Centre, but, with effect from 1 September 2009 (within the period covered by the appeal) that business was transferred to

Enterprises (which had been established in order to manage the lettings to third parties of the College's other facilities).

8. Since that time, Enterprises has run the business transferred from Developments in its (Enterprises') Sports division, which it runs alongside another business run in its Lettings and Events division (it also runs the College's school shop and café). The Sports division has never been profitable within Enterprises – and the business was not profitable when run by Developments, principally because of a large annual depreciation charge associated with its lease of the land used for the construction of the Sports Centre.

9. Charges made by Enterprises for its sport-related services are lower than those made by comparable service providers (such as David Lloyd Leisure), principally because of time restrictions on use.

10. Mr Llewellyn's evidence was that when Enterprises and Developments were set up they entered into covenants to make a gift of all their taxable profits to the College. In his Witness Statement he said that both deeds of covenant had been lost but referred to mention of the existence of them in the companies' accounts and board minutes.

11. However at the start of proceedings in the appeal on the second day (18 December 2014) various copy documents not previously located by the College were handed up by Mr Thomas QC. These included a Deed of Covenant dated 27 August 1993 made by Developments in favour of the College, and some correspondence in 1998 relating to a different deed of covenant made by Developments in favour of the College. The 1993 Deed made by Developments was made pursuant to a resolution of the board of that company dated 26 August 1993 (which was in evidence) that Developments would pay to the College in the current accounting period and "during each of its following accounting periods" an annual sum equal to the profits of Developments for each such accounting period as described in the eventual Deed.

12. The 1998 correspondence indicates that advice was taken from Coopers & Lybrand by the Bursar of the College as to the principles governing the level of payment to be made by Developments to the College under what was referred to as "the existing deed of covenant", namely the Deed entered into on 27 August 1993. Coopers & Lybrand also suggested that the 1993 Deed be replaced "to reflect the changes in the November 1996 budget whereby payments can be made up to 9 months following the end of the accounting period".

13. A Deed of Covenant dated 6 May 1998 made by Developments in favour of the College was produced, which included a provision to the effect that Developments "may take advantage of Finance Act 1997 Section 64 and postpone making the payment until no later than nine months after the end of the accounting period". The Inland Revenue (Audit and Compliance) by a letter dated 18 September 1998 confirmed that the deed had been "admitted as a valid disposition of income for tax purposes".

14. We accept therefore that a deed in terms of the Deed dated 27 August 1993 was made by Developments, and that a deed in similar terms (although it was not produced) was made by Enterprises in May 1995. (We were shown the minutes of a board meeting of Enterprises held on 25 May 1995 stating that "the Deed of Covenant was approved, signed by the Chairman and Secretary and Sealed"). We also accept that a replacement deed was made by Developments in 1998.

15. The Deed dated 27 August 1993 provided as follows:

> Developments would pay to the College in each of its accounting periods an annual sum equal to Developments' profits for each such accounting period less income tax if appropriate. The payments were to be made as follows: the first on or before 31 August 1993, the payments for the accounting periods up to 31 August 1997 annually before 31 August, and subsequently on 31 August. There was provision for adjustment in the event of estimated payments being made.
>
> Developments' profits were defined as profits of Developments "as computed for corporation tax purposes before deducting any payment under this Deed but after deduction of all other charges on income or any part thereof which for corporation tax purposes shall be allowable against the total profits for the accounting period in question".
>
> The covenant was to commence on 27 August 1993 and was to continue for the term of four years in any event, and thereafter until terminated by Developments in writing at any time after 31 August 1998, or "until such time as the annual sums payable [thereunder] cease to qualify as a charge on income of Developments within the meaning of section 338 of the Income and Corporation Taxes Act 1988 [("ICTA")] for the purposes of corporation tax, or would cease so to qualify were any payment due [thereunder] in any accounting period of [Developments]".

16. The Deed dated 6 May 1998 provided as follows:

> Developments would pay to the College as a covenanted payment to charity within the meaning of section 339(8) ICTA "an annual sum equal to the annual income of Developments" less income tax at the basic rate for the time being in force. There was provision for the payments to be made before the end of an accounting period or not less than 9 months after the end of an accounting period. There was provision for adjustment in the event of estimated payments being made.
>
> "Annual income of [Developments]" was defined to mean its distributable income as defined in paragraph 8(1), Schedule 19, ICTA but without deducting the amount of corporation tax payable in respect of such income or the annual sum payable under the deed.
>
> The covenant was to commence within and include the accounting period of Developments (as defined in section 12 ICTA) which included 6 May 1998 and was to continue for each accounting period thereafter until and including the

accounting period ending 31 August 2002 "and shall continue thereafter until determined by either party by written notice to the other".

17. It is to be noted that the tax law in relation to donations to charity by companies was substantially amended by the Finance Act 2000. There was no evidence that any new or substitute deeds or arrangements were entered into by Developments or Enterprises in response to those amendments.

18. Accounts of Developments and of Enterprises (and of the College) were in evidence, covering the years ended 31 August 2009 to 2013. The accounts of Enterprises in evidence also covered the year ended 31 August 1996.

19. Note 5 to the Accounts of Developments for the year ended 31 August 2009 stated that "[n]o charge for taxation arises in view of the company's arrangement to pass all of its taxable profits to Bradfield College under gift aid". But after that year that statement was removed. Mr Llewellyn's evidence was that PricewaterhouseCoopers, who audited the accounts, had since explained to him that the statement remained applicable and that they were not aware why it was removed, suggesting that it was possible that they decided in 2009 that it was unnecessary as the tax reconciliation on the accounts gave an adequate explanation as to why no tax was due.

20. The accounts of Enterprises for the year ended 31 August 1996 (audited by Coopers & Lybrand) contained a directors' report in which it was stated that in that year Enterprises made a payment under deed of covenant to the College of £52,407 (1995: £46,157). The figure of £52,407 reflects the operating profit of Enterprises for the year ended 31 August 1996 as per its profit and loss account, of £52,190, together with interest received of £217. We noted that the 1995 comparable figures showed that the payment to the College under deed of covenant of £46,157 had been £1,300 more than the operating profit and interest received for that year (1995).

21. Mr Llewellyn explained that the amount gifted each year was an estimated amount required to cover the taxable profits and that to the extent that, for example, capital allowances were available, some of a company's operating profit might be retained.

22. Indeed the accounts showed (as per the profit and loss accounts) that the payments to the College "under gift aid" were usually of an amount that would leave the paying company with a profit on ordinary activities before taxation of a positive amount, derived from its operating profit and interest receivable.

23. Thus, in this way, Enterprises retained £1,709 profit in the 2008 year, £51,376 profit in the 2009 year (as it was able to reduce its taxable profits to nil by reason of a surrender of losses by way of group relief to Enterprises by Developments), £1,648 profit in the 2010 year, £3,553 profit in the 2011 year, £3,388 profit in the 2012 year and £2,831 profit in the 2013 year. The payments by Enterprises to the College "under gift aid" in those years were: 2008: £415,000; 2009: £300,000; 2010: £380,000; 2011: £330,000; 2012: £320,000; and 2013: £364,000.

24. Mr Llewellyn's evidence was that the board of Enterprises wanted to retain a small profit because it was considered desirable to do so. Suppliers to the company

would look at the accounts and the board considered that it would be advantageous that they should see a small bottom line accounting profit. It was always intended that there should be no taxable profit retained in the company. Capital allowances were generally available to achieve this.

25. Mr Llewellyn explained that his recollection was that the retention of profit by Enterprises in the 2009 year was motivated by a wish to eliminate negative reserves of approximately £50,000 which were anticipated when the business of Developments was acquired with effect from 1 September 2009.

26. The accounts of Developments show that in the year ended 31 August 2008 it made an operating loss of £217,922, received interest of £2,296, but nevertheless made a payment to the College "under gift aid" of £5,000. The year ended 31 August 2009 was the last year in which Developments traded (its trading activities were transferred to Enterprises with effect from 1 September 2009). In the 2009 year Developments made a net loss on ordinary activities before taxation of £209,984 and made no payment to the College "under gift aid" (or otherwise as a gift). In the 2010 to 2013 years Developments was effectively dormant.

27. By virtue of its shareholding in Enterprises and Developments, the College would have been entitled to receive any profit distributed by either of those companies by way of dividend. In fact, neither company has ever declared a dividend.

28. The Memorandum and Articles of Association of Enterprises and of Developments were in evidence. They were in relatively standard form, the companies having been bought off the shelf. In particular, both companies' objects were defined in their respective Memoranda of Association in the most general terms permitting the carrying on of business for profit. There was nothing in the Articles of Association of either company prohibiting distributions by way of dividend, bonus or other means until the Articles of Enterprises were amended by a Special Resolution passed on 30 January 2014 by the insertion of a new Article as follows:

> 'Prohibition of distributions by way of dividend, bonus or any other means
>
> No distribution of or out of the company's profits or gains, other than on a winding up under Regulation 117 of Table A (see Note), shall be made, and regulations 102 to 108 and 110 of Table A in S.I. 1985/05 are hereby dis-applied, save that this shall not prevent the making of charitable donations under the Gift Aid Scheme to a member that is a charity under English law.'

29. Both Mr Russell and Mr Llewellyn were cross-examined on the intention of Enterprises (and Developments, when it was trading) to make a profit. Their evidence was clear, that both companies intended to maximise their revenue with a view to paying all or almost all of any surplus over to the College under the deeds of covenant.

The legislation

30. The domestic legislation describing the VAT exemption for sport, sports competitions and physical education is in Group 10 of Schedule 9, VATA. Item 3 of that Group provides as follows:

'3. The supply by an eligible body to an individual, except where the body operates a membership scheme, an individual who is not a member, of services closely linked with and essential to sport or physical education in which the individual is taking part.'

31. The relevant Notes to Group 10 are as follows:

'(2A) Subject to Notes (2C) and (3), in this Group "eligible body" means a non-profit making body which –

(a) is precluded from distributing any profit it makes, or is allowed to distribute any such profit by means only of distributions to a non-profit making body;

(b) applies in accordance with Note (2B) any profit it makes from supplies of a description within Item 2[1] or 3; and

(c) is not subject to commercial influence.

(2B) For the purposes of Note (2A)(b) the application of profits made by any body from supplies of a description within Item 2 or 3 is in accordance with this Note only if those profits are applied for one or more of the following purposes, namely –

(a) the continuance or improvement of any facilities made available in or on connection with the making of the supplies of those descriptions made by that body;

(b) the purposes of a non-profit making body.

(2C) In determining whether the requirements of Note (2A) for being an eligible body are satisfied in the case of any body, there shall be disregarded any distribution of amounts representing unapplied or undistributed profits that falls to be made to the body's members on its winding-up or dissolution.'

32. Notes (4) to (17) inclusive make detailed provision for determining whether a body is to be taken, in relation to a sports supply, to be subject to commercial influence. It is not necessary to set these provisions out because HMRC, as we understand it, does not (any longer) suggest that Developments or Enterprises or the College was subject to commercial influence within the meaning of Group 10, Schedule 9, VATA and no evidence before us suggested that any of them was subject to commercial influence within that meaning. We find that none of them was so subject.

33. The relevant provisions of the Principal VAT Directive (Council Directive 2006/112/EC) ("PVD") are articles 132 and 133.

34. Article 132 of the PVD provides relevantly that Member States shall exempt: -

'1(i) the provision of children's or young people's education, school or university education, vocational training or retraining, including the supply of services and of goods closely related thereto, by bodies governed by public law having such as their aim or by other organisations recognised by the Member State concerned as having similar objects;

…

[1] Item 2 of Group 10, Schedule 9, VATA provides exemption for the grant, by an eligible body established for the purposes of sport or physical recreation, of a right to enter a competition in such an activity.

(m) the supply of certain services closely linked to sport or physical education by non-profit making organisations to persons taking part in sport or physical education;'

35. The parties made reference in their submissions to Article 133 of the PVD, which provides relevantly as follows:

'Member States may make the granting to bodies other than those governed by public law or each exemption provided for in points (b), (g), (h), (i), (l), (m), and (n) of Article 132(1) subject in each individual case to one or more of the following conditions:

(a) the bodies in question must not systematically aim to make a profit, and any surpluses nevertheless arising must not be distributed, but must be assigned to the continuance or improvement of the services supplied;

…'

Relevant case law

36. Mr Thomas referred us to *Canterbury Hockey Club v Revenue and Customs Commissioners* (Case C-253/07) [2008] STC 3351 and *Revenue and Customs Commissioners v Bridport and West Dorset Golf Club Ltd* (Case C-495/12) [2014] STC 663. Those cases established that the exemption for certain services closely linked to sport or physical education supplied by non-profit making organisations may not be limited by restrictions as regards recipients of the services in question, provided they are persons taking part in sport or physical education (*Canterbury Hockey Club*, Judgment [39]) and exemption, if it is available, applies to supplies made to members and non-members alike (*Bridport and West Dorset Golf Club*, Judgment [29]).

37. Both sides relied on *Kennemer Golf & Country Club v Staatssecretaris van Financiën* (Case C-174/00) [2002] STC 502. The third question addressed to the Court of Justice in *Kennemer* is especially relevant in this appeal. That question (as formulated by Advocate-General Jacobs – see [36] of his Opinion) was:

'If an organisation is to be classed as non-profit-making for the purposes of art 13A(1)(m) of the Sixth Directive [now Article 132(1)(m) PVD], to what extent may it none the less make a surplus and what is the relevance in that regard of the first indent of art 13A(2)(a) [Article 133(a) PVD].'

38. The Court of Justice decided that it is the aim which an organisation pursues which will determine whether or not it is 'non-profit-making'. (Judgment [26]). A non-profit-making aim is an aim which is not that of achieving profits for its members. In this, a non-profit-making organisation is contrasted with a 'commercial' undertaking.

39. Whether or not an organisation pursues an aim of achieving profits for its members must be determined having regard to the objects of the organisation in question as defined in its constitution and in the light of the specific facts of the case (Judgment [27]). (This interpretation was anticipated by the Court of Appeal in *Customs and Excise Commissioners v Bell Concord Educational Trust Ltd.* (1989) 4 BVC 51 – an authority cited by Mr Shepherd for HMRC.)

40. Where it is found that an organisation achieves profits, whether or not it seeks to make them or makes them systematically, this will not mean that an organisation which does not aim to distribute such profits to its members is taken out of the category of non-profit-making organisations (Judgment [28]).

41. The condition now in Article 133(a) of the PVD is an optional condition which Member States may impose as an additional condition (Judgment [30]).

42. The Court of Justice endorsed the distinction made by Advocate-General Jacobs between surpluses and profits, respectively corresponding to the French words '*bénéfices*' and '*profits*'. The French word '*profits*' is used to refer to financial advantages for the organisation's members, whereas '*bénéfices*' refers to surpluses arising at the end of an accounting period which may, or may not, depending on the circumstances, be intended to be distributed in one way or another to enrich the natural or legal persons having a financial interest in the organisation (Judgment [33] and Opinion [45]). The aim of an organisation to achieve profits in the sense of '*profits*', or financial advantages for its members, would preclude the organisation's categorisation as 'non-profit-making'. The aim of an organisation simply to achieve profits in the sense of '*bénéfices*', or surpluses of income over expenditure, would not have that effect (Judgment [33]).

43. Thus, Article 132(1)(m) of the PVD is to be interpreted as meaning that an organisation may be categorised as 'non-profit-making' even if it systematically seeks to achieve surpluses which it then uses for the purposes of the provision of its services (Judgment [35]).

The parties' submissions

44. Both parties accept that there is no definition of the term "non-profit making body" for the purposes of the definition of "eligible body" in Note (2A) to Group 10, Schedule 9, VATA.

45. Mr Thomas, for the College, submitted that it was plain from Notes (2A), (2B) and (2C) read together – as they should be read together – that the legislation imposes only two conditions for a body to be an "eligible body" – namely, that it must be permitted only to distribute profits to another non-profit making body, or that distribution of profits be restricted to winding-up (where there is no limitation on the character or status of the persons to whom the distributions may be made); and, secondly, that any profits made from (in this case) sporting supplies either be ploughed back into the continuance or improvement of the facilities for the making of such supplies or that they be applied for the purposes of a non-profit making body (in which case there is not restriction on their manner of application).

46. He accepted that *Kennemer* established that an organisation may not be classified as non-profit making if it pursues the aim of achieving profits for its members, and that, as a general rule, the aim of an organisation is to be ascertained by reference to its objects as defined in its constitution and in the light of the specific facts of the case. He also accepted that at the relevant time (that is, before January 2014) the

Memorandum and Articles of Association of Enterprises did not contain any specific prohibition on the distribution of profits.

47. He submitted, however, that the specific facts of this case which require to be taken into account include the fact that Enterprises is and at all material times has been the wholly-owned subsidiary of the College, which is a charity, and accepted to be a non-profit making body, and the fact that Enterprises has at all material times been under a binding obligation not to distribute its profits, but to apply them for the purposes of the College, a non-profit making body, by covenanting them to the College.

48. In this regard, Mr Thomas submitted that whereas a company could unilaterally change any Articles of Association containing a prohibition on the distribution of profits, an obligation under Deed of Covenant bound a company more effectively to make over all its profits to the covenantee. A distribution made in disregard of a company's obligation under a deed of covenant would be liable to be traced and recovered in a restitution claim. He submitted that the small amounts of profits actually retained by Enterprises should be disregarded as they were negligible in context and, in any event, were available for distribution to the College and nobody else.

49. He placed particular reliance on the domestic legislation, submitting that Group 10, Schedule 9, VATA by its terms indicates that there is no inherent objection to an "eligible body" making profits for its members, and to intend systematically to do so, provided that the members are themselves all non-profit making bodies.

50. Mr Thomas contended that this result was sensible and logical and in accord with the purpose of Article 132 of the PVD as interpreted in *Kennemer*, because a group of bodies may be perceived as a unified whole, forming a larger non-profit making entity, in the sense that the group's profits are used for public benefit rather than private gain (as by distribution to natural or legal persons entitled to retain distributed profits for their own benefit). He submitted that in a case such as the present, the use of subsidiaries has been effectively forced on the College since, being a charity, it cannot engage in non-primary purpose trading (whether or not for a profit).

51. He submitted that the evidence showed that all the profits made by the College and its subsidiaries had been applied in the furtherance of one or more of the public benefits provided by them – *viz:* education and sporting services.

52. Mr Shepherd, for HMRC, submitted that on a correct interpretation of the definition of "eligible body" in Note (2A) to Group 10, Schedule 9, VATA, a body must, as a threshold condition, be a 'non-profit making body'. He submitted that the evidence showed that Developments and Enterprises were not 'non-profit making' bodies and that accordingly they could not be, and were not, "eligible bodies" within the definition and it was not necessary even to consider paragraphs (a), (b) and (c) of Note (2A) or Notes (2B) and (2C).

53. He expanded this submission by contending that a body which intended or aimed to achieve a surplus in a business activity (an excess of revenues over expenses, costs and taxes needed to sustain the supplies) was not a 'non-profit making body' because that profit accrues to the owner of the business who may or may not decide to reinvest it in the business.

54. He contrasted the above position (that of Developments and Enterprises) with the case of a body which does not set out to achieve the surplus referred to. In such a case, the body would be a 'non-profit making body' and the question of whether or not it was an "eligible body" would be determined by whether the conditions in paragraphs (a), (b) and (c) of Note (2A) were satisfied.

55. He submitted that this interpretation reflects the provisions of Article 133(a) of the PVD. He accepted that Article 133 provided an option for Member States to impose the conditions to which the granting of exemptions would be subject, but he submitted that the optional condition – that bodies other than those governed by public law must not systematically aim to make a profit, and any surpluses nevertheless arising must not be distributed, but must be assigned to the continuance or improvement of the services supplied – had in fact been implemented within UK domestic legislation by the enactment of Note (2A) to Group 10, Schedule 9, VATA.

56. Mr Shepherd submitted that the Memorandum and Articles of Developments and Enterprises at the relevant times showed that they each had the objects of a profit-making company. This was reflected in their financial statements. The overall business activities of Enterprises had to be considered (in accordance with *Kennemer*, Judgment [21]).

Discussion and Decision

57. The first point we address is the construction of Note (2A) to Group 10, Schedule 9, VATA.

58. In the absence of a definition of 'non-profit making body' for the purposes of Note (2A) and Note (2B) of Group 10, Schedule 9, VATA, the Tribunal must ascertain the meaning of the term from the statutory context (*viz:* Notes (2A) and (2B) and also the guidance given by the Court of Justice in *Kennemer* as to the meaning of 'non-profit making organisation' for the purposes of Article 132(1)(m) PVD which Item 3 of Group 10 (together with Notes (2A) and (2B)) is intended to implement.

59. We do not accept that, as Mr Shepherd submits, it is permissible to construe Note (2A) by effectively stopping reading the Note at the mention of 'non-profit making body' and giving an extraneous meaning to that phrase without regard to the subsequent provisions of Note (2A) – never mind Note (2B).

60. In construing Notes (2A) and (2B) we must endeavour to ascertain the legislative purpose behind the use of the term 'non-profit making body' from the context of Notes (2A), (2B) and (2C) read together as a whole, bearing in mind that they were enacted as a whole.

61. So reading Notes (2A), (2B) and (2C), we agree with Mr Thomas that it is evident that Parliament's purpose in adopting the phrase 'non-profit making body' was to refer to a body not subject to commercial influence (a matter to be ascertained by references to Notes (4) to (17)) which may or may not aim to make a profit. Any profit it makes, however, either must not be distributed or may only be distributed to a non-profit making body, or must be applied in the continuance or improvement of the facilities referred to in Note (2B) or for the purposes of a non-profit making body.

62. The guidance in *Kennemer*, however, while making it plain that it is permissible for a 'non-profit making organisation' to aim systematically to achieve surpluses ('*bénéfices*'), does emphasise that an organisation having the aim of achieving financial advantages for its members through distributing profits ('*profits*') in any way does not come within the categorisation of 'non-profit making' (Judgment [33]).

63. It appears therefore either that the concept of a 'non-profit making body' being allowed to distribute any profit it makes (and aims to make) by means of a distribution to a non-profit making body – which is certainly contemplated by Note (2A) construed according to its terms – is either contrary to the essence of a 'non-profit making organisation' in Community law as it has been interpreted, or is an extension – maybe permissible – of the Community law meaning of the term as laid down in *Kennemer*.

64. We add here that we do not discern from *Kennemer* any similar bar to a 'non-profit making organisation' applying its profits for the purposes of (another) non-profit making organisation – as is permitted by Note (2A)(b) and Note (2B)(b). That would not amount to aiming to achieve financial advantages for the first organisation's members, at any rate in a case where the second organisation was not a member of the first organisation.

65. If it was necessary to determine whether by Note (2A)(a) the UK has legitimately extended the meaning of 'non-profit-making organisation' as interpreted in *Kennemer*, it might be appropriate for the Tribunal to refer a suitable question to the Court of Justice.

66. However it is not necessary to determine this question because in any event, as Mr Thomas submitted, the College can rely on the terms of Note (2A)(a) as enacted.

67. The three elements (a), (b) and (c) describing attributes of a non-profit making body in the definition of "eligible body" in Note (2A) are cumulative. They must all be present for a non-profit making body to be an "eligible body".

68. In construing the definition we do, however, consider that a threshold issue arises, although it is a different threshold issue from the crucial one identified by Mr Shepherd. The threshold issue we have identified is on what basis the Tribunal is to ascertain whether or not a particular body (here Enterprises and Developments) is precluded from distributing any profit it makes, or is allowed to distribute any such profit by means only of distributions to a non-profit-making body in terms of Note (2A)(a).

69. On this point the guidance of the Court of Justice in *Kennemer* is that we must determine this question having regard to the objects of the organisation in question as defined in its constitution and in the light of the specific facts of the case (Judgement [27]). In this paragraph the Court of Justice appears to have endorsed the Advocate-General's reasoning in paragraphs [46] and [47] of his Opinion. In those paragraphs Advocate-General Jacobs said this:

> '46. … the focus must be on the aims of the organisation concerned rather than on its results – the mere fact that an entity does not make a profit over any given period is not enough to confer non-profit-making status. Moreover, from the fact that 'non-profit-making' is used to qualify 'organisation', it would seem that the aims in question are those which are inherent in the organisation rather than those which it may be pursuing at a particular point in time.
>
> 47. When assessing those aims, therefore, it is necessary but not sufficient to look at the organisation's express objects as set out in its statutes. It is also necessary however to examine whether the aim of making a distributing profit can be deduced from the way in which it operates in practice. And in that context it in not enough to look simply for an overt distribution of profits in the form of, say, a direct return on the investment represented by contributions to the organisation's assets. Such distributions might also, at least in some circumstances, take the form of unusually high remuneration for employees, redeemable rights to increasingly valuable assets, the award of supply contracts to members, whether or not at process higher than the market rate, or the organisation of sporting 'competitions' in which all members won prizes. No doubt further methods of covert distribution can be devised.'

70. In our judgment, the guidance makes it clear that 'the objects of the organisation in question as defined in its constitution' are the primary – and indispensable, even if not necessarily sufficient – source from which to ascertain the aims of the organisation, bearing in mind that its aims are to be contrasted with its results.

71. It is at this point that we consider that the College's argument breaks down. Mr Thomas accepts – as he must – that in the relevant periods the Memorandum of Association and Articles of Association of Enterprises did not contain any specific prohibition on the distributions of profits. (The same applies to The Memorandum and Articles of Developments.)

72. Mr Thomas invited us to concentrate on the specific facts of the case (having regard to *Kennemer*, Judgment [27]). He emphasised that Enterprises (and Developments) had at all material times been wholly-owned subsidiaries of a non-profit making organisation, namely the College. He also laid great store on the obligation on Enterprises (and Developments) to apply its profits by gifting them under deed of covenant to the College.

73. We accept that these are relevant specific facts – and we shall have something to say about them in the next paragraphs – but it is clear from *Kennemer* that reference to such specific facts cannot be a substitute for reference to the constitution of an organisation. Reference to such specific facts is necessary to ensure that the non-profit making aims of the organisation as stated in its constitution are in fact carried out in practice.

74. As to the fact that Enterprises and Developments are and have been at all relevant times wholly-owned subsidiaries of the College, this is, of course, a fact that could

have changed at any time. If the College had wished to dispose of its holdings in Enterprises and Developments to a commercial organisation, there would have been nothing Enterprises or Developments could have done to prevent it. If that had happened, then, subject to the efficacy of the Deeds of Covenant in favour of the College, there would have been nothing to prevent a situation arising where any profits ('*profits*') of Enterprises and Developments would have been distributable to the financial advantage of its new members – indeed its new members could be expected to ensure that such distributions were made to them.

75. We accept that the College did not dispose of its holdings in Enterprises and Developments and that it never had any intention of doing so, but we do not regard that 'specific fact' as obviating the necessity of the constitutions of Enterprises and Developments containing appropriate restrictions on distribution, which they did not.

76. As to the relevance of the Deeds of Covenant, we again accept that it is a 'specific fact' that the Deeds were entered into and that Enterprises and Developments regarded themselves as bound to pay up all (or almost all) of their taxable profits to the College – and that they did so.

77. Again, we do not regard that 'specific fact' as obviating the necessity of the constitutions of Enterprises and Developments containing appropriate restrictions on distribution.

78. However, as the argument in the appeal progressed, it became clear that the Deeds did not in fact achieve a binding obligation necessitating the application of the companies' profits for the purposes of the College with the force contended for by Mr Thomas.

79. First, it was clear from the evidence that there was a residue of profit actually retained by Enterprises in the all the years from 2009 to 2013 inclusive (which covered the VAT periods relevant to the appeal). This was despite the obligation apparently stated in the Deed to pay up to the College an annual sum equal to the relevant company's profits as computed for corporation tax purposes or the relevant company's distributable income as defined in paragraph 8(1), Schedule 19, ICTA.

80. Furthermore, the retention of a residue of profit was intentional – to reassure suppliers who might look at the companies' accounts.

81. Secondly, from the Deeds that were produced in evidence it was clear that after 27 August 1997 Developments could unilaterally terminate the obligation under the 1993 Deed at any time. If, as we assume, a similar provision was included in the deed entered into by Enterprises in 1995, then Enterprises could have unilaterally terminated its obligation after 1999. As to the Deed dated 6 May 1998 entered into by Developments, the obligations thereunder remained binding until 31 August 2002 and thereafter could have been unilaterally determined by Developments by written notice to the College. There was no evidence that Enterprises had entered into a similar deed, but, if it had, we assume that similar provisions would have applied.

82. It is to be noted that 31 August 2002 was a full 6 years before the commencement of the VAT periods in issue in the appeal (11/08 to 08/12). We therefore find that there was no binding obligation on Enterprises or Developments in the relevant VAT periods which could not have been unilaterally terminated at any time. This, of course, is also a 'specific fact' which is relevant in ascertaining whether or not Enterprises and Developments were precluded from distributing any profit they made. It suggests that in the relevant VAT period they were not so precluded.

83. On analysis, the only point of any force remaining to support Mr Thomas's argument that Enterprises and Developments were in the relevant VAT periods non-profit-making bodies satisfying the conditions in Note (2A), Group 10, Schedule 9, VATA is that they were both companies wholly owned by the College and the College never had any intention of disposing of its ownership interests in them. But, as we have said above, we do not regard that 'specific fact' as obviating the necessity of the constitutions of Enterprises and Developments containing appropriate restrictions on distribution, which they did not. We consider that in reality the focus of Mr Thomas's argument was on the results of Enterprises and Developments, rather than on their aims – *cf* Advocate-General Jacobs's Opinion in *Kennemer* at [46].

84. Finally, although it does not affect our decision, we will state that in our view the UK has not adopted or implemented in Group 10, Schedule 9, VATA the optional condition contained in Article 133(a) of the PVD.

85. For the reasons stated above, we hold that neither Enterprises nor Developments was an "eligible body" for the purposes of Group 10, Schedule 9, VATA in the relevant VAT periods (11/08 to 08/12) and we dismiss the appeal.

Further appeals

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

JOHN WALTERS QC
TRIBUNAL JUDGE

RELEASE DATE: 22 January 2015