[2016] UKUT 0491 TCC

Appeal number: UT/2015/0099

VALUE ADDED TAX –– exemption of sports services – Group 10, Schedule 9, VATA – whether two subsidiaries of the Appellant were eligible bodies within Note (2A) to Group 10 – whether restriction on ability to distribute profits to be ascertained primarily by reference to the constitutions of the subsidiaries – significance of other 'specific facts' – **Kennemer Golf & Country Club v Staatssecretaris van Financiën** ***applied - appeal dismissed***

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

BETWEEN:

ST ANDREW'S COLLEGE BRADFIELD

Appellant

- and –

THE COMMISSIONERS FOR
HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

Tribunal: The Hon Mr Justice Warren
Judge Greg Sinfield

Sitting in public at Royal Courts of Justice, Rolls Building, Fetter Lane, London, EC4A 1NL on 26 July 2016

Roger Thomas QC, instructed by Crowe Clarke Whitehill LLP, for the Appellant

Jonathan Bremner, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This is an appeal by St Andrew's College, Bradfield ('the College'), a co-educational boarding school, against a decision of the First-tier Tribunal (Tax Chamber) ('FTT') released on 22 January 2015, [2015] UKFTT 0034 (TC), ('the Decision'). The College had appealed to the FTT against a decision of the the Respondents ('HMRC') to refuse the College's claim for a repayment of VAT which the College accounted for in quarterly VAT periods 11/08 to 08/12.

2. The College is the representative member of a VAT group which includes two wholly owned subsidiaries, Bradfield College Developments Limited ('Developments') and Bradfield College Enterprises Limited ('Enterprises'). Developments and Enterprises made supplies of sports services. Supplies of sports services by Developments and Enterprises were treated as made by the College as representative member of the VAT group. The College had charged and accounted for VAT at the standard rate on those supplies. The basis of the College's claim was that the supplies were exempt under section 31 of and item 3 of Group 10 of Schedule 9 to the VAT Act 1994 ('VATA') as supplies by an eligible body of services closely linked with and essential to sport or physical education.

3. It was common ground that the College, as an educational charity, was itself an eligible body. Even though, as the representative member of the VAT group, the College was treated as making all supplies actually made by Developments and Enterprises, that did not mean that the supplies were exempt. Section 43(1AA) of the VATA provides that a provision, such as Note (2A), has effect as if the only description applicable to the representative member, i.e. the College, were the description in fact applicable to the body that actually made the supplies, i.e. Developments or Enterprises. The only issue in the FTT was whether Developments and Enterprises were 'eligible bodies' within the meaning of Notes (2A) to (2C) to Group 10 of Schedule 9. This depended on whether each company was a 'non-profit-making body' as described in Note (2A).

4. The FTT (Judge John Walters QC and Mrs Shameem Akhtar) dismissed the College's appeal, holding that, in the relevant period, Developments and Enterprises were not eligible bodies within the meaning of Notes 2A to 2C to Group 10 of Schedule 9 VATA. The College now appeals, with the permission of the FTT, against the Decision. Save as otherwise indicated, paragraph references in square brackets in this decision are to the paragraphs in the Decision.

5. For the reasons set out below, we have decided that there is no error of law in the Decision and the College's appeal is dismissed.

Legislation

6. Article 132(1)(m) of Directive 2006/112/EC (the 'Principal VAT Directive' or 'PVD') provides:

> "Member States shall exempt the following transactions:
>
> …

> (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 …"

7. Article 132(1)(m) of the Principal VAT Directive was formerly article 13A(1)(m) of the Council Directive 77/388/EEC of 17 May 1977 ('the Sixth VAT Directive') which was in identical terms. Accordingly, case law of the Court of Justice (which we will refer to as the 'CJEU') in relation to article 13A(1)(m) the Sixth VAT Directive is relevant to the interpretation of Article 132(1)(m) of the Principal VAT Directive.

8. Article 133 of the Principal VAT Directive (formerly article 13A(2)(a) of the Sixth Directive) further provides (inter alia) that:

> "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;"

9. Article 132(1)(m) of the Principal VAT Directive is implemented in UK law by section 31 of and Group 10 of Schedule 9 to the VATA. Section 31 of the VATA provides that a supply of services is an exempt supply for VAT purposes if it is of a description for the time being specified in Schedule 9 to the VATA. Item 3 of Group 10 of Schedule 9 to the VATA provides exemption from VAT for:

> "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."

10. Section 96(9) of the VATA provides that Schedule 9 must be interpreted in accordance with the notes in that Schedule. Notes (2A) to (2C) to Group 10 of Schedule 9 provide (so far as material) that:

> "(2A) Subject to Notes (2C) and (3), in this Group 'eligible body' means a non-profit making body which –
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> > (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 profits it makes from supplies of a description within Item 2 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 in 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."

Facts

11. There is no challenge of the type described by the House of Lords in *Edwards v Bairstow* [1956] AC 14 to the findings of fact by the FTT. The background to and facts of this appeal are fully set out at [1] to [4] and [7] to [29]. There is no need to repeat those paragraphs and the relevant facts for the purposes of this appeal can be summarised as follows.

12. Developments and Enterprises were both wholly-owned subsidiaries of the College. Until 1 September 2009, Developments managed the Sports Centre at Bradfield which had been built in the early 1990s. From 1 September 2009, Enterprises carried on the management of the Sports Centre. Developments and Enterprises both made supplies of services closely linked with and essential to sport or physical education, namely the right to use the facilities of the Sports Centre and other facilities such as a golf course and tennis courts, to individuals taking part in sport or physical education.

13. The FTT found at [27] and [28]:

> "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 …"

It was, common ground before the FTT (see [71]) and us that, during the period under consideration, neither the Memorandum of Association nor the Articles of Association of either Developments or Enterprises contained any prohibition or restriction on the distribution of profits.

14. Both Developments and Enterprises entered into deeds of covenant whereby they agreed to pay to the College annually an amount equal to their profits as computed for corporation tax. The FTT found, at [29], that both Developments, when it was trading, and Enterprises intended to maximise their revenue with a view to paying all or almost all of any surplus to the College under the deeds of covenant. The FTT accepted, in [76], that Developments and Enterprises regarded themselves as bound to pay all (or almost all) of their taxable profits to the College and did so.

15. Although the College had relied on the existence of the deeds of covenant in the FTT, Mr Roger Thomas QC, who appeared for the College in the FTT and before us, told us that the College no longer relied on them as a separate ground. The deeds of

covenant, which had not previously been located, were produced on the second day of the hearing before the FTT and were found not to be as helpful as had been hoped. The FTT found, at [78], 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."

This was because, first, Enterprises had deliberately retained a residue of profit in the relevant years (see [79] and [80]) and, secondly, Developments and Enterprises could have unilaterally terminated the deeds of covenant at any time (see [81]).

Decision

16. The only issue for the FTT was whether Developments and Enterprises were eligible bodies within the meaning of Note (2A) to Group 10 of Schedule 9. In the FTT, there was no dispute that Note (2A)(b) was satisfied as Developments and Enterprises applied any profits arising in accordance with Note (2B) and HMRC did not rely on Note (2A)(c). It was common ground that Developments and Enterprises were not precluded from distributing any profit that they made and thus they could not satisfy the condition in the first part of Note (2A)(a). The outcome of the appeal turned on the proper interpretation of the second part of Note (2A)(a), namely whether Developments and Enterprises were only allowed to distribute profits to another non-profit making body, namely the College.

17. Having set out the relevant legislation, which we have set out above, the FTT considered the relevant case law and, in particular, Case C-174/00 *Kennemer Golf & Country Club v Staatssecretaris van Financiën* [2002] STC 502 ('*Kennemer*'). At [37] to [43], the FTT stated:

> "… 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.
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> 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]). …
>
> 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]).
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> 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])."

18. At [57] et seq, the FTT addressed the construction of Note (2A). The FTT stated in [58] that:

> "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."

19. The FTT rejected HMRC's submission that it is permissible to construe Note (2A) by effectively stopping reading the Note at the mention of "non-profit making body" and giving an independent meaning to that phrase without regard to the subsequent provisions of the Notes. The FTT held, at [60], that Notes (2A) to (2C) had to be read together as a whole. Applying that approach, the FTT held as follows at [61] to [63]:

> "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.
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> 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*."

20. The FTT observed, in [65], that if it had been necessary to determine whether, by Note (2A), the UK had legitimately extended the meaning of 'non-profit making organisation' as interpreted in *Kennemer*, it might have been appropriate to refer a suitable question to the CJEU. The FTT concluded that it was not necessary to determine whether Note (2A)(a) is consistent with *Kennemer* because the College could and did rely on the terms of Note (2A)(a) as enacted.

21. The FTT then considered Note (2A)(a) and how it applied to Developments and Enterprises. The FTT first asked on what basis they should ascertain whether a particular body 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.

22. In [69], the FTT decided that, in determining whether a body came within Note (2A)(a), the guidance of the CJEU in [27] of *Kennemer* showed that they must have 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. The FTT referred to the guidance given by Advocate General Jacobs at [46] and [47] of his Opinion in *Kennemer* and noted, at [70], that:

> "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."

23. The FTT, in [71], stated that they considered that it was at this point that the College's argument broke down. The FTT noted that Mr Thomas accepted that the Memoranda of Association and Articles of Association of Developments and Enterprises did not contain any specific prohibition on the distribution of profits. While accepting that the "specific facts of the case" relied upon by Mr Thomas (namely that (a) Developments and Enterprises had at all material times been wholly-owned subsidiaries of a non-profit making organisation, namely the College; and (b) that Developments and Enterprises were under an obligation to apply their profits by gifting them under deed of covenant to the College) were relevant, the FTT declined Mr Thomas's invitation to concentrate on them in preference to the constitutions of Developments and Enterprises. The FTT held that an examination of 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 but they were not a substitute for reference to the constitution of the organisation. In contrast, Mr Thomas now submits that it was the FTT which went wrong in [71] and subsequent paragraphs and that the College's argument was sound: see further at paragraph 37 below.

24. The FTT considered the two specific facts relied on by the College in more detail in [74] to [83]. In summary, the FTT held, in [75], [77] and [83], that those facts did not overcome the lack of appropriate restrictions on distribution of profits in the Memoranda of Association and Articles of Association of Developments and Enterprises. In relation to the fact that Developments and Enterprises were, at all material times, wholly-owned subsidiaries of the College, the FTT held, at [74], that this could have changed at any time. As to the deeds of covenant, the FTT concluded, at [81], that they did not in fact create a binding obligation necessitating the application of the companies' profits for the purposes of the College. The FTT concluded, in [83], that because the constitutions of Developments and Enterprises did not contain

appropriate restrictions on distribution of profits, neither company was an eligible body in the relevant VAT periods.

Summary of submissions

25. The College now appeals, with the permission of the FTT, on the ground that the FTT erred when they held that Developments and Enterprises were not eligible bodies. The College bases its arguments on UK legislation and the Principal VAT Directive.

26. First, the College argued that Notes (2A) to (2C) to Group 10 of Schedule 9 to the VATA cannot be made to conform to Article 132(1)(m) of the Principal VAT Directive. The College relied o*n Kennemer* to show that the UK legislation could not be reconciled with the Directive. The College sought to rely on the provisions of UK law without regard to the Principal VAT Directive. It maintained that the FTT ought to have held that, under UK law, a company which is solely owned by one or more non-profit making bodies may itself be a non-profit making body even though it is permitted to distribute profits provided that it meets the requirements of Note (2A)(a), (b) and (c). Developments and Enterprises were precluded from distributing any profits that they made to any person other than the College, which was a non-profit making body, and thus Developments and Enterprises were eligible bodies within Note (2A). The College also argued that the FTT overlooked the fact that, even if the constitution of the relevant company contained a restriction on the distribution of profits, the members of the company could amend its Articles of Association to remove the restriction at any time. When considering whether, as a matter of fact, the company was at the relevant time precluded from distributing profits to any person other than a non-profit making body, the FTT should have applied Note (2A) in the context of the companies' constitutions and the fact that payments were only made to the College. The College submitted that, in the light of the constitutions and the specific facts, the FTT ought to have concluded that Developments and Enterprises were both eligible bodies.

27. Secondly, the College contended that, even if the Principal VAT Directive is relevant, the FTT had misunderstood the decision of the CJEU in *Kennemer*. The College submitted that the terms of the constitution of a corporation do not determine conclusively whether the body has the aim of achieving profits for its members.

28. HMRC submitted that the aims of both Developments and Enterprises plainly included the aim of achieving profits for their members, in this case, the College. The "specific facts" relied upon by the College could not override this. The FTT were right to find 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". Accordingly, neither Enterprises nor Developments were an "eligible body" in the relevant sense.

Discussion

29. The College relies on the terms of the UK legislation and not the provisions of the Principal VAT Directive on the ground that the two are inconsistent and the College is entitled to rely on the allegedly wider scope of the domestic legislation. It is appropriate, therefore, to consider first whether the supplies by Developments and Enterprises are exempt under UK law. The College accepts that Developments and Enterprises do not qualify under the first part of Note (2A)(a). The College relies specifically on the second part of Note (2A)(a). The issue is whether, given that their

sole shareholder was the College, and given the deeds of covenant, Developments and Enterprises were allowed to distribute any profit that they made by means of distributions only to a non-profit making body and thus qualified under the second part of Note (2A)(a).

30. Mr Thomas submitted that, until 30 January 2014, Developments and then Enterprises were able to distribute profits but only to the sole member, namely the College. In fact, the companies did not pay any dividends but made contributions to the College by way of gift aid under the deeds of covenant. Mr Thomas submitted that both activities were permitted by Note (2A) and were consistent with the companies being eligible bodies. He contended that, taking account of the companies' Articles together with the share register at the time, there was a practical, and indeed inevitable, prohibition against distributing profits to anyone other than a non-profit making body because the only person that Developments and Enterprises were allowed to distribute profits to was the College. Mr Thomas made the point that, even where there were entrenched provisions, the Articles of Association could always be amended if all the members agreed to the amendment. He contended that once it was appreciated that it is not legally possible to prevent the removal or amendment of a restriction on distribution of profits, the reasoning of the FTT based on the absence of such a provision in this case is shown to be very weak. The constitutional documents of the company offer guidance but no more than that. Mr Thomas submitted that if there were a company with several members, some non-profit making and some profit making, the absence of restriction in the Articles of Association may be relevant. But where, as here, the only member is a non-profit making organisation then the value of the constitutional documents is very much reduced. He submitted that the FTT should have had regard to the fact that the sole member, the College, was a non-profit making company and that Developments and Enterprises only made payments to the College. The FTT should have found that the companies satisfied the conditions for exemption in Note (2A).

31. We do not accept this submission. The memorandum and articles of association of Developments and Enterprises did not, at the material time, prohibit the distribution of profits other than to an eligible body: the Memorandums of both Developments and Enterprise contained wide objects, in particular, in relation to Developments, Clause 3(T) which conferred power "To dispose by any means of the whole or any part of the assets of the Company…." and in relation to Enterprises, Clause 3(V) which included power to pay money for any "national, charitable, benevolent, educational, social, public, general or useful object". It does not form part of our reasoning, but we suppose that it is those provisions which were relied on as conferring power on Developments and Enterprises to enter into the deeds of covenant.

32. Quite apart from that, the deeds of covenant did not have the effect that all of the operating profits of Developments and Enterprises would pass to the College: see the discussion at [10] to [23] and, in particular, [21] and [22] where the FTT recorded that "to the extent, for example, capital allowances were available, some of a company's operating profits might be retained" and 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". In those circumstances, the deeds of covenant do not, of themselves, establish that, as a matter of fact, Developments and Enterprises could make distributions only to non-profit making bodies.

33. Further the deeds of covenant, as the FTT found, could be terminated at any time and, if that happened, there was nothing to prevent Developments and Enterprises entering into similar arrangements with other bodies that were not non-profit making. Moreover, the College could have ceased to be a non-profit making body or, more plausibly, sold all or part of its shareholding in the companies to a commercial, ie profit making, body.

34. In our view, therefore, and even without regard to the guidance in *Kennemer*, Developments and Enterprises fail the test in the second part of Note (2A)(a). Note 2A(a), read as a whole, appears to us to be a prescriptive provision which requires specific restrictions on a body's ability to distribute any profit that it makes. We consider that, in order to meet the test, a body must show that it is subject to a restriction on its ability to distribute profits which provides that it can only distribute profits to a non-profit making body. That requires something more than the consequential prohibition on distributing profits to someone other than a non-profit-making body that exists only because (and for as long as) the sole member is such a body. Even if that is wrong, it is not established, for the reasons which we have just given, that as a matter of fact, Developments and Enterprises were in fact allowed to distribute all of their profits by means only of distributions to a non-profit making body. For that reason, too, the test just referred to is failed.

35. Mr Thomas submitted that the Directive is not relevant since, on his approach, the UK legislation is incompatible with the Directive in allowing exemption where distributions are permitted to be made only to eligible bodies. He suggested that it was strange that, having decided that Note (2A) was not compliant with the Principal VAT Directive, the FTT should then apply a test relating to article 132(1)(m) of the Directive. He contended that it was absurd to apply *Kennemer* where it could not apply because the UK legislation does not conform with the Directive.

36. We disagree. We consider that the correct approach is to construe UK legislation in the light of the EU law that it seeks to implement (see *HMRC v IDT Card Services Ltd* [2006] EWCA Civ 29, [2006] STC 1252 at [68]). This is so, in our view, even if the intended implementation is somehow defective. Accordingly, the Notes to Group 10 should be construed in the light of Article 132(1)(m). This is so, in particular, even if the UK has gone further in allowing exemption than the Directive permits, as Mr Thomas submits is the case (see further at [42] below).

37. Adopting that approach, we consider that the construction of Note (2A) which we have reached without reference to EU law is supported by the construction of Article 132(1)(m) adopted by the CJEU in *Kennemer*. We have already referred (at [25] above) to the FTT's reliance on the guidance given by the Advocate General in *Kennemer* at [46] and [47]. It is useful to set out those passages here. 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.
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> 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 and distributing profit can be deduced from the way in which it operates in practice. And in that context it is 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 prices 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.'

38. The CJEU appears to have endorsed the Advocate General's reasoning in those paragraphs at [27] of the judgment:

> "It is for the competent national authorities to determine whether, 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, an organisation satisfies the requirements enabling it to be categorised as a non-profit-making organisation."

39. We have addressed what the FTT had to say about this aspect of the case in [23] and [24] above. Mr Thomas submitted that the FTT had misinterpreted what the CJEU said in *Kennemer* and then elevated the guidance to a hard and fast rule. He said that was not what the CJEU said: rather, it said only that the national court should *have regard* to the body's objects. He said that the CJEU in *Kennemer* was clear that "non-profit making" does not mean "non-profit making" (we think that Mr Thomas is here referring to "non-profit making" in a commercial sense as understood by English lawyers) but means non-profit distributing. Mr Jonathan Bremner, for HMRC, submitted that it is the College, not the FTT, which misreads [28] of *Kennemer*. In [28], the CJEU said:

> "Where it is found that [an organisation satisfies the requirements enabling it to be categorised as a non-profit-making organisation], the fact that an organisation subsequently achieves profits, even if it seeks to make them or makes them systematically, will not affect the original categorisation of the organisation as long as those profits are not distributed to its members as profits. Clearly, Article 13A(1)(m) of the Sixth Directive does not prohibit the organisations covered by that provision from finishing their accounting year with a positive balance. Otherwise, as the United Kingdom points out, such organisations would be unable to create reserves to pay for the maintenance of, and future improvements to, their facilities."

40. Mr Bremner said that, when the CJEU says "profits" in [28], it is referring to "surpluses". As the FTT discusses in [42] (quoted in [24] above), there is a distinction between "bénéfices", ie surpluses, and "profits" in the French text. Looking at the French text confirms that the first sentence of [28] of *Kennemer* should be read as saying:

> "Where it is found that [an organisation satisfies the requirements enabling it to be categorised as a non-profit-making organisation], the fact that an organisation subsequently achieves *surpluses*, even if it seeks to make them or makes them systematically, will not affect the original categorisation of the organisation as long as those *surpluses* are not distributed to its members as profits."

41. Mr Bremner submitted that the question then is whether the company has the aim of making profits that will enrich its shareholders. In referring to the distinction between surpluses and profits on which HMRC rely, Mr Thomas accepted that the CJEU did draw the distinction, but submitted that it is impossible to reconcile that view with Note (2A). Article 132(1)(m) says that a non-profit making organisation may not aim to make profits to be distributed to its members. That is not what Note (2A) says: it

allows the distribution of profits to another non-profit making body. The UK legislation cannot be made to conform with Article 132(1)(m) of the Principal VAT Directive. Looking at both the EU and UK legislation, neither excludes from being a non-profit organisation an organisation that aims to make surpluses but the UK legislation allows a body to distribute profits to members provided they are non-profit making organisations. That is permissible under the UK legislation even though it is not permitted by the Directive.

42. We consider that Note 2A (and Note (2B)) might be made to conform by reading "profits" in that provision as having two different meanings in the same way as it does in the English language version of [28] of the judgment in *Kennemer*. The term "non-profit making body" refers to profit in the sense of amounts capable of being distributed as financial advantages to members of the body whereas "profit" in Note (2A)(a) and (b) means surpluses. Mr Thomas described this as a desperate attempt to reconcile UK legislation and the Principal VAT Directive. We would not describe it in such extreme terms although there is obvious merit in Mr Thomas' argument. It is not necessary for us to decide the point and it is undesirable that we do so since it may be central to the availability of the exemption in another case and should be decided on particularly focused argument in such a case.

43. What we do say, however, is that we should adopt a construction of the UK legislation which departs as little as possible from the requirements of the Directive. Accordingly, exemption should not be afforded in a case where the constitution of the relevant body as it stands at the relevant time would permit distribution of profits to a body which is not an eligible body even if, on the facts of the case, distributions could in practice be distributed only to an eligible body. At the relevant times, the constitutions of Developments and Enterprises permitted distributions to shareholders who might have included bodies which were not eligible bodies. Neither the fact that the College was the only shareholder nor the fact that profits were covenanted to Developments and Enterprises results in exemption being available.

44. Our conclusion is not altered by the decision of the CJEU in *Hoffmann (Criminal Proceedings against)* Case C-114/00, [2004] STC 740 ('*Hoffmann*'). Mr Thomas relied on this case which he maintained showed that the CJEU in *Kennemer* cannot have intended the "constitution" of a body to be the sole means of determining whether a body is non-profit making. Mr Hoffmann was a concert promoter and the issue in the case was whether the term "cultural bodies" in Article 13A(1)(n) of the Sixth Directive also covers an individual soloist who supplies cultural services. The CJEU held that the term "cultural bodies" was broad enough to include individual soloists. Mr Thomas submitted that, in *Hoffmann*, the CJEU rejected the argument that article 13A(2)(a), which referred to "bodies", could not apply to individuals in the same way as it applied to organisations. There is no suggestion that an individual could not satisfy the test in the article because he or she did not have constitutional documents so the national court was thrown back on looking at the facts of the case. Mr Thomas submitted that *Hoffmann* showed that the FTT were wrong to say that constitutional documents are an indispensable source. He stated that the College accepted that such documents were a useful source but not indispensable. In our view, *Hoffmann* does not assist the College in this case. In a case where there is a relevant constitution, that is not only a useful source but is the starting point. It is true, as stated in *Kennemer* at [27], that the question must be decided having regard to the objects of the organisation as defined in its constitution and in the light of the specific facts of the case, so that the construction

is not necessarily conclusive. The constitution, however, plays a very important role and where, as in the present case, reference to it provides a way of limiting the extent to which the UK legislation is taken outside the scope of the Directive, it is decisive.

Disposition

45. For the reasons given above, the College's appeal against the Decision is dismissed.

Costs

46. Any application for costs in relation to this appeal must be made in writing within one month after the date of release of this decision. As any order in respect of costs will, if not agreed, be for a detailed assessment, the party making an application for such an order need not provide a schedule of costs claimed with the application as required by rule 10(5)(b) of the Tribunal Procedure (Upper Tribunal) Rules 2008.

The Hon Mr Justice Warren

Judge Greg Sinfield

Release date: 4 November 2016