[2021] UKFTT 0052 (TC)

TC08038

VAT – HMRC refusal of application to cancel VAT registration - whether supplies made in restaurant were closely related to exempt supplies of education – held yes – decision to refuse to cancel registration unreasonable – appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2018/07409

BETWEEN

STEP BY STEP (NORTHERN IRELAND) LIMITED **Appellant**

-and-

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

TRIBUNAL: JUDGE JEANETTE ZAMAN

The Tribunal determined the appeal on 22 January 2021 without a hearing with the consent of both parties under the provisions of Rule 29 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. A hearing was not held because of the ongoing restrictions resulting from the COVID-19 pandemic. The documents to which I was referred are described in the decision notice.

DECISION

INTRODUCTION

1. This is an appeal by Step By Step (Northern Ireland) Limited ("SBS") against HMRC's refusal to cancel its VAT registration.

2. SBS is a charity which had registered for VAT in 2011. It applied for that registration to be cancelled on 20 February 2018 on the basis that it did not make any taxable supplies. HMRC refused that application, concluding that the supplies of education and vocational training made by SBS were outside the scope of VAT (rather than exempt) as they were grant-funded and that the supplies made by a restaurant operated by SBS were not closely related to any supply of education or vocational training in any event.

3. For the reasons set out below I have concluded that the provision of training by SBS is an exempt supply of education or vocational training and that the supplies made by the restaurant were closely related to that exempt supply and were accordingly exempt. SBS no longer needed to be registered for VAT and HMRC's refusal to cancel that registration was unreasonable. The appeal is allowed.

PAPERS AND EVIDENCE

4. I had a hearing bundle of 267 pages and a bundle of authorities of 38 pages. The hearing bundle included the Notice of Appeal, HMRC's statement of case dated 29 November 2019, correspondence between the parties (which included extracts from the Charity Commission website and papers on qualifications in the hospitality and catering industry) and the accounts of SBS for the year ended 29 February 2016.

5. The index to the hearing bundle listed the accounts of SBS for the years ended February 2016, February 2017 and February 2018. Those for the years ended February 2017 and February 2018 were not included in the hearing bundle which had been sent to me. In response to my direction to provide the same, HMRC provided those to the Tribunal on 8 February 2021.

6. Furthermore, the Tribunal was aware of the decision of the Upper Tribunal in *Colchester Institute Corporation v HMRC* [2020] UKUT 368 (TCC) which was released on 22 December 2020 (after the papers were put together for this appeal). I directed that the parties should provide any written representations which they wanted to make on that decision. HMRC provided written representations on 16 February 2021.

7. Thus whilst this appeal was listed to be determined by me on the papers on 22 January 2021, my decision takes account of the papers described above which I received after that date.

FACTS

8. SBS is a company limited by guarantee and registered as a charity with the Charity Commission of Northern Ireland which runs the One Eighty Restaurant (the "Restaurant").

9. SBS registered for VAT as an "intending trader" with an effective date of registration of 1 February 2011.

10. On the website of the Charity Commission for Northern Ireland, under "what your organisation does" ,it is stated "Step by Step NI Ltd operates the One Eighty Degrees Restaurant as a not for profit social enterprise. The restaurant is used as a training environment for young people with learning disabilities to give them the qualifications, skills and experience to gain meaningful employment in the hospitality industry…". The charity's classifications include the advancement of education.

Provision of training by SBS

11. SBS supplies training services under an agreement with Southern Regional College (the "College" or "SRC") dated 1 August 2017 (the "Training Services Agreement"). There was no evidence as to whether this agreement had been entered into following a change in the activities of SBS or whether it reflected the status quo. In any event, I note that the application to cancel its VAT registration was made by SBS after this agreement had been entered into.

12. The Training Services Agreement includes the following provisions:

(1) Background – SBS has been engaged to provide training services on behalf of SRC.

(2) The definitions include that of a "Participant", which is defined as "those students of SRC".

(3) Clause 2 (Commencement and Duration) – This provides that SBS will "provide the Services to the College" on the terms of the agreement, whether they were carried out before, on or after the date of the agreement. Clause 2.3 requires that SBS enrol and register participants within the current lifetime of the existing Training for Success 2017 programme.

(4) Clause 3 sets out SBS's responsibilities:

(a) Clause 3.1 requires SBS to provide the services in accordance with Schedule 1 and by doing so shall achieve the Target (defined by reference to the performance standards in Schedule 2), and shall allocate sufficient resources to the Services to enable it to comply with this obligation.

(b) Clause 3.2 requires SBS to meet any performance dates specified in the Target, and operate within the current Training for Success 2013 Operational Guidelines and the Training for Success 2017 Operational requirements.

(5) Clause 5 addresses charges and payments:

(a) Clause 5.1 provides that "In consideration of the provision of the Services by the Provider, the College shall pay the charges as set out in Schedule 3."

(b) There are then provisions for timing of payments and stating that the College will not accept any additional costs that have not been included in the agreement.

(6) Clause 6 includes a warranty that SBS will perform the Services with the best care and skill and in accordance with generally recognised commercial practices and standards and in accordance with the target and performance standards set out in Schedule 2.

13. Schedule 1 sets out the Services, and specifies the requirements of the Training for Success 2013 and Training for Success 2017 programmes:

(1) Training for Success 2013 – The programmes deliverable under this agreement are the delivery of the Skills for Work (Disabled) strand of Training for Success 2013.

(a) The components to be provided by SBS are specified, and they include professional and technical skills qualifications, personal and social development and employability skills.

(b) SBS is also to provide the service of recruitment of Participants to these programmes in conjunction with the College, an induction programme,

completion of personal training plans, ongoing monitoring and review of Participants, completion of a progress file, access to a work placement, and career advice and guidance.

(2) Training for Success 2017 – The components and additional services are broadly as set out above.

(3) The programme delivered under this agreement will be subject to the same quality control and all applicable external standards as all other College programmes.

(4) SBS will provide "on course" support and assistance to Participants with identified needs that may arise before or after the course has commenced. This includes ensuring Participants have support in a non-threatening environment, providing information on additional learning support available in the College and support with the management of learning.

(5) SBS must liaise with the College, including regular meetings with College staff and participate in progress reviews.

14. Schedule 2 sets out the performance standards, which differ between Training for Success 2013 and Training for Success 2017. For Participants enrolled in Training for Success 2013, SBS must ensure a minimum of 65% of all starters achieve all the agreed targeted qualifications described in their personal training plan. The performance of SBS is to be monitored and reviewed against specified guidelines. For Participants enrolled in Training for Success 2017, a table sets out targets for retention, achievement, compliance and service quality. There are then provisions for performance monitoring.

15. Schedule 3 deals with Pricing. That provides:

> "1. In each Claim Period SRC shall, and upon receipt of any necessary documentation, calculate the amount due to the Provider in respect of the Services provided. SRC shall advise the Provider of the amount due to it, which will equate to 80% of the DFE Funding Allocation. The Provider shall then issue an invoice to SRC for such amount as notified to it and SRC will make such payments in accordance with clause 5.2.
>
> 2. The Provider hereby acknowledges and agrees that SRC may make payments to the Provider for the provision of Services prior to receiving the DFE Funding Allocation…
>
> …
>
> 4. If part of the training is carried out (E.g. Essential Skills) by Southern Regional College, the college will deduct a full cost recovery rate for training delivered and resources deployed."

16. A "Claim Period" is a period of four weeks. "DFE Funding Allocation" means the funding due to SRC from the Department for Economy, Northern Ireland in respect of the provision of Services to the Participants.

Operation of the Restaurant

17. The Restaurant is staffed by both students and employees of SBS. Its customers are members of the public.

Financial statements of SBS

18. Whilst noting that SBS did not apply for the cancellation of its VAT registration until February 2018, I have considered all three sets of accounts which were provided.

19. The Trustees' Annual Report included as part of the accounts for the year ended 29 February 2016 addresses the number of trainees on the programme (there were 17 from September 2015), implementation of a new training structure and SBS' work with other societies. It explains that there was a reduction in recruitment that year due to a reduced number of school leavers with learning support needs and the specific eligibility requirements of the Training for Success programme. The project operated by SBS is an accredited training centre with ABC Awards and Open College Network NI – this enables the project to deliver the qualification requirements.

20. The Financial Review in that report refers to a backdrop of limited resources and insecurities over funding. The principal funding sources are described as income generated by the café operations and income per trainee from the Department of Employment and Learning. The charity was seeking funding from a much broader group of bodies as well as plans to increase the programmes on offer and the number of trainees attending.

21. The financial statements show "Salaries & Wages" of £62,101 for restaurant trading and £73,453 for provision of training, totalling £135,554 (against a total of £143,875 for 2015)

22. The Trustees' Annual Report for the year ended 28 February 2017 refers to SBS's decision to merge with Enable NI, another organisation operating in the same geographical area with a similar group of beneficiaries. The report states that a plan had been devised to increase the revenue in restaurant trading, increase training income through an increased number of trainees and increase applications for funding to grant-making trusts and foundations.

23. The Financial Review refers to there being a significant deficit of £40,000 for that year, resulting from a loss of revenue from both the Restaurant and SRC in terms of training income.

24. The statement of financial activities sets out the "incoming resources" for the year, which is made up of donations (unrestricted and restricted) of £5,526 and £12,997 respectively, restaurant trading of £110,740 and provision of training of £70,213. The notes include an analysis of the movement on funds from 2016 to 2017 and show that as at 1 March 2016 there had been donations from NIE of £200, Armagh, Banbridge & Craigavon Council of £1,278 and Lidl in the Community of £1,000. During the year ended February 2017 £9,480 had been received from Awards for All Northern Ireland and a further £3,517 from the local council. These two amounts made up the amount recorded as restricted donations.

25. I only had a copy of a draft of the accounts for the year ended 28 February 2018, although neither party made any representations that they would be unreliable for this reason.

26. The Financial Review in the Trustees' Annual Report refers to there being a deficit of £14,000 which had resulted primarily from one-off redundancy costs and the timing of grant expenditure. Incoming resources are listed as donations of £21,318 and £10,000, restaurant trading of £100,515 and provision of training of £87,038. The analysis of the movement on funds shows a restated balance at 1 March 2017 of £9,480 from the Big Lottery Fund (which I infer is the same as Awards for All Northern Ireland) and £200 from NIE. During the year a further £10,000 was received from the local council.

27. These three sets of accounts, and the provisions of the Training Services Agreement, show that SBS was receiving income from three sources:

(1) The operation of the Restaurant – this was the biggest contributor each year.

(2) The provision of the training – on the basis of the Training Services Agreement, I infer that these amounts were those paid to SBS by SRC in accordance with Schedule 3 of that agreement, and were thus indirectly funded by the Department for Economy, Northern Ireland. This was the second largest contributor.

(3) Other grants, including from the local council and the Big Lottery Fund.

Application to cancel VAT registration

28. On 20 February 2018 SBS applied to de-register for VAT. The application form states that its supplies were solely or mainly zero-rated and SBS wanted to apply for exemption from VAT registration. In the text box, it is stated that the Restaurant was established in 2011 as an educational/vocational training establishment for young people with learning disabilities. The environment is used to train and educate trainees giving them the opportunity to develop their skills and experience whilst undertaking qualifications for employment in the hospitality industry. It added that SBS should never have been registered for VAT. That form was signed by Nigel Hampton of SBS.

29. HMRC have (correctly) treated SBS as arguing that its supplies are exempt (not zero-rated).

30. On 16 April 2018, HMRC refused the application to de-register SBS for VAT, on the basis that it was not possible to determine from the information available, including previous VAT returns, that the company was eligible to de-register. HMRC also confirmed that the company should continue to account for VAT.

31. After further correspondence, which included HMRC again refusing de-registration on 13 June 2018, SBS requested a review of this decision and on 8 October 2018 HMRC upheld the decision in a Review Conclusion Letter. SBS gave Notice of Appeal to the Tribunal on 20 November 2018.

RELEVANT LEGISLATION

32. Article 2 of the Principal VAT Directive (Council Directive 2006/112/EC) sets out the transactions which are subject to VAT:

> "Article 2
>
> 1. The following transactions shall be subject to VAT:
>
> (a) the supply of goods for consideration within the territory of a Member State by a taxable person acting as such;
>
> …
>
> (c) the supply of services for consideration within the territory of a Member State by a taxable person acting as such;"

33. So far as material, Article 9 defines "taxable persons" for these purposes as follows:

> "TAXABLE PERSONS
>
> Article 9
>
> 1. 'Taxable person' shall mean any person who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity.
>
> Any activity of producers, traders or persons supplying services, including mining and agricultural activities and activities of the professions, shall be regarded as 'economic activity'. The exploitation of tangible or intangible property for the purposes of obtaining income therefrom on a continuing basis shall in particular be regarded as an economic activity."

34. Title IX of the Principal VAT Directive provides for exemptions from VAT in respect of supplies of certain goods and services. Chapter 2 of Title IX makes provision for exemption of activities in the public interest. Articles 132 to 134 provide (so far as relevant):

> "Article 132
>
> 1. Member States shall exempt the following transactions:
>
> …
>
> (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;
>
> …
>
> Article 133
>
> Member States may make the granting to bodies other than those governed by public law of 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
>
> …
>
> Article 134
>
> The supply of goods or services shall not be granted exemption, as provided for in points (b), (g), (h), (i), (l), (m) and (n) of Article 132(1), in the following cases:
>
> (a) where the supply is not essential to the transactions exempted;
>
> (b) where the basic purpose of the supply is to obtain additional income for the body in question through transactions which are in direct competition with those of commercial enterprises subject to VAT…"

35. Section 2 VATA 1994 implements Article 2. It states:

> "2. Value added tax
>
> (1) Value added tax shall be charged, in accordance with the provisions of this Act –
>
> (a) on the supply of goods or services in the United Kingdom (including anything treated as such a supply)…"

36. Section 4 VATA 1994 sets out the scope of taxable supplies and s5 sets out the meaning of supply:

> "4. Scope of VAT on taxable supplies
>
> (1) VAT shall be charged on any supply of goods or services made in the United Kingdom, where it is a taxable supply made by a taxable person in the course or furtherance of any business carried on by him.
>
> (2) A taxable supply is a supply of goods or services made in the United Kingdom other than an exempt supply.
>
> …

5. Meaning of supply: alteration by Treasury order.

(1) Schedule 4 shall apply for determining what is, or is to be treated as, a supply of goods or a supply of services.

(2) Subject to any provision made by that Schedule and to Treasury orders under subsections (3) to (6) below—

(a) "supply" in this Act includes all forms of supply, but not anything done otherwise than for a consideration;

(b) anything which is not a supply of goods but is done for a consideration (including, if so done, the granting, assignment or surrender of any right) is a supply of services.

…"

37. Exemption is provided for by s31(1) VATA 1994:

"A supply of goods or services is an exempt supply if it is of a description for the time being specified in Schedule 9 and an acquisition of goods from another member State is an exempt acquisition if the goods are acquired in pursuance of an exempt supply."

38. Schedule 9 provides (so far as relevant):

"Group 6 – Education

Item No

1. The provision by an eligible body of –

(a) education;

…or

(c) vocational training.

…

4. The supply of any goods or services (other than examination services) which are closely related to a supply of a description falling within item 1 (the principal supply) by or to the eligible body making the principal supply provided –

(a) the goods or services are for the direct use of the pupil, student or trainee (as the case may be) receiving the principal supply; and

(b) where the supply is to the eligible body making the principal supply, it is made by another eligible body.

…

NOTES

(1) For the purposes of this Group an "eligible body" is-

…

(e) a body which –

(i) is precluded from distributing and does not distribute any profit it makes; and

(ii) applies any profits made from supplies of a description within this Group to the continuance or improvement of such supplies.

…

(3) "Vocational training" means –

Training, re-training or the provision of work experience for –

(a) any trade, profession or employment; or

(b) any voluntary work connected with –

(i) education, health, safety, or welfare; or

(ii) the carrying out of activities of a charitable nature."

39. Paragraph 3(a) of Schedule 1 VATA 1994 provides that "a person who has become liable to be registered under this Schedule shall cease to be so liable at any time if the Commissioners are satisfied in relation to that time that he—(a) has ceased to make taxable supplies"

40. Paragraph 13 of Schedule 1 provides:

> "13(1) Subject to subparagraph (4) below, where a registered person satisfies the Commissioners that he is not liable to be registered under this Schedule, they shall, if he so requests, cancel his registration with effect from the day on which the request is made or from such later date as may be agreed between them and him.
>
> (2) Subject to subparagraph (5) below, where the Commissioners are satisfied that a registered person has ceased to be registrable, they may cancel his registration with effect from the day on which he so ceased or from such later date as may be agreed between them and him.
>
> (3) Where the Commissioners are satisfied that on the day on which a registered person was registered he was not registrable, they may cancel his registration with effect from that day.
>
> (4) The Commissioners shall not under subparagraph (1) above cancel a person's registration with effect from any time unless they are satisfied that it is not a time when that person would be subject to a requirement to be registered under this Act.
>
> (5) The Commissioners shall not under subparagraph (2) above cancel a person's registration with effect from any time unless they are satisfied that it is not a time when that person would be subject to a requirement, or entitled, to be registered under this Act.
>
> …"

41. Section 83(1)(a) VATA 1994 provides that an appeal lies to the Tribunal with respect to the registration or cancellation of registration of any person.

SUMMARY OF PARTIES' SUBMISSIONS

42. SBS's grounds of appeal (set out in its Notice of Appeal) can be summarised as follows:

(1) SBS supplies training for SRC under the Training Services Agreement, and as part of this it provides work-based education and training through the operation of the Restaurant;

(2) SBS's supplies of training fall within item 1(a) or (c) of Group 6, Schedule 9 VAT Act 1994;

(3) the supplies made by the Restaurant are exempt within item 4. The training services are provided as a business activity, the activity in the Restaurant is essential to

the education or vocational training and otherwise satisfies the criteria in *Brockenhurst*; and

(4) SBS is entitled to deregister for VAT in accordance with paragraph 3(a) of Schedule 1 VAT Act 1994 as it does not make taxable supplies for VAT purposes.

43. HMRC's position (in their statement of case and written submissions of 15 February 2021) is that:

(1) as the education provided by SBS is fully grant-funded, though not ultimately government funded, it is not a supply made in the course or furtherance of business and therefore outside the scope of VAT. The students make no payment towards the education;

(2) SBS has produced no evidence to satisfy the direct link test set out in the decision in *Colchester*;

(3) as there is no underlying supply of education (in the course or furtherance of business), the Restaurant's supplies cannot be "closely related" to such a supply; and

(4) even if there were an underlying supply of exempt education, SBS's catering supplies would not meet the criteria in *Brockenhurst*.

44. The Tribunal's directions of 12 September 2020 required the parties to outline any factual assertions made by the other party which the party replying does not accept.

45. HMRC replied on 18 September 2020:

> "The Appellants assert that they are entitled to de-register for VAT based on supplies of food from their café being exempt, as they are "closely related" to supplies of education. The Respondents do not accept this. The education is fully grant-funded and therefore outside the scope of VAT. The supplies of food made by the café are therefore not "closely related" to a supply of education as there is no such supply. Consequently the supplies made by the café are not exempt, and in any case the café is in competition with other businesses."

46. SBS acknowledged the Tribunal's directions, replying to other questions raised therein, and simply said "The Appellant reserves the right to make additional submissions to the Tribunal in relation to this case." That email was sent on 18 September 2020 and no further submissions have been received.

DISCUSSION

47. SBS applied for its VAT registration to be cancelled. Paragraph 13 of Schedule 1 VATA 1994 requires that SBS satisfies the Commissioners of HMRC that it is not liable to be registered. Having failed to so satisfy the Commissioners (as can be seen from the refusal letters of 16 April 2018 and 13 June 2018, and the review conclusion letter of 8 October 2018), an appeal lies to the Tribunal against that refusal to cancel the VAT registration. However, as the decision is that of HMRC, I only have a supervisory jurisdiction – I can only interfere with the decision if it is shown that the decision is one which no reasonable body of Commissioners could reach.

48. SBS applied to cancel its VAT registration on the basis that it "has ceased to make taxable supplies". The activities of SBS involve both the provision of training to students and the operation of the Restaurant.

49. HMRC submit that the provision of training is outside the scope of VAT. This position is relevant to the treatment of both the provision of training itself and the operation of the Restaurant, as HMRC's submission is that the supplies made by the Restaurant cannot benefit

from exemption under item 4 of Group 6 unless there is an exempt supply of education or vocational training within item 1 (rather than one which is outside the scope) and in any event that the activities of the Restaurant are not "closely related". SBS submits that its activities are exempt.

50. HMRC does not dispute that (i) the training in question is education or vocational training which is otherwise capable of falling within item 1 of Group 6, (ii) that it is provided by SBS, or (iii) that SBS is an "eligible body" within note 1(e) of Group 6. I have proceeded to consider SBS' appeal on that basis.

51. The issues which need to be determined are:

(1) whether item 4 only exempts supplies which are closely related to an exempt supply of education or vocational training or if it is sufficient that the supply is closely related to the provision of education or vocational training (even if such provision is outside the scope of VAT);

(2) whether the provision of training by SBS is within the exemption provided for by item 1 of Group 6; and

(3) whether the supplies made by the Restaurant are "closely related" for the purposes of item 4.

Does item 4 require that the provision of education or vocational training be exempt?

52. Given that HMRC accepts that the training provided by SBS is education or vocational training which is otherwise capable of falling within item 1 and that SBS is an eligible body, I have addressed first whether HMRC's first argument (that SBS does not make exempt supplies of education or vocational training) is actually a pre-condition for the supplies made by SBS in the Restaurant to be capable of exemption within item 4.

53. Item 1 itself refers to the "provision" by an eligible body of education or vocational training, and does not specify within it whether such provision must otherwise be a taxable supply. However, item 4 lists "the supply of …services…which are closely related to a supply of a description falling within item 1 (the principal supply) by or to the eligible body making the principal supply…".

54. The definition of a supply in s5 VATA 1994 is somewhat all-encompassing, providing that it "includes all forms of supply, but not anything done otherwise than for a consideration". The use of the word supply thus brings with it the requirement that something is done for a consideration. Section 31(1) VATA 1994 states that a supply is exempt if it is of a description specified in Schedule 9. So item 1 of Group 6 in that Schedule is exempting certain activities that have already met the wide definition of a supply, ie that they are provided for a consideration, notwithstanding that item 1 does not itself use that word.

55. I therefore agree with HMRC that SBS must establish that its provision of education or vocational training is exempt within item 1 in order to be able to argue that the supplies made by the Restaurant can be exempted under item 4.

Is the provision of training by SBS an exempt supply within item 1 of Group 6?

56. HMRC submitted that a body that is grant-funded is not making a supply in the course or furtherance of a business and therefore that its supplies are outside the scope of VAT. Furthermore, addressing (at my direction) the decision of the Upper Tribunal in *Colchester*, SBS had not provided the required evidence to demonstrate a direct link between payments received and a provision of education services.

57. SBS submitted that the Training Services Agreement details various services to be provided in return for consideration and accordingly there is a business supply for VAT purposes.

58. Neither party referred me to any of the case law of the Court of Justice of the European Union ("CJEU") addressing the meaning of economic activity or consideration or the relevance of grant funding, the only cases included in the authorities' bundle being the decision of the CJEU in Case C-699/15 *HMRC v Brockenhurst College* [2017] STC 1112 and that of the Upper Tribunal in *Loughborough Students' Union v HMRC* [2018] UKUT 0343 (TCC).

59. The recent decision of the Upper Tribunal in *Colchester* is both relevant and binding on me. Colchester Institute Corporation ("CIC") is a further education corporation providing further and higher and education and vocational training programmes to over 11,000 students. The appeal before the Upper Tribunal concerned whether the provision of education and /or vocational training by CIC provided free of charge to students and funded by grants from two government funding agencies was a "supply of services for consideration" for the purposes of Article 2(1)(c) Principal VAT Directive and if so whether it is an "economic activity" for the purposes of Article 9.

60. By the time of the hearing before the Upper Tribunal the scope of the appeal had narrowed to a single question, namely whether there was "a supply of services for consideration". HMRC had accepted that, if the Upper Tribunal were to conclude the activities were "supplies of services for consideration" within Article 2, no issue would arise in relation to "economic activity" which was established on the facts. Conversely, if there was no "supply for consideration", as the Tribunal had held, that would be an end of the matter because necessarily this would amount to non-business activity (on the basis of *Wakefield College*).

61. As with this appeal, it had not been in dispute that CIC was an "eligible body" or that the courses it provided were "education" or "vocational training". The arrangements for grant funding were described as follows:

> "18. At the relevant times, CIC was funded primarily by three government agencies: the Skills Funding Agency ('SFA'), the Education Funding Agency ('EFA') 6 and the Higher Education Funding Council for England ('HEFCE'). The appeal relates to courses funded by the EFA and SFA, referred to the in the Decision collectively as 'the funding agencies'. The EFA funds the provision of education and vocational training for students aged 19 and under, certain categories of students aged over 19, and students with learning difficulties aged between 19 and 25. The SFA funds all or part of the provision of education and vocational training for students aged 18 and over who have not achieved a specified level of academic qualification, or who are entitled to free education or training ([31]-[33]).
>
> 19. CIC receives tuition fees for other students who are not eligible for EFA, SFA or HEFCE funding ([35]).
>
> 20. CIC's annual income is approximately £40m. EFA funding amounts to approximately £19.7m; SFA funding, to approximately £4.7m; HEFCE funding, to approximately £7.5m. Fees charged to international students who are not entitled to EFA, SFA or HEFCE funding amounts to approximately £700,000. CIC also generates approximately £3.7m income per annum from activities other than the provision of education and vocational training (including rental of studio and other space) ([30] and [32]-[36]).

> 21. CIC enters into agreements with the EFA and the SFA each year in relation to the funding the agencies provide. The agreements are in standard form, are not negotiable, and incorporate by reference a series of other documents which collectively set out the basis on which funding is provided and the obligations placed on the college to deliver education and vocational training. The agreement with the EFA is entitled 'Conditions of Funding Agreement'; the SFA agreement, 'Financial Memorandum' ([37]-[38]).
>
> …
>
> 29. The funding summary exhibit to Gary Horne's witness statement elaborates on the funding process as follows. In January/February of each year the SFA uses current performance data to inform the calculation of allocation for the following year. Colleges are required by the SFA to submit a funding claim based on in year performance from the February return. Colleges are required to project forward based on their current enrolment and assumptions on likely retention rates using historical trends. Then in March the SFA sends its funding allocation statement for the following year. There is generally a caveat to state the allocations are subject to change ahead of the year commencing so for example on 28 July 2015 the allocation was reduced by 3% ahead of the 1 August start date. From August onwards SFA sends the final allocation. Variations through the year are also sent where in-year over- performance or under- performance can be reflected in increased or decreased allocations for apprenticeships subject to business case reviews.
>
> 30. Where students are fully funded by the EFA or the SFA, the fee set out on the Receipt is the baseline funding amount per student for that course. The actual amount paid for that student by the funding agencies will depend on their respective funding formulae. The actual funding received by CIC from the EFA to deliver its courses could be more or less than the aggregate of the amount stated on the Receipts issued for EFA funded courses. Similarly, the amount received by CIC from the SFA (together with any fees charged to the student) in any year would not exactly match the aggregate shown on the Receipts issued in respect of SFA funded courses ([50]-[51]).”

62. In setting out the relevant law, the Upper Tribunal noted (at [46]) that it was clear that consideration can be third party consideration, ie paid by a person who is not the recipient of the supply, citing case law which referred to the “need for a direct link between the service provided and the consideration received”. Moreover, third party consideration can be in the form of a subsidy paid from public funds, so long as the subsidy bears a direct link with the goods or services at issue.

63. The Upper Tribunal concluded that there was a direct link between the funds coming into CIC and the courses provided to students for free; in consequence, there was a supply of services for consideration. They considered that the agreements between the funding agencies and CIC were “key to the analysis”:

> “76. … There are four important features of the agreements, in our judgement, which provide the answer to the question.
>
> 77. First, although the agreements did not state in terms which courses CIC was to provide, they did restrict the funding to courses within a list on the Government's website. The essence was that the funding was for those courses; CIC was not at liberty to do anything else with the money.
>
> 78. Secondly, the amount paid was by way of formula and not negotiated. (There was some room for negotiation if larger student numbers were anticipated for some reason, but that did not arise in the periods considered

> by the FTT and that anyway was an exception to the general rule.) The use of a formula is not itself a basis for concluding that the payments are not consideration, as *Rayon d'Or* shows. But in this case, the components of the formula give clues as to what the grant payment were for. The starting point was a "per student" amount (of £4,000); the number of students was based on the last year's intake, used as a proxy for the expected number of students in the current year; there were a number of adjustments to be made which related to the courses themselves – mostly reflecting the higher costs of providing courses (or certain types of courses) to students within the catchment of CIC. The formula was therefore highly specific to CIC's outputs – to the number of students, the type of students, the number of courses and the type of courses.
>
> 79. Thirdly, one way or another, CIC would have to pay back any part of the grant funding which was not used for supplying the courses as anticipated at the beginning of the year. ...
>
> 80. Fourth, in order to give the funding agencies full sight of its activities, and to permit accurate application of the relevant funding formulae, CIC submitted an ILR for each student on a monthly basis, comprising over 200 fields of data for each student. The ILRs were required under the agreements. By them, the funding agencies were given detailed information about how the funds are being spent by CIC. With that information, the funding agencies were able to adjust their payments to match that data and according to the standard formula. With that information, the funding agencies were able to see how their grant funding had been spent.
>
> 81. Taken together, we conclude that these features, all contained within the agreements, seen in context, indicate the existence of a direct link between the grants coming into CIC and the courses provided to CIC's students for free. We accept, of course, that the link could have been more direct than it was: the funding was not specific to any particular course or courses, it did not reflect the specific costs of any particular course, nor did it identify the particular students who would take those courses. But the law does not require such a degree of specificity; the concept of "direct link" encompasses a range of possibilities."

64. HMRC submitted that SBS has not provided any evidence in relation to the conditions which they must fulfil in order to obtain their grant funding and that without sight of the relevant documentation it will be impossible to ascertain whether SBS can satisfy the direct link test established in *Colchester*.

65. In *Colchester* the provisions of the funding agreements were key to the Upper Tribunal's analysis. HMRC are correct to note that here I do not have any evidence as to the basis on which grants were made to SBS. However, I do not consider that this is determinative of the issue. That overlooks the fact that the grants were only one of three sources of income of SBS (and the smallest source by a considerable margin). Furthermore, the approach taken by the Upper Tribunal is to assess the features of the funding agreements, taken together and seen in context, acknowledging that the concept of a "direct link" encompasses a range of possibilities.

66. The activities of SBS have been described consistently in its registration with the Charity Commission and in its accounts as being the operation of the Restaurant as a training environment for young people with learning disabilities to give them the qualifications, skills and experience to gain meaningful employment in the hospitality industry.

67. The basis on which SBS provides training to students is set out in the Training Services Agreement. The provisions of that agreement could be read as raising a question as to whether or not SBS is itself providing the education or vocational training – it refers to SBS as providing training services "on behalf of" SRC, and Participants are defined as students "of SRC". However, not only has HMRC failed to challenge this point but also I am satisfied, having regard to the activities of SBS and the obligations it has undertaken under the Training Services Agreement (including as to recruitment of students, monitoring of performance and employment of the training staff), that SBS is providing education or vocational training to students.

68. That agreement clearly provides that in consideration for providing these services (namely programmes which satisfy the Training for Success requirements and associated obligations relating to recruitment and ongoing support and assistance) it will be paid an amount by SRC. I have no doubt that this is consideration for the provision of training to students by SBS, and accordingly that this is a "supply" for the purposes of VATA 1994. SBS does have other income (from the restaurant and the grants), but that does not preclude the amounts charged to SRC from being consideration.

69. In *Colchester* HMRC had accepted that if it were found that there were supplies of services for consideration there would be no separate issue as to whether there was economic activity. I did not have the benefit of any submissions on this point. However, having regard to all of the circumstances, including the provision of training to students in return for payment and the operation of the Restaurant (which was open to the public and which HMRC argue in the context of item 4 is in competition with other commercial enterprises) I am satisfied that SBS does carry on an economic activity (for the purposes of the Principal VAT Directive) and carries on a business (for the purposes of VATA 1994). This is irrespective of the fact that as a charity it operates on a not-for-profit basis.

70. I have therefore concluded that the provision of training by SBS is an exempt supply within item 1 of Group 6.

Are the supplies from the Restaurant "closely related" supplies for the purposes of exemption under Item 4?

71. Item 4 exempts the supply of goods or services which are "closely related" to a supply of a description falling within Item 1 (the principal supply) by or to the eligible body making the principal supply provided that the goods or services are for the direct use of the pupil, student or trainee receiving the principal supply.

72. The submissions of the parties focused on the question of whether the supplies by the Restaurant were "closely related" to the supply of education. Neither party addressed the condition in item 4 that the goods or services must be for the direct use of the pupil, student or trainee receiving the principal supply of education. This condition does not derive from Article 132(1)(i) and I have focused on whether the requirements expressly set out in the Principal VAT Directive are met.

73. The question whether supplies are "closely related" to the supply of education or vocational training was addressed by the CJEU in *Brockenhurst College*. Brockenhurst is a higher education establishment which offers courses in catering and hospitality (as well as the performing arts). For the purpose of enabling the students to learn skills in a practical context, the College, through its students acting under the supervision of their tutors, runs a restaurant and stages performances aimed at persons not connected to the establishment. This practical training was designed as part of the courses, and the students were aware of this at the time they enrolled.

74. HMRC in that case argued that item 4 precluded the supply from being exempt as it was not for the "direct use of the student". The CJEU stated:

> "26. In that regard, the application of the exemption for activities 'closely related' to education is, in any event, subject to three conditions, laid down, in part, in Articles 132 and 134 of Directive 2006/112. In essence, first, both the principal supply and the supplies of services closely related to it must be provided by bodies referred to in Article 132(1)(i) of that directive; secondly, those supplies of services must be essential to the exempt activities; and, thirdly, the basic purpose of those supplies of services must not be to obtain additional income for those bodies by carrying out transactions which are in direct competition with those of commercial enterprises liable for VAT (see, to that effect, judgments of 14 June 2007, *Horizon College*, C-434/05, EU:C:2007:343, paragraphs 34, 38 and 42, and 25 March 2010, *Commission v Netherlands*, C-79/09, not published, EU:C:2010:171, paragraph 61).
>
> …
>
> 28 As regards the second condition, it follows from paragraph 39 of the judgment of 14 June in *Horizon College* (C-434/05, EU:C:2007:343), that, in order to be classified as supplies of services essential to the exempt activities, those supplies must be of a nature and quality such that, without recourse to them, there could be no assurance that the education provided by the body referred to in Article 132(1)(i) of Directive 2006/112 and, consequently, the education from which their students benefit, would have an equivalent value. ….
>
> 29. In the present case, it is apparent from the order for reference that the practical training was designed to form an integral part of the student's curriculum and that, if it were not provided, students would not fully benefit from their education.
>
> 30. In that regard, the order for reference notes that the catering functions of the restaurant are all undertaken by students of the College, under the supervision of their tutors, and that the purpose of operating the College's training restaurant is to enable the students enrolled in catering and hospitality courses to learn skills in a practical context.
>
> 31. The same applies to the performing arts courses. The College, through the students enrolled on those courses, stages concerts and performances to enable the students to acquire practical experience.
>
> 32. It must be stated that, without these practical aspects, the education provided by the College in the fields of catering and hospitality and of the performing arts would not have an equivalent value.
>
> 33. That finding is corroborated by the assertion of the United Kingdom of Great Britain and Northern Ireland that the College's training restaurant is tantamount to a classroom for the students, and the assertion of the European Commission that students benefit from preparing meals and performing table service in a real-life setting, which is an important part of their education.
>
> 34. In those circumstances, it appears that the supplies of restaurant and entertainment services at issue in the main proceedings must be regarded as essential to guaranteeing the quality of the principal supply of education provided by the College.
>
> 35 As regards the third condition, it must be noted that that condition is an express enunciation of the principle of fiscal neutrality, which precludes, in

particular, treating similar supplies of services, which are thus in competition with each other, differently for VAT purposes (see, to that effect, judgment of 14 June 2007, *Horizon College*, C-434/05, EU:C:2007:343, paragraph 34 and the case-law cited).

36 In the main proceedings, it is common ground, first of all, that the restaurant and entertainment services provided by the College are open only to people previously registered on a mailing list held by that establishment. In particular, the referring court has stated that, for the performances, the audience usually consists of the friends and family of the College students, as well as people previously registered on the College's database.

37 Further, the College's training restaurant is available only by reservation and upon the condition that it be fully booked, with a minimum of thirty covers being required for the students to obtain maximum benefit from their supply of services. Thus, meals are cancelled if the required threshold is not reached, unlike in a commercial restaurant where reservations are in principle unconditionally honoured.

38 Lastly, it is clear from the information provided by the referring court that the concerts, performances and restaurant services are entirely organised, carried out and supplied by students enrolled at the College, a situation which is fundamentally different from that of students undertaking an internship in a commercial entity, where they join a professional team supplying such services in the competitive conditions prevailing in the respective markets.

39 It thus appears that the services offered by the College, as part of the courses taught to its students, to a limited number of third parties, are substantially different from those habitually offered by a commercial theatre or restaurant and are aimed at a different public, in that they do not meet the same needs of the consumer.

40 Furthermore, it is not disputed that the prices charged by the College cover only 80% of the cost of the meals. It does not therefore appear that the services at issue in the main proceedings are intended to generate additional income for the College by carrying out transactions in direct competition with those of commercial enterprises subject to VAT, such as restaurants or theatres.

41 Consequently, the services offered by the College to a limited number of third parties do not appear to be comparable to those offered by commercial restaurants and theatres, and the exemption from VAT for services supplied by the College does not amount to a difference in tax treatment.

42 Lastly, it must be borne in mind that it is for the national court to ascertain, on the basis of the guidance provided by the Court, that those conditions are indeed satisfied in the light of the factual circumstances of the case before it.

43. In the light of all the foregoing considerations, the answer to the questions referred is that Article 132(1)(i) of Directive 2006/112 must be interpreted as meaning that activities carried out in circumstances such as those at issue in the main proceedings, consisting in students of a higher education establishment supplying, for consideration and as part of their education, restaurant and entertainment services to third parties, may be regarded as supplies ‘closely related’ to the principal supply of education and accordingly be exempt from VAT, provided that those services are essential to the students’ education and that their basic purpose is not to obtain additional income for that establishment by carrying out transactions

> in direct competition with those of commercial enterprises liable for VAT, which it is for the national court to determine."

75. The CJEU thus set out three conditions for application of the exemption based on the requirements of the Principal VAT Directive:

(1) both the principal supply and the supplies of services closely related to it must be provided by bodies referred to in Article 132(1)(i);

(2) those supplies of services must be essential to the exempt activities; and

(3) the basic purpose of those supplies of services must not be to obtain additional income for those bodies by carrying out transactions which are in direct competition with those of commercial enterprises liable for VAT.

76. In the present appeal, although HMRC had disputed that SBS made a relevant principal supply of exempt education, it had not challenged SBS' status as an organisation recognised by the UK as having similar objects to relevant bodies governed by public law. This first condition is therefore satisfied in the light of my earlier conclusion that SBS did make relevant principal supplies.

Are the supplies essential to the exempt activities?

77. As can be seen above, in *Brockenhurst* the CJEU emphasised that:

(1) the practical training was designed to form an integral part of the student's curriculum, and the purpose of operating the training restaurant was to enable students enrolled in catering and hospitality courses to learn skills in a practical context (see [29] and [30]);

(2) without these practical aspects the education provided would not have an equivalent value (see [32]); and

(3) the College's training restaurant is tantamount to a classroom for the students, and the assertion of the European Commission that students benefit from preparing meals and performing table service in a real-life setting, which is an important part of their education (see [33]).

78. In these circumstances the CJEU stated that the supplies of restaurant services must be regarded as essential to guaranteeing the quality of the principal supply of education provided by the College.

79. HMRC submitted that the supplies by the Restaurant operated by SBS were not essential to the exempt supply of exemption. In particular, HMRC submitted that the Restaurant was not student-led, drawing attention to the significant wages and salaries paid for restaurant staff as shown in the accounts of SBS.

80. SBS's position was set out in its grounds of appeal which include the following explanations:

(1) On a typical day there will be five trainers/assessors on duty at SBS' premises who would be responsible for delivering training, supervision and assessment of the students for the purposes of the various formal qualifications.

(2) SBS provides education and vocational training to students with learning difficulties. Reasons for this level of staff include that there is a high level of risk associated with providing education particularly in a kitchen environment to students with learning difficulties, and the students require a higher level of support and supervision due to their additional training needs due to their disability.

(3) Students will take orders from customers and will serve food to customers. Students will prepare food. Students are therefore involved in the entire culinary function. Students are not paid for their work as it is part of their education under the Training for Success programme.

(4) Students have the opportunity to input into menu changes and also generate new ideas in relation to food to be supplied. This is subject to the individual's level of ability with reference to their individual disability.

(5) SBS's premises include a classroom upstairs where theory lessons are taught and the restaurant facilities downstairs where theory is put into practice.

(6) SBS considers that providing the downstairs restaurant facilities as an extension of the upstairs classroom in order for the students to learn practical skills is essential to their education and preparation for work in accordance with the Training for Success programme. Exposing these students to a practical environment and interacting with customers is essential to their education and personal development. If students were to undertake such education without the practical aspects, such education would not have the same equivalent value as education provided with practice in a live environment.

81. SBS has not produced any evidence from witnesses of fact in support of the above explanation. The only evidence before me is that which is described under Facts above, the most relevant of which are the accounts and the Training Services Agreement. I also had the qualification specifications for NOCN.

82. Having considered the evidence before me in the light of the guidance given by the CJEU in *Brockenhurst*, I have concluded that the supply of goods and services in the Restaurant is essential to the provision of training by SBS. The running of the Restaurant is central to the description of the training provided by SBS in its accounts. It is referred to as the "training environment", used to give students qualifications, skills and experience. The teaching of the course in classrooms could enable students to obtain qualifications and some skills. However, the experience is gained through working in the Restaurant.

83. I do not consider that the fact that SBS employs paid staff as well using (unpaid) students casts doubt on this conclusion. SBS has provided an explanation for the staffing levels (albeit unevidenced) but I do not rely on SBS's explanation. It seems to me that the experience gained by students working in the Restaurant can still be essential to the education or vocational training provided by SBS even if SBS employed some paid staff working alongside them.

Is the purpose of those supplies to obtain additional income by carrying out transactions which are in direct competition with those of commercial enterprises?

84. In *Brockenhurst* the CJEU drew attention to:

(1) the restaurant and entertainment services were open only to people previously registered on a mailing list. The restaurant was available only by reservation and upon the condition that it be fully booked, with a minimum of thirty covers being required. Meals are cancelled if the required threshold is not reached (see [36] and [37]);

(2) the concerts, performances and restaurant services are entirely organised, carried out and supplied by students enrolled at the College (see [38]); and

(3) the prices charged by the College cover only 80% of the cost of the meals – this demonstrated that the services at issue were not intended to generate additional income for the College by carrying out transactions in direct competition with those of commercial enterprises subject to VAT, such as restaurants or theatres (see [40]).

85. I did not have the benefit of any witness evidence as to the purpose of the supplies made by the Restaurant.

86. It was common ground that the Restaurant was open to the public. Its customers were not confined to friends and family of students in the same way as in *Brockenhurst*.

87. HMRC submitted that the Restaurant's opening hours and pricing were such as to compete with normal commercial cafes and that the Restaurant was advertised in the press, on Facebook and had a website which was under development. SBS submitted in its grounds of appeal that the opening hours of the Restaurant (9am to 4pm, Monday to Saturday) were shorter than what would be expected, and that these opening hours were not designed to compete with other commercial businesses.

88. Neither party produced any evidence as to what "normal" opening hours or pricing might be, and HMRC did not produce any evidence of the advertising to which it referred in its statement of case. However, even in the absence of such evidence I consider that a Restaurant which is open along the lines described above may well in fact be competing for customers with other commercial businesses, irrespective of whether or not its opening hours are shorter than such other businesses.

89. On pricing, SBS points out in its grounds of appeal that it had operated at a significant deficit in 2016 and 2017, and that it had recovered costs of only about 75% of the Restaurant's expenses (once overheads were taken into account). This is supported by the evidence in the accounts and I accept that there was such a deficit. However, I also note that Article 134 refers to generating additional income, and not whether this is sufficient to generate a profit.

90. Article 134 states that a supply must not be granted exemption where the "basic purpose" of the supply is to obtain additional income for SBS through transactions which are in direct competition with those of commercial enterprises subject to VAT. Both the Principal VAT Directive and the CJEU in *Brockenhurst* are looking at the purpose of the supply, albeit that in *Brockenhurst* the CJEU provided guidance by reference to the surrounding facts to help ascertain that purpose.

91. The customer profile, opening hours and profitability (or otherwise) of the Restaurant are not themselves determinative. They are relevant factors to be taken into account when assessing the purpose of the operation of the Restaurant. I am satisfied that the purpose of operating the Restaurant was to enable students to gain experience of working within the hospitality industry, whether that be in the kitchens or dealing with customers. To obtain that experience it was necessary that the Restaurant had customers, and that would in turn lead to the generation of income for SBS. However, that was a consequence and not the purpose.

92. I have concluded that the supplies made by the Restaurant are exempt supplies as "closely related" to exempt supplies of education.

CONCLUSION

93. I have concluded that the only supplies made by SBS are exempt supplies, and have reached this conclusion on the basis of evidence which was provided to HMRC in support of the cancellation application. In the light of all the circumstances, the decision to refuse to cancel SBS' VAT registration is one which no reasonable body of Commissioners could have reached. Accordingly, the appeal is allowed and the decision to refuse to cancel the VAT registration is quashed. HMRC shall re-make the decision.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

94. 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.

JEANETTE ZAMAN
TRIBUNAL JUDGE

RELEASE DATE: 24 FEBRUARY 2021