Neutral Citation: [2023] UKFTT 214 (TC)

Case Number: TC08740

FIRST-TIER TRIBUNAL
TAX CHAMBER

By remote video hearing

Appeal reference: TC/2016/06252

VALUE ADDED TAX – supplies of services closely related to exempt supplies of education – preliminary issues – Item 4 Group 6 Schedule 9 VATA 1994 and Article 134(b) PVD – whether exclusion from exemption for supplies where the basic purpose is to obtain additional income through transactions in direct competition with commercial enterprises can be read into the UK domestic provision – application of the Marleasing principle – If so, whether that was the basic purpose of the appellant's supplies

Heard on: 7 and 8 November 2022
Judgment date: 21 February 2023

Before

Tribunal Judge Cannan

Between

FAREHAM COLLEGE

Appellant

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: Michael Firth of counsel, instructed by VATangles VAT Consultancy

For the Respondents: Peter Mantle of counsel, instructed by the Solicitor's Office and Legal Services of HM Revenue and Customs

DECISION

INTRODUCTION

1. This is an appeal against HMRC's refusal to repay VAT said to have been overpaid by the appellant in relation to VAT periods 07/11 to 04/15. The appellant is a further and higher education college which offers courses including catering, hair and beauty and performing arts. Students work in a training restaurant, training hair and beauty salons and a performing arts centre operated by the appellant. The students thereby gain practical work experience as part of their courses.

2. The appellant accounted for output tax on supplies made to members of the public from the restaurant, the hair and beauty salons and the performing arts centre in the period 1 May 2011 to 30 April 2015. It contends that the supplies were exempt pursuant to Group 6 Schedule 9 Value Added Tax Act 1994 ("VATA 1994") on the basis that they were closely related to exempt supplies of education. The appellant therefore made a claim on 30 July 2015 for repayment of output tax overpaid in the sum of £69,757.

3. Group 6 Schedule 9 VATA 1994 exempts the following supplies from VAT:

> 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.

4. HMRC refused the appellant's claim for repayment by letter dated 5 July 2016 on the ground that the supplies were not exempt. That decision was upheld on a statutory review dated 20 October 2016. An appeal against the decision was notified to the Tribunal on 16 November 2016.

5. HMRC contend that the exemption in Group 6 Item 4 is to be construed by reference to Articles 132 and 134 Principal VAT Directive which provide for exemption and exclusion from exemption as follows:

> 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 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.

6. It is HMRC's case that the exemption in Item 4 Group 6 falls to be construed as including the exclusion from exemption in Article 134(b). If so, HMRC say that the basic purpose of the appellants' supplies was to obtain additional income for the appellant through transactions which were in direct competition with those of commercial enterprises subject to VAT.

7. There are two issues which arise for determination in this decision. The parties have referred to these as Issue A and Issue B and I shall do likewise:

> (A) Whether Item 4 Group 6 is to be construed as excluding from exemption supplies where the basic purpose of the supply is to obtain additional income for the body through transactions which are in direct competition with those of commercial enterprises subject to VAT.
>
> (B) If so, whether the basic purpose of the appellants' supplies was to obtain additional income for the appellant through such transactions.

8. There is a third issue which arises on the appeal. HMRC say that supplies of education to fully grant funded students are not supplies for consideration and therefore a non-business activity. That issue was determined against HMRC by the Upper Tribunal in *Colchester Institute Corporation v HM Revenue & Customs [2020] UKUT 368 (TCC)*. HMRC intend to take that issue to the Court of Appeal in another appeal by a different appellant. I am not concerned with that issue. This decision will therefore determine Issue A and Issue B as preliminary issues. The determination of the third issue may arise in due course in relation to the quantum of any recovery of output tax to which the appellant might be entitled.

9. I should also say that this appeal is a lead case pursuant to Tribunal Rule 18 in relation to Issue A and Issue B, and there are a number of appeals by other colleges which are stayed pending the determination of those issues.

FINDINGS OF FACT

10. The appellant is a further and higher education college. This appeal is particularly concerned with the courses it offers at Levels 1, 2 and 3 in the fields of catering and hair and beauty. The evidence before me included oral evidence from Ms Holly Stephenson who is the manager of Avenue 141, a training restaurant operated by the appellant. She has worked for Fareham College since 2017. Her father, Andrew Stephenson is a chef who runs a restaurant near Chichester and also works as a part time trainer in Avenue 141. He provided a witness statement which was not challenged by HMRC.

11. There was no oral evidence from any witness who worked in the hair and beauty salons operated by the appellant. The appellant had intended to adduce evidence from Ms Tracy Dickinson who had been a manager of those salons since August 2017. Ms Dickinson provided a witness statement dated 13 June 2019 but has since left the appellant's employment. The appellant sought to rely on her witness statement, whilst accepting that the weight I should give her evidence would be reduced because she was not available for cross-

examination. HMRC accept that her witness statement should be admitted in evidence on that basis.

12. The parties have prepared a statement of agreed facts which includes the following:

> 2. The relevant supplies are made by *Fareham* operating a training restaurant, a hair & beauty salon and a performing arts centre, from which services are provided to members of the public by Fareham using the students attending related courses provided by the College.
>
> 3. The provision of the relevant supplies by Fareham through the training restaurant, hair & beauty salon and performing arts studio are essential to the provision by the College of the vocational training that it provides.

13. I take the reference to "relevant supplies" as being the supplies on which the appellant is seeking recovery of overpaid tax.

14. There was no evidence at all before me in relation to the performing arts centre operated by the appellant, save for references to performing arts in the statement of agreed facts.

15. I also had evidence from Ms Karen Shreves who is the head of finance and resource operations at the appellant, and from the appellant's VAT consultant, Mr Noel Tyler.

16. HMRC relied on a witness statement from Mr Graham Speight, an officer of HMRC. Mr Speight had no direct knowledge of the operation of the training restaurant, the hair and beauty salons or the performing arts centre. It is not necessary for me to refer specifically to his evidence.

17. I shall first consider supplies relating to the appellant's training restaurant, which operated throughout the relevant period and continues to operate. For this purpose and for the purposes of this decision generally, the relevant period is 1 May 2011 to 30 April 2015. Ms Stephenson directed her evidence to the period when she was employed by Fareham which is after the relevant period. However, save where indicated, there was no suggestion that the training restaurant operated any differently in the relevant period and my findings of fact therefore relate to that period.

18. Avenue 141 operates as a silver service, fine dining restaurant. It is situated in the heart of the educational buildings of the Fareham College campus at Bishopfield Road, Fareham. It is open to the public, but it is not a high street location. The restaurant is managed by Ms Stephenson. Her role involves assisting students on the appellant's catering courses to operate the restaurant. She also trains students in all aspects of front of house operations. She has no involvement in classroom training or in the training kitchens operated by the appellant.

19. The appellant offers full time Level 1 courses in hospitality and catering. I understand that Level 1 courses involve building core skills and are generally pre-GCSE level, providing a skills based qualification. There were 16 students on Level 1 courses at the time of the hearing.

20. The appellant offers a full time Level 2 diploma in professional cookery. I understand that Level 2 courses are generally GCSE level qualifications. In year one, students gain hands-on experience cooking in the training kitchen at Avenue 141. In year two, students continue to develop employability skills in the training kitchen. There were 18 students on the Level 2 course at the time of the hearing.

21. The appellant offers a full time Level 3 diploma in professional cookery. I understand that Level 3 courses are equivalent to A Levels. This is a one-year course, and takes the training to a more demanding level. Students are required to design menus, prepare food and

cook in the training kitchen. They also have an opportunity to achieve an additional college certificate in patisserie and confectionery. At the time of the hearing there were 3 students on the Level 3 cookery course.

22. For students interested in other careers in the hospitality sector, the appellant offers a one-year Level 3 diploma in food and beverage service supervision. Students are actively involved in the day-to-day running of Avenue 141, with significant emphasis on leadership and supervision of staff under the guidance of lecturers. Students are required to design menus, learn appropriate communication skills, lead a team, supervise customer service, manage stock control and use resources effectively. They also have the opportunity to achieve an additional college certificate in barista skills and mixology. At the time of the hearing there were 3 students on this course.

23. Many local restaurants and hospitality providers employ students who have taken the appellant's courses.

24. Mr Stephenson is one of the trainers. He works on the preparation of food with students on the Level 2 and Level 3 diplomas in professional cookery. I understand that these courses are accredited by City and Guilds. He teaches practical skills, which can only be learned in a working kitchen rather than a classroom.

25. Theory based teaching on the courses is conducted in a traditional classroom. Practical work is conducted in the restaurant and kitchens at Avenue 141. There are two kitchens at Avenue 141, a larger kitchen and a smaller kitchen. The larger kitchen serves the restaurant. Most lessons are in the smaller kitchen, which is used to complement skill theory lessons. Ingredients used in teaching classes are stored together with ingredients used in the restaurant and they are not distinguished as such.

26. Avenue 141 has its own page on the appellant's website. For at least part of the relevant period it had its own website which included an online booking facility. Apart from that facility, bookings are made by phone or email. Avenue 141 also has its own Facebook page, again using the appellant's social media platform. It has won awards and accreditation within the college sector for the training that it provides to students. It is accredited with an AA College Rosette and has a Gold Accreditation from the Hospitality Guild.

27. Customers are advised to book in advance and 98% of customers do so. Reservations can be made on the day, depending on availability. The evidence was that potential customers are identified through the appellant's own database and via social media. I infer that the appellant has a database of email addresses and/or residential addresses through which Avenue 141 is marketed.

28. The restaurant is listed on Tripadvisor. Customers understand that the restaurant is run by students and the reviews are good, emphasising the quality of the food and service and the low price. Avenue 141 was ranked 19 out of 181 restaurants in Fareham in 2014, on the basis of 92 reviews. The entry on Tripadvisor included a link to the restaurant's website pages and a phone number for telephone bookings.

29. The restaurant is only open during term-time, operating 26 weeks a year. It has a maximum of 50 covers but the average service is 41 covers. There are usually 8 students working in the kitchen and 8 students working front of house during any service. The students will be at different levels of study with more experienced students supporting less experienced students. A commercial kitchen serving a restaurant that size would usually have only 2 chefs and fewer front of house staff.

30. The restaurant opens for lunch on Tuesday to Friday from 11.45am to 3pm . Students' course timetables are either 9am to 2pm or 10am to 3pm. The students are all full-time,

attending the college for 20 hours per week. Sessions either in the kitchen or front of house will last 5 hours. The restaurant opens for dinner on Tuesdays and Thursdays from 6.30pm to 10pm. Theme nights are also occasionally held in the restaurant, and it is available for venue hire.

31. The latest booking for lunch is 12.30pm. The latest booking for dinner is 7.15pm. Customers are generally served within a time period of about 2 ½ hours, including teas and coffees and paying the bill.

32. The restaurant has set lunch menus priced at £11 for two courses and £14 for three courses. There are choices of 3 starters, 4 main courses and 4 desserts The dinner menu is a la carte, with choices of 4 starters, 5 main courses and 4 desserts, all separately priced. Most dishes on the set lunch menu also appear separately priced on the evening a la carte menu. Prices are kept low to maintain the level of customers. A two course set lunch could include devilled crab fishcake and confit duck leg, with accompaniments. In the evening those dishes would be priced at £5.50 and £9.50 respectively. Ms Stephenson's evidence, which I accept, is that this is "an incredibly low price for the quality of the food".

33. The restaurant operates in as realistic a working manner as possible, so that students can experience the pressures of working within the hospitality industry. The skills and training that the students receive whilst working at Avenue 141 are requirements of City and Guilds which requires skills to be taught in a realistic working environment. Those skills are essential for students to obtain employment and progress within the catering and hospitality industry and can only be gained in a working kitchen.

34. Ms Stephenson's evidence was that Avenue 141 does not operate at a profit. By way of example, she said that a bottle of wine might cost £8 and be sold for £12. Taking into account overheads, it would operate at a loss. Her understanding from the finance department was that the restaurant was not there to make a profit, but to cover the costs of ingredients. Ms Shreves is her line manager. Whilst Ms Stephenson was not taken to any financial analysis, I do not discount her evidence in this regard. She is the manager of the restaurant and might be expected to have a good understanding as to whether it operated at a profit or loss or was intended to operate at a profit or loss. Whilst there was no direct evidence in this regard, I infer that as manager she would be responsible for, or at least aware of how prices were set and whether they were set to cover costs or make a profit. I return to the question of profit and loss when I come to consider Ms Shreves evidence.

35. I am satisfied from the evidence and it is common ground that operating the restaurant at Avenue 141 is essential to the catering and hospitality courses that the appellant supplies. The role of the appellant's teaching staff in the context of Avenue 141 is to supervise and teach the students in the training kitchen and front of house.

36. Avenue 141 has much higher staffing levels and a greater requirement for supervision than a commercial restaurant. There is also much more food wastage than there would be in a commercial restaurant. It operates on restricted hours and days, and only during term-time. The decision to offer a set lunch menu and an a la carte dinner menu is driven not by commercial considerations, but by the need to broaden the experience of students. Customers adjust their expectations to the context in which it operates, namely as a training restaurant, with lower prices than would be charged in a commercial restaurant providing fine dining and silver service. The reason that low prices are charged is to reflect the fact it is a training restaurant and to ensure an appropriate level of customers to make the working environment realistic.

37. I turn now to consider the hair and beauty salon. The appellant has a hair and beauty training salon on the college campus in Fareham known as Salon 141. It operated throughout

the relevant period and continues to operate. The appellant also operated a training salon with a high street location in Gosport throughout the relevant period, but that salon closed in 2016. There is no evidence why the appellant opened a salon in Gosport. In particular whether it was needed to provide additional training opportunities for students or some other reason.

38. As I have said, Ms Dickinson was not available to be cross-examined on her witness statement. Some of her evidence was agreed. I make the following findings of fact in relation to the operation of the two salons.

39. The appellant operates a range of courses in hairdressing and beauty therapy at Level 2 and Level 3. Courses are either full or part time and last one or two years. They are designed to equip students for careers in hairdressing and beauty therapy and in other more specialised areas, such as hairdressing and make up for stage and screen.

40. Ms Dickinson managed the Fareham salon from August 2017 onwards. Her work involved assisting students and apprentices in running the salons and training students and apprentices on hair and beauty techniques. She was not involved in the delivery of classroom training, which was carried out by the appellant's other teaching staff.

41. The courses involve training in a range of techniques and skills essential to the industry. Hairdressing courses include cutting, styling, colouring, applying treatments, customer consultations and safe working practices. Beauty therapy courses include massage, skincare, body treatments, make up application and nail services. Academic aspects of the courses include the study of essential anatomy, physiology and safe industry practices.

42. The training salons are fully equipped. The courses offer real work experience with paying clients using the salons. They involve the use of innovative equipment, resources and professional product lines.

43. Hairdressing and beauty therapy courses require practical, 'hands-on' experience. They involve the mastering of a range of skills that can only be obtained and honed in a practical training environment. It is a requirement of the course examination body that students are trained in a practical working environment, and that their practical abilities are tested.

44. The documentary evidence included pages from a website for Salon 141 at Fareham. The date these pages were printed is not clear, but there is no reference to the Gosport salon. I infer they post-date closure of the Gosport Salon and the relevant period. However, I have no reason to believe that the operation of the Fareham salon changed after the relevant period. The Fareham salon is described as follows:

> A well-equipped commercial hair and beauty salon in Fareham offering local customers a range of high-quality treatments … all at incredible prices … you will enjoy a friendly welcome and the highest standards of customer care.
>
> Choose the experience level of the stylist/therapist right for you. Remember all treatments are completed or observed by our fully qualified staff members.
>
> Your visit is more than a visit to us. It contributes to the learning and experience of Fareham College students and graduates.
>
> Hair and Beauty courses at Fareham College have an excellent reputation for producing the highest quality hairdressers and beauty stylists and this could not be achieved without the valuable experience that students gain by working in the salons.
>
> Our students learn from the hands-on exposure and expectation of paying customers from the Fareham and Gosport communities. Salon 141 offers excellent opportunities for students who will experience every aspect of the Hair and Beauty industry, ensuring that they leave with the competence and confidence to work in and manage a modern, professional salon.

> Our graduates and students are fully supervised by highly skilled and qualified staff at all times to ensure the highest standards of professionalism and customer service. There are different levels of experience available depending on your preference and, with extremely reasonable prices, your visit to Salon 141 will not only save you money but will go a long way in developing someone's career as well.

45. The website has a description of the various stylists and therapists, including Ms Dickinson who was available Tuesday to Saturday, two hair stylists and a beauty therapist who are described as being self-employed team members and who had studied at Fareham College up to Level 3 before beginning their career at Salon 141. One hair stylist is described as having just started his Level 3 course. Two hair stylists and a beauty therapist are simply described as such. All staff at the salon were involved in training students, but it is not clear what proportion of their time would be spent doing so.

46. The Fareham salon is in the heart of the appellant's campus at Bishopfield Road. It is open 6 full days a week. There is no suggestion that it is only open in term time.

47. The pricing of various styling options and treatments depend on whether they are being performed by a hair graduate, hair designer or hair director. A footnote says that hair trainees are occasionally available at a 10% discount.

48. It is not clear from Ms Dickinson's evidence how supplies to customers take place in the training salons. In particular whether, and if so in what way, students on the courses provide services to paying members of the public. The footnote referred to above refers to trainees only occasionally being available to provide services. Ms Dickinson's witness statement states that she and her fellow instructors themselves provide services to paying customers whilst training students. She also refers to students themselves providing services under the supervision of instructors. I understand that there are occasions when students would practice on each other. Further, it is not clear to what extent Ms Dickinson and fully qualified members of staff make supplies which do not involve the training of students.

49. Having said that, HMRC have accepted in the statement of agreed facts that the relevant supplies are services provided to members of the public by Fareham using the students.

50. I turn now to consider the financial evidence available in relation to the training restaurant and the training salons. In particular, evidence as to whether they operated at a profit or loss. Ms Shreves gave evidence as to the financing of the restaurant and the hair and beauty salons. She has responsibility for the daily financial operations and budgetary control systems of the appellant. She has worked for the appellant for some 25 years.

51. The costs of running the restaurant and the salons and the general costs of teaching students on the relevant courses are not separately accounted for in the appellant's accounting system. As a result, Ms Shreves found it difficult to separate out the costs attributable to the supplies in question. She did however make an attempt to do so. She extracted information from the appellant's income and expenditure accounts for the financial years 2010-11 to 2015-16 and attempted to show the income and expenditure attributable to the restaurant and the salons.

52. In each year Ms Shreves' figures showed an excess of expenditure over income. By way of summary, the averages of her figures for each year between 2011 and 2015 were as follows:

	Avenue 141	**Fareham**	**Gosport**

		Salon	Salon
	£	£	£
Average Income:	50,080	53,936	33,225
Average Expenditure:	111,927	92,284	91,821
Average Deficit:	(61,847)	(38,348)	(58,596)

53. In compiling the figures for Avenue 141, Ms Shreves used the salaries of all teaching and curriculum staff who provided training in the setting of Avenue 141. No apportionment was made because Ms Shreves considered that the primary role of the relevant staff members would be to provide training in Avenue 141. She was not aware that there was a smaller kitchen at Avenue 141 where training was given outside the context of paying customers. As a result, not all the staff costs are attributable to supplies to the general public. The salaries figure did not include salaries of teaching staff who provided classroom teaching Their salaries were assigned to a different cost centre in the accounts.

54. The expenditure for Avenue 141 included what was described as "trading account" expenditure. This was the cost of food, drinks and other consumables. Ms Shreves stated that stock for the restaurant was ordered and retained separately. She was not aware that restaurant stock was kept together with stock for general teaching and training. Initially, Ms Shreves said that stock purchased for the restaurant was accounted for in a separate cost centre, which she used to identify the cost of sales. However, she accepted that not everything included in the accounts was used to make supplies to the public.

55. In compiling the figures for the Fareham salon and the Gosport salon, Ms Shreves used the salaries of teaching and curriculum staff who were directly involved with the salons, as opposed to classroom teaching staff. However, there was no apportionment to reflect the fact that not all the time spent by staff involved supervising students. Some of that time could involve supplies where no training was involved, or training students where no supply was being made to a customer by a student.

56. Expenditure in relation to the salons also included "trading account" expenditure. That was the cost of consumables for the salons, whether or not used for paying customers. It included dyes, beauty products, shampoos and conditioners.

57. Expenditure for the Gosport salon included rent and rates for the premises and electricity usage. Again, this was the total cost, without any apportionment for supplies which did not involve training students or training where no supply was being made to a customer. No rent, rates or electricity were included in the figures for the Fareham salon.

58. Overall, Ms Shreves maintained that despite the absence of any apportionment between expenditure related purely to teaching and expenditure related to supplying services to the public, all three units made an operating loss. She pointed out that no overheads or capital expenditure incurred by the college had been attributed to the units. I do not make any findings of fact in this regard at this stage, and return to the position in my discussion of the issues.

DISCUSSION

59. The two issues fall to be considered separately. The first issue is a pure point of law as to the construction of the exemption in Item 4 Group 6 and any exclusions from that exemption. The second issue is whether the appellant's supplies are in fact excluded from exemption.

Issue A – construing Item 4 Group 6

60. There is no explicit reference in the domestic legislation to what the parties call "the basic purpose test" in Article 134(b). However, HMRC say that Item 4 should be construed so as to give effect to that provision. They rely on what is known as the *Marleasing* principle set out by the CJEU in *Marleasing SA v La Comercial Internacional de Alimentación SA* Case C-106/89 at [8]:

> … in applying national law, whether the provisions in question were adopted before or after the directive, the national court called upon to interpret it is required to do so, as far as possible, in the light of the wording and the purpose of the directive in order to achieve the result pursued by the latter and thereby comply with the third paragraph of Article 189 of the Treaty.

61. It is now well established that this Tribunal is required to interpret UK domestic legislation in such a way, in so far as possible. Later case law has emphasised the limitations on this principle, and that the exercise is one of interpretation and not law-making.

62. I have been referred to the way in which the courts have subsequently described and applied the *Marleasing* principle in practice in the following series of cases:

HMRC v IDT Card Services Ireland Limited [2006] EWCA Civ 29 ('*IDT*');

HMRC v EB Central Services Limited [2008] EWCA Civ 486 ('*EBCS*');

Vodafone 2 v HMRC (No 2) [2009] EWCA Civ 446, [2009] ('*Vodafone 2'*);

Test Claimants in the FII Group Litigation v HMRC [2012] UKSC 19 ('*FII SC'*)

Robertson v Swift [2014] UKSC 50 ('*Robertson')*

Test Claimants in the FII Group Litigation v HMRC [2021] UKSC 31 ('*FII SC 2'*)

Ampleaward Limited v HMRC [2021] EWCA Civ 1459 ('*Ampleaward*')

63. The judgment of the Court of Appeal in *Vodafone 2* is a useful starting point, in particular [37] and [38] which summarise the relevant principles by reference to previous authorities (omitting citations):

> 37. We were referred in the parties' respective written arguments and orally to a number of reported cases on the principles to be observed in looking for a conforming interpretation in either the European Community or Human Rights contexts … The principles which those cases established or illustrated were helpfully summarised by counsel for HMRC in terms from which counsel for V2 did not dissent. Such principles are that:
>
> 'In summary, the obligation on the English courts to construe domestic legislation consistently with Community law obligations is both broad and far-reaching. In particular:
>
> (a) It is not constrained by conventional rules of construction …;
> (b) It does not require ambiguity in the legislative language …;
> (c) It is not an exercise in semantics or linguistics …;
> (d) It permits departure from the strict and literal application of the words which the legislature has elected to use …;
> (e) It permits the implication of words necessary to comply with Community law obligations …; and
> (f) The precise form of the words to be implied does not matter …'
>
> 38. Counsel for HMRC went on to point out, again without dissent from counsel for V2, that:

> 'The only constraints on the broad and far-reaching nature of the interpretative obligation are that:
>
> > (a) The meaning should "go with the grain of the legislation" and be "compatible with the underlying thrust of the legislation being construed." … An interpretation should not be adopted which is inconsistent with a fundamental or cardinal feature of the legislation since this would cross the boundary between interpretation and amendment; … and
> >
> > (b) The exercise of the interpretative obligation cannot require the courts to make decisions for which they are not equipped or give rise to important practical repercussions which the court is not equipped to evaluate…'

64. Those are the relevant principles and they are not contentious. They were endorsed by the Supreme Court in *Robertson* at [21], adding at [22]:

> 22. It is important to note that, in order to observe the imperative that this guidance contains, the court must not only keep faith with the wording of the Directive but must have closely in mind its purpose…

65. Mr Mantle and Mr Firth drew my attention to passages in the authorities seeking to emphasise various aspects of those principles and the way in which they have been applied in certain contexts. Mr Mantle emphasised what Lord Sumption in *FII SC* described as its "highly muscular approach". Mr Firth emphasised what he said were the limitations of the principle, in particular that a public authority cannot rely on the direct effect of a directive against an individual and that the principle does not permit an interpretation which is *contra legem*, in other words contrary to the express terms of the domestic provision.

66. Mr Mantle specifically referred to a passage from the judgment of Arden LJ as she then was in *IDT*, which was endorsed by the Court of Appeal in *EBCS*:

> 90. … In determining whether the solution is one of interpretation or impermissible law-making, the relevant test remains whether the interpretation that would be required to make the statute in question Convention-compliant or in this case, EU law-compliant, would involve a departure from a fundamental feature of the legislation. As I see it, the latter cannot be the case where the effect of the interpretation would be to bring the statute into conformity with the objectives of the Sixth Directive in the absence of clear statutory language to the effect that Parliament intended that there should not be such conformity.

67. Mr Firth placed considerable reliance on the decision of the Court of Appeal in *Ampleaward*, which is the most recent detailed consideration of the *Marleasing* principle. He referred to various passages, including [91] were the Court of Appeal noted authorities in the CJEU that:

> 91. … a public authority was not entitled to rely on the directive against an individual. From one perspective that is what HMRC is attempting to do in the present case, albeit under the guise of a conforming interpretation.

68. The Court of Appeal cited with approval a passage from the CJEU in *Criminal proceedings against Arcaro* (Case C-168/95), noting that it was not limited to criminal proceedings:

> 42. … [The] obligation of the national court to refer to the content of the directive when interpreting the relevant rules of its own national law reaches a limit where such an interpretation leads to the imposition on an individual of an obligation laid down by a directive which has not been transposed…

69. HMRC accept that they cannot rely on the direct effect of Article 134 in the present appeal. They do not accept that they are seeking to do so under the guise of a conforming interpretation.

70. Mr Firth also relied on the following passages in *Ampleaward*:

> 87. The conclusion that the House of Lords drew from Marshall in Duke v GEC Reliance Ltd [1988] 1 All ER 626 at 636, [1988] AC 618 at 639–640 was, in the words of Lord Templeman, that:
>
> > 'Section 2(4) of the European Communities Act 1972 does not in my opinion enable or constrain a British court to distort the meaning of a British statute in order to enforce against an individual a Community directive which has no direct effect between individuals.'
>
> 88. The Supreme Court very recently approved that case in the context of the limits of the Marleasing principle: Test Claimants in [*FII SC 2*] at [143].
>
> …
>
> 93. ... Of equal interest is Advocate General Elmer's discussion of the limits of *Marleasing* in [*Arcaro*]. He said:
>
> > '[39] In that case law the court has made it clear that the aforesaid rule of interpretation is to be applied 'so far as possible' in order to interpret provisions of national law in accordance with Community law. That rule of interpretation cannot however be applied so as to undertake an actual redrafting of the provisions of national law. That would be tantamount to introducing the direct effect of provisions of a directive imposing obligations on individuals by the back door and contrary to art 189 of the Treaty.
> >
> > [40] In other words, if the wording of the national rule allows of several interpretations, the national court must apply, from amongst the various interpretations, the one which will bring the provision of national law into harmony with Community law. If on the other hand the wording of the law leaves no room for interpretation because for example the law clearly says A, the rule of interpretation cannot be used contrary to the wording of the law so as to say B, even though B (but not A) is in accordance with Community law.'
>
> 94. The CJEU returned to the limits of *Marleasing* in case C-268/06 *Impact v Minister for Agriculture and Food* [2008] 2 CMLR 47 at [100]:
>
> > 'However, the obligation on a national court to refer to the content of a directive when interpreting and applying the relevant rules of domestic law is limited by general principles of law, particularly those of legal certainty and non-retroactivity, and that obligation cannot serve as the basis for an interpretation of national law *contra legem*.'
>
> 95. The expression "*contra legem*" means "against the law". In the context of the *Marleasing* principle, the content of that phrase was explained by Advocate General Bot in *Dansk Industri (DI) v Estate of Karsten Eigil Rasmussen* (Case C-441/14), [2016] 3 CMLR 27 at [68]:
>
> > 'The Latin expression '*contra legem*' literally means 'against the law'. A *contra legem* interpretation must, to my mind, be understood as being an interpretation that contradicts the very wording of the national provision at issue. In other words, a national court is confronted by the obstacle of *contra legem* interpretation when the clear, unequivocal wording of a provision of national law appears to be irreconcilable with the wording of a directive. The Court has acknowledged that *contra legem* interpretation represents a limit on the obligation of consistent interpretation, since it cannot require national courts to exercise their interpretative competence to such a point that they substitute for the legislative authority.'
>
> …
>
> 99. It must not be forgotten that the *Marleasing* principle is a principle of *interpretation*. A court is not entitled to cross the boundary into amending legislation enacted by Parliament: see

> *Football Association Premier League Ltd v QC Leisure* [2012] EWCA Civ 1708, [2013] Bus LR 866. That is all the more so where there may be several ways in which legislation may be made compliant, which involve policy choices which a court is ill-equipped to make: *Ghaidan v Godin-Mendoza* [2004] 2 AC 557 at [33] per Lord Nicholls.

71. In *Ampleaward*, HMRC invited the Court of Appeal to construe section 18(3) VATA 1994, which deals with supplies of goods in bonded warehouses, in conformity with the PVD which gave member states the option to exempt certain supplies from VAT. The Court of Appeal found that on ordinary principles of construction the domestic provision had gone further than permitted by the PVD. It had impermissibly widened the scope of an exemption. The Court of Appeal considered that the words of section 18(3) were "*clear and unambiguous*". The interpretations proposed by HMRC were either contra legem and an invitation to read 'A' as 'B', or involved policy choices which was for Parliament to resolve and not the courts. I note that was the basis on which the Court of Appeal dismissed HMRC's appeal. It did not reject HMRC's proposed interpretations on the basis that they relied on the direct effect of a directive against an individual.

72. With all these principles in mind, I consider the construction of Item 4 which HMRC invite me to find. Mr Mantle submits that the obvious way to give Item 4 a conforming construction is to read in the words of Article 134(b). He submits that such an approach is relatively straightforward because Article 134(b) implements the principle of fiscal neutrality. Domestic provisions and the PVD must be interpreted in so far as possible to give effect to that principle.

73. Mr Firth submitted that *Arcaro*, *Impact* and *Duke*, all of which are referred to in *Ampleaward*, establish that the *Marleasing* principle cannot be used to distort national legislation. Mr Mantle did not dispute that proposition. He did dispute that was the effect of construing Item 4 as incorporating Article 134(b).

74. Mr Firth relies on five principal objections to the construction put forward by HMRC.

75. Firstly, he submits that it is not open to HMRC to give the term "closely related" in Item 4 and Article 132(1)(i) a meaning which encompasses the exclusion in Article 134(b). HMRC cannot rely on any wider meaning than has previously been given to the term "closely related" by the CJEU in this context in *HM Revenue & Customs v Brockenhurst College* C-699/15:

> 24. The term 'closely related', contained in art 132(1)(i) of Directive 2006/112, is not defined therein. Nevertheless, it is clear from the wording of that provision that it relates to the supply of services which are closely linked to 'children's or young people's education, school or university education, vocational training or retraining'. Thus, a supply of services can be regarded as 'closely related' to those latter services only where they are actually supplied as services ancillary to the education provided by the relevant establishment, which constitutes the principal supply…

76. Secondly, HMRC's construction of Item 4 in so far as it relies on giving meaning to the term "closely related" is inconsistent with the PVD. If the term "closely related" incorporated the exclusions in Article 134 there would be no need to set out those exclusions in Article 134.

77. Thirdly, there is no basis on which the term "closely related" can have the meaning for which HMRC contend. A supply can be closely related to another supply even if it is not essential to the other service (Article 134(a)) and regardless of its basic purpose (Article 134(b)).

78. I do not consider that these objections are well-founded. HMRC do not seek to construe the term "closely related" in Item 4, or to give it any wider meaning than that found in *Brockenhurst College*. HMRC's case is based on reading words derived from Article 134(b) into Item 4, relying on the principles at [37] of *Vodafone 2*. It does not rely on giving any extended meaning to the term "closely related".

79. At one stage, Mr Mantle did seek to argue that the purpose of Article 134 was to qualify the concept of supplies of goods and services "closely related thereto" in Article 132. I cannot see that it does. Article 132(1)(i) is the exemption for supplies of education, including supplies of services and goods closely related thereto. Article 134 excludes from exemption supplies which are not essential to the exempt transactions, and supplies which have the basic purpose of obtaining additional income in direct competition with commercial enterprises. A supply may be closely related in the sense of ancillary to the supply of education, without being essential thereto or having that basic purpose. To that extent, I agree with Mr Firth.

80. I shall therefore focus on Mr Mantle's principal submission that the words in Article 134 should be read into Item 4 so as to ensure conformity with the PVD, without regard to the question of whether those words can be read into the term "closely related" in Item 4. That is not to say that use of the words "closely related" in Item 4 is entirely irrelevant. Their use does at least indicate that Parliament was intending to implement the PVD. It is not a case of HMRC seeking to rely on a directive which has not been implemented in UK law. Further, it is necessary to interpret Item 4 in a way which conforms to the purpose and objective of the Directive. One of those objectives is to ensure fiscal neutrality which is the purpose of Article 134(b). The CJEU recognised this in *Brockenhurst* at [35]. Having identified that Article 134(b) was one of three conditions to which the exemption of activities closely related to education is subject, it stated:

> 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, para 34 and the case law cited).

81. Fourthly, Mr Firth submits that HMRC's interpretation of Item 4 causes it to say something that it plainly does not say. He submits that if HMRC's interpretation is permissible, then anything in a directive which has been omitted from domestic provisions could be introduced into those provisions.

82. Mr Firth pointed out that at [86] in *Ampleaward*, the Court of Appeal referred to the following observations of the CJEU in *Marshall v Southampton and South West Hampshire Area Health Authority* (*Teaching*) (Case 152/84):

> 46. It is necessary to recall that, according to a long line of decisions of the court (in particular Becker v Finanzamt Munster-Innenstadt Case 8/81 [1982] ECR 53), wherever the provisions of a directive appear, as far as their subject matter is concerned, to be unconditional and sufficiently precise, those provisions may be relied on by an individual *against the state* where that state fails to implement the directive in national law by the end of the period prescribed or where it fails to implement the directive correctly.
>
> …
>
> 48. With regard to the argument that a directive may not be relied on against an individual, it must be emphasised that according to art 189 of the EEC Treaty the binding nature of a directive, which constitutes the basis for the possibility of relying on the directive before a national court, exists only in relation to "each Member State to which it is addressed". *It*

> *follows that a directive may not of itself impose obligations on an individual and that a provision of a directive may not be relied on as such against such a person.* It must therefore be examined whether, in this case, the authority must be regarded as having acted as an individual. (Emphasis added)

83. Mr Firth submitted that there is a more limited approach to the *Marleasing* principle where the state is seeking to impose obligations on taxpayers, compared to where a taxpayer is seeking to create rights against the state. He submitted that *Ampleaward* was an illustration of that more limited approach where the court refused to impose an obligation on the taxpayer. As stated above, I do not accept that any such limited approach formed part of the reasoning of the Court of Appeal. Mr Firth also referred to what the Supreme Court said in *FII SC 2* at [143]:

> 143. It is also necessary to bear in mind that the obligation to interpret national law in conformity with the requirements of EU law is subject to the qualifications explained in European cases such as Criminal proceedings against Kolpinghuis Nijmegen BV (Case 80/86) [1987] ECR 3969 and Impact v Minister for Agriculture and Food (Case C-268/06) [2008] ECR I-2483, as well as domestic cases such as Duke v GEC Reliance Ltd [1988] AC 618.

84. As Mr Mantle observed, the Supreme Court in *FII SC2* referred to limitations on the *Marleasing* principle in passing. It was not necessary for it to consider the extent of the principle in that case and I do not consider that anything can be read in to [143] which limits the principle as explained by the Court of Appeal in *Vodafone 2* and endorsed by the Supreme Court in *Robertson*.

85. Mr Firth made a similar point in relation to *Faccini Dori v Recreb Srl* (Case C-91/92) which was cited by the Court of Appeal in *Ampleaward* at [89] and in which the CJEU said:

> 22. It need merely be noted here that, as is clear from the judgment in *Marshall* [1986] 2 All ER 584 at 600, [1986] ECR 723 at 749 (paras 48–49) the case law on the possibility of relying on directives against state entities is based on the fact that under art 189 a directive is binding only in relation to "each Member State to which it is addressed". That case law seeks to prevent "the state from taking advantage of its own failure to comply with Community law".
>
> 23. It would be unacceptable if a state, when required by the Community legislature to adopt certain rules intended to govern the state's relations - or those of state entities - with individuals and to confer certain rights on individuals, were able to rely on its own failure to discharge its obligations so as to deprive individuals of the benefits of those rights. Thus the court has recognised that certain provisions of directives on conclusion of public works contracts and of directives on harmonisation of turnover taxes may be relied on against the state (or state entities).

86. These paragraphs of *Faccini* are concerned with the rights of individuals to rely on the direct effect of directives against the state, and highlight the well-established proposition that member states cannot rely on the direct effect of directives. I agree with Mr Mantle that they are not concerned with the *Marleasing* principle. I was not referred to any authority that the state cannot rely on a conforming interpretation of a domestic provision in order to impose a charge to VAT. In both *IDT* and *EBCS*, HMRC was able to rely on a conforming interpretation to impose a charge to VAT.

87. In *IDT*, the Court of Appeal was concerned with the VAT treatment of phone cards in the UK and Ireland. Phonecards purchased in the UK were not subject to VAT, but there was a charge to VAT when the card was redeemed for telecommunication services. In Ireland the position was reversed. VAT was charged on the supply of a phonecard and no VAT was charged when the card was redeemed. The taxpayer sold phone cards in the UK which were redeemed by accessing telecommunication services in Ireland. On the face of it, therefore, the supply escaped VAT in both jurisdictions. In the Court of Appeal, Arden LJ identified the

avoidance of non-taxation as one of the objectives of the Sixth Directive and that the potential escape from liability to VAT both in the UK and in Ireland contravened that principle. She went on to hold that the domestic legislation could be interpreted so as to bring it into conformity with EU law using the *Marleasing* principle. She stated at [111]:

> 111. In addition it is not an objection to the application of the *Marleasing* principle that it may result in the imposition of a civil liability where such a liability would not otherwise have been imposed under domestic law: see for example *Centrosteel Srl v Adipol GmbH,* where the effect of interpreting Italian law in accordance with the directive on commercial agents was that a contract made by an agent who was not registered in accordance with the purely domestic provisions of Italian law was enforceable and not void. This point was specifically made by Advocate General Jacobs in para 35 of his opinion. The Court of Justice reached the same conclusion although it did not advert to this point. However it distinguished the application of the *Marleasing* principle from the general principle that a directive cannot (viz without domestic implementation) impose obligations on an individual (judgment, para 15).

88. Similarly, *EBCS* was a case where the Court of Appeal used the *Marleasing* principle to read down words from the Sixth Directive in order to make UK domestic provisions on the zero-rating of luggage storage services at airports consistent with the Sixth Directive. In doing so, the taxpayer was denied the zero-rating of supplies which would otherwise have been available on a conventional construction of the domestic provisions.

89. Mr Firth also submitted that there must be a domestic rule of interpretation that would permit Article 134 to be implied into Item 4. If there is no such rule, then that interpretation is not permissible. He referred to a decision of the CJEU in *Cresco Investigation GmbH v Markus Achatzi* Case C-193/17 at [71] – [75] and to a passage from the Supreme Court decision in *Harpur Trust v Brazel* [2022] UKSC 21:

> 44. A necessary step in the argument of the Harpur Trust is the principle of EU law that domestic legislation which implements EU law should be interpreted by domestic courts so as to conform with the EU legislation it is designed to implement. This principle is often called the Marleasing principle, after the case of Marleasing SA v La Comercial Internacional de Alimentatión SA [1990] ECR I-4135, a decision of the European Court of Justice, which preceded the CJEU. But EU law only requires UK legislation to be so interpreted if that result is consistent with domestic rules of statutory interpretation: see the decision of the House of Lords in Fleming v Revenue and Customs Comrs [2008] UKHL 2; [2008] 1 WLR 195, and Hein at para 50.

90. I do not consider that the Supreme Court was departing in any way from the settled approach to the *Marleasing* principle which it had endorsed in *Robertson*. If it had been, it would have set out precisely why and in what way it was departing from that approach. In *Harpur Trust*, the Supreme Court acknowledged at [52] that there was no requirement for the domestic provision to conform with EU law in the way that the claimant contended. The *Marleasing* principle was therefore not engaged.

91. Mr Mantle accepted that the tribunal must apply a domestic rule of interpretation, but submitted that the relevant rule of interpretation was to be found in *Vodafone 2* and *Robertson*. It was founded on the principles of interpretation established in *Ghaidan v Godin-Mendoza* [2004] UKHL 30 in the context of Convention rights. It arose because of the obligation of member states to implement directives pursuant the EEC Treaty. I agree with Mr Mantle's submission, which is made good when one considers *IDT*. Arden LJ considered the principles outlined in *Ghaidan*, in the context of the European Convention on Human Rights and section 3 Human Rights Act 1998, and the obligation established in *Marleasing* to construe domestic legislation consistent with obligations under the EEC Treaty. She concluded at [92]:

> 92. … Section 3 imposes an obligation to interpret legislation compatibly with Convention rights, not a discretion to do so. Accordingly, I consider that the differences in concept between section 3 interpretation and interpretation under the *Marleasing* principle are more apparent than real. As already stated I consider that the *Ghaidan* case is a helpful guide when determining the interpretation under the *Marleasing* principle. I see no reason why the same robust techniques used to make legislation compatible with the ECHR should not equally apply to make domestic legislation comply with the laws of the European Union.

92. I agree with Mr Mantle that the authorities referred to above establish a rule of construction in the law of England and Wales as to the circumstances in which the *Marleasing* principle will be applied. It is not necessary to identify any other rule of construction. The Court of Appeal in *Ampleaward* did not qualify that rule of construction. That case is simply an illustration of the limits of the rule.

93. Fifthly, Mr Firth submits that HMRC's interpretation is contra legem. It requires one to say that a supply which is closely related to another supply, applying the meaning of those words in *Brockenhurst College*, is not in fact closely related.

94. Contra legem is a limitation on the *Marleasing* principle. It applies where the proposed interpretation contradicts the very wording of the domestic provision. There was a contradiction in *Ampleaward*. The words "in any member state" were clear and unambiguous and could not be replaced by the words "in the United Kingdom".

95. Mr Firth raised a number of arguments associated with his submission that HMRC's interpretation is contra legem:

> (1) Parliament has not attempted to implement Article 134. It implemented Article 132 and must be taken to have chosen not to implement Article 134, despite its obligation to do so.
>
> (2) In Schedule 9 VATA 1994, Items 5 to 5C concern the provision of education and vocational training in certain specific cases. Parliament has made express reference to the supply of any goods or services "essential" thereto. He suggested that if Parliament intended Item 4 to be subject to the condition in Article 134(a) then it would have limited Item 4 to supplies which were essential to the transactions exempted. Where Parliament has chosen to implement a directive in a certain way, it is not for courts or tribunals to override the will of Parliament.
>
> (3) Whilst the basis for the exemption in Item 4 is Article 132(1)(i), Parliament was not simply intending to implement the PVD. Hence, it incorporated Item 4(a), which was not a restriction contained in the PVD.
>
> (4) Item 4 refers to the supply of "any" goods or services which are closely related to the principal supply. Imposing a restriction on what goods or services were exempt in addition to the principal supply was contra legem.
>
> (5) Introducing a basic purpose test where there was no reference to the purpose of the supply in the domestic provisions amounted to a distortion of those provisions which it is clear from *Duke* is not permissible.
>
> (6) There is no "textual anchor" in Item 4 on which to attach the words of Article 134(b). The existing wording, which requires the supply to be closely related to the principal supply, does not provide such an anchor. Those words might possibly permit the requirement in Article 134(a) that the supply be essential to the principal supply to be read in to Item 4. However, the basic purpose in Article 134(b) has nothing to do with how closely related supplies might be.

96. I do not consider that these points take the arguments any further or establish that implying the words of Article 134(b) into Item 4 would be contra legem. In short, there is nothing in these submissions which causes me to consider that implying the words of Article 134(b) into Item 4 is inconsistent with the words used by Parliament in Item 4. The provision in Article 134(b) clearly goes with the grain of the legislation, which must in any event be construed to be consistent with fiscal neutrality. It is compatible with the underlying thrust of the legislation. There is no distortion and it is not necessary to identify any textual anchor.

97. I do not consider that HMRC's interpretation is *contra legem*. It does not directly contradict the words used by Parliament in Item 4, nor does it require 'A' to be read as 'B'. It simply ensures that the exemption is implemented in a way which is consistent with the purpose of Articles 132 and 134. It cannot be said from the words actually used in Item 4 that Parliament clearly intended to implement the exemption in a way which did not conform with the PVD.

98. It is clear from *Vodafone 2* that the *Marleasing* principle is broad and far-reaching, and that it permits the implication of words necessary to comply with the UK's obligation to implement Articles 132 and 134. As the Court of Appeal stated in *Vodafone 2*, the precise form of the words to be implied does not matter.

99. I am satisfied that Item 4 should be interpreted as including the exclusion from exemption in Article 134(b). It is not strictly necessary for me to consider whether Item 4 should also be interpreted as including the exclusion from exemption in Article 134(a), because HMRC accept that on the facts of this case the relevant supplies were essential to the transactions exempted.

100. Contrary to Mr Firth's submission, such a conclusion does still leave limits on the interpretative process. In particular, interpretations which do not go with the grain of the legislation, which would be contra legem or which require courts or tribunals to become involved in policy decisions are not permitted. None of those limitations apply in this case.

Issue B – Are the appellant's supplies excluded from exemption?

101. I now consider whether the appellant's supplies were excluded from exemption because the basic purpose of the appellant in making those supplies was to obtain additional income through transactions which were in direct competition with commercial enterprises. There appear to be two elements to the exclusion in Article 134(b) which I have held is implied into Item 4. Firstly, that the basic purpose of the supply is for the appellant to obtain additional income. Secondly, that the appellant does so through transactions which are in direct competition with commercial enterprises. The parties both approached their submissions on the basis of these two elements.

102. An issue arises as to the burden of proof in this context. The appellant says that it is for HMRC to establish that the basic purpose of the appellant was to obtain additional income through transactions in direct competition with commercial enterprises. In support of that submission, Mr Firth submitted:

> (1) HMRC are asserting that the basic purpose of the supplies falls within the exclusion and should therefore bear the burden of proof. The appellant should not be required to prove a negative; and
>
> (2) The exclusion from exemption in this case is analogous to other situations where exclusion from exemption depends on establishing a distortion of competition and where HMRC have the burden of proof, in particular Article 13 PVD.

103. HMRC say that the long established general rule is that taxpayers bear the burden of proving that an assessment or decision of HMRC is wrong. None of the exceptions to that rule apply in this context.

104. As regards the first element of the exclusion, Mr Mantle says that the appellant is in the best position to adduce evidence as to its basic purpose in making the supplies. As regards the second element, Mr Mantle says that it involves an application of the principle of fiscal neutrality and there is no reason why the appellant should not bear the burden of proving that its supplies are not in competition with other commercial operators. The position is not analogous to Article 13 PVD, where the burden is on HMRC to establish that there is distortion of competition.

105. The Upper Tribunal in *Massey v HM Revenue & Customs* [2015] UKUT 405 considered the burden of proof in appeals involving the EU law concept of abuse of law, at [58] to [60]. In doing so, it referred to the general rule and to situations where HMRC bears the burden of proof, in particular where HMRC allege fraud or that a transaction is a sham and where an assessment to a penalty is under appeal:

> 58. In tax appeals, it has long been established that the taxpayer has the burden of showing that the assessment issued or decision reached by HMRC is wrong (see T Haythornthwaite & Sons v Kelly (Inspector of Taxes) (1927) 11 TC 657 for direct tax appeals and *Tynewydd Labour Working Men's Club* for appeals relating to VAT). In cases where fraud is alleged, it is accepted that HMRC bears the burden of proof…
>
> 59. Fraud is not the only situation where HMRC bear the burden of proof in tax appeals. As Mr Gordon observed, HMRC have the onus of proving an allegation that a transaction is a sham: see *Hitch v Stone* (*Inspector of Taxes*) [2001] EWCA Civ 63, [2001] STC 214 (at [32] per Arden LJ). It has also long been accepted that HMRC bear the burden of proving that a person is liable to a penalty for late submission of a return or late payment of tax whereas the taxpayer bears the burden of establishing that he or she has a reasonable excuse.
>
> 60. In determining who bears the burden of proof in an appeal where abuse of law is alleged, it is necessary to consider which party substantially asserts that there is or has been an abuse. As discussed above, it is the nature of an abusive arrangement that the taxpayer's appeal would succeed on the purely formal application of the legislation. The appeal will only fail if it can be shown that there is an abuse, ie the resulting tax advantage is contrary to the VAT Directives and the essential aim of the transactions is to obtain a tax advantage. If abuse were not alleged or, having been alleged, cannot be established then the appeal must be allowed. It follows that establishing that a tax advantage is contrary to the VAT Directives and the essential aim of the transactions is to obtain a tax advantage is an essential part of HMRC's case in an appeal where abuse of law is alleged. Accordingly, HMRC bear the burden of proving those matters.

106. Mr Firth submitted that in the present appeal, it was HMRC which is seeking to establish an exclusion to the rule that the appellant's transactions are prima facie exempt. They are doing so by asserting a positive case as to the appellant's basic purpose and that the appellant's transactions are in competition with those of commercial operators. In those circumstances the burden must lie on HMRC to establish the exclusion from exemption.

107. I do not agree. The appellant is seeking to challenge HMRC's decision not to repay output tax said to have been overpaid. It is seeking to establish that its supplies were exempt from tax, which must include an assertion that the exclusion from exemption in Article 134(d) does not apply. In my view, the position is governed by the long established principle that the taxpayer has the burden of showing that the assessment issued or decision reached by HMRC is wrong. None of the exceptions to that principle apply. Indeed, the appellant is clearly in the best position to adduce evidence to establish its basic purpose in making the

supply. Further, there is no reason why the appellant should not bear the burden of establishing that its supplies are not in competition with those of commercial operators.

108. Nor do I consider that the position is analogous to appeals concerning Article 13. In outline, Article 13 PVD provides that certain public bodies are not regarded as taxable persons where they make supplies as such. This is subject to a proviso that they are to be regarded as taxable persons in relation to supplies where their treatment as non-taxable would lead to significant distortions of competition. It has been common ground in authorities dealing with the application of that provision that HMRC bears the burden of proving that if the public body is treated as non-taxable then it would lead to a significant distortion of competition. See for example, *Isle of Wight DC v HM Revenue & Customs* [2015] EWCA Civ 1303 at [23].

109. The general rule in Article 2 is that VAT is charged on all supplies of goods for consideration in a member state by a taxable person. Article 13 defines what is meant by a taxable person in the context of public authorities. Prima facie a public authority acting as such is not a taxable person. It is not surprising that HMRC would be required to prove that the proviso was engaged to bring a public authority back within the scope of VAT. In contrast, Article 132 provides for exemption from VAT. The taxpayer has to establish entitlement to the exemption from VAT under Article 132. Article 134 simply sets out conditions for the exemption to apply. It must be for the taxpayer to establish that all the conditions for exemption are satisfied. This is consistent with the approach of the CJEU in *Brockenhurst* at [26]:

> 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 arts 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 art 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…

110. I approach Issue B therefore on the basis that it is for the appellant to establish the third condition referred to in *Brockenhurst* is engaged so that the relevant supplies remain exempt.

111. Looking at the first element of Article 134(b) it is necessary for the appellant to establish that the basic purpose of the appellant's supplies was not to obtain additional income. I understand that there are no other references in the PVD to the term "basic purpose" and the parties could not identify any authority as to the meaning of that term.

112. Mr Firth submitted that reference to "the" basic purpose indicates that there can only be one such purpose, and that use of the word "basic" indicates that it is the essential or fundamental purpose which is relevant. That is the natural reading of Article 134(b).

113. Mr Mantle did not accept that submission. He submitted that depending on the circumstances a taxpayer could have more than one basic purpose, and those purposes could be intertwined. The term should not be construed narrowly because it provides for an exclusion from exemption. The condition should also be interpreted in the context of the purpose of Article 134(b), which is to ensure fiscal neutrality.

114. I agree with Mr Firth's straightforward submission. In my view, Article 134(b) does not require any gloss. It requires identification of the single basic purpose of the taxpayer in making the supply.

115. I am conscious that there is a separate requirement in Article 134(a) that the supplies in question must be essential to the exempt transactions. It is not in dispute here that the supplies are essential to the exempt transactions. HMRC accept that it is essential for the appellant to provide students with a realistic working environment as part of their vocational courses. The meaning of the term "essential" in this context was considered by the CJEU in *Brockenhurst*, which also involved a training restaurant. In relation to the second condition in Article 134(a), the CJEU said as follows:

> 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.

116. It seems from [28] and [32] of *Brockenhurst* that the test of whether a supply is essential to the exempt transaction is not a "but for" test. In other words, exemption from VAT does not depend on the fact that the principal supply could not take place without the closely related supply. However, for the closely related supply to be exempt it must be established that the principal supply would not have "equivalent value" without it.

117. It is also notable that at [30], the CJEU took into account the purpose of the college in operating the training restaurant as part of its consideration of whether the supplies were essential to the exempt transactions.

118. Exemption is excluded only if the basic purpose of the taxpayer is to obtain additional income. Given that a related supply must also be essential to the exempt transaction, one purpose is always likely to be the provision of education. However, the Article envisages that the provision of education will not necessarily be the basic purpose of the related supply.

119. Mr Firth acknowledged that it is difficult to think of a supply that is essential to a supply of education where the basic purpose is not providing education. However, I agree with him that whilst the two conditions may overlap, that is not a reason to adopt a different interpretation of the basic purpose. The consideration for the supply may result in additional income, perhaps significant additional income. The basic purpose of the supply may be to obtain that additional income. It seems to me that in considering the purpose of the supply, all the circumstances in which the supply is made must be considered, including the consideration for the supply. On that approach, I can see that a taxpayer may have the basic purpose of obtaining additional income whilst also having a purpose of providing education. What matters is the basic purpose of the taxpayer in making the supply in the way in which it is made. In some cases, obtaining additional income may simply be a consequence of the related supply and not itself a basic purpose. Indeed, in this case Mr Mantle accepted that charging for the supplies was necessary to provide a realistic working environment. Charging too low a price might mean that customers would be less likely to complain or criticise if the supply did not meet their expectations. In other cases, obtaining additional income may be the basic purpose of the supply, notwithstanding that the supply also enhances the value of the education.

120. Mr Mantle submitted that Mr Firth's submission amounted to a misreading of Article 134. He submitted that Article 134(a) and (b) were "alternative, not cumulative". I am not sure what Mr Mantle meant by that distinction, but it is clear from *Brockenhurst* and also *HM Revenue & Customs v Bridport and West Dorset Golf Club Ltd* Case C-495/12 at [23] that these sub-paragraphs give rise to two separate conditions for exemption. They are separate, but as Mr Firth says the facts relevant to whether a supply is essential to the exempt transaction may well also be relevant in identifying the basic purpose of making the supply.

121. Mr Mantle submitted that the "basic purpose" is to be determined objectively, in other words on the basis of objective evidence and taking into account the objective features of the relevant supplies. I agree that is the right approach. The subjective intentions of the appellant, which were expressed in some of the witness evidence, are not relevant.

122. In *Brockenhurst*, it appeared to the CJEU that the college's basic purpose was not to obtain additional income through transactions which were in direct competition to commercial enterprises. The principal factors relevant to that conclusion were the restricted basis on which the training restaurant operated and the fact that the prices charged by the college covered only 80% of the cost of the meals. This meant that there was no breach of the principle of fiscal neutrality. It stated as follows:

> 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.

123. During the course of submissions, consideration was given to the meaning of "additional income" in this context. Mr Mantle accepted that there would only be additional income if the consideration for the related supplies exceeded the costs associated with making the supplies. In this context, it seems to me that it is necessary to take into account not only the direct costs of making the supplies, but also the associated overheads. In the context of a training restaurant, this will include the cost of the food provided, and any wastage, the cost of variable overheads such as electricity and the costs of fixed overheads such as rent and rates. Mr Mantle appeared to accept that an appropriate apportionment of such costs could be made.

124. It also seems to me that if a taxpayer consistently makes a surplus on that basis, then obtaining additional income is likely to be one of the purposes of the supply, if not necessarily the basic purpose. Similarly, if a taxpayer consistently makes a deficit on that basis, it is unlikely that its purpose would be to obtain additional income.

125. Article 134(b) also focusses on the basic purpose of the supplies, not the basic purpose of operating the training restaurant. If during a theme night the price of meals was increased significantly then the basic purpose of making those supplies is more likely to be obtaining additional income. I say that only by way of illustration. There was no evidence that prices were increased in that way.

126. Mr Mantle submitted that an important part of the appellant's purpose was to train students, but its purpose was also to obtain additional income. As previously stated, in my view there can only be one basic purpose.

127. I shall first consider supplies from the training restaurant. The only supplies made from the training restaurant are relevant supplies, in the sense of supplies made by students to members of the public in order to obtain realistic work experience.

128. Based on the evidence as a whole and my findings of fact, I am satisfied that the appellant did not set out to operate Avenue 141 at a profit. In reaching that conclusion I rely on the evidence of Ms Stephenson and Ms Shreves and my findings as to how Avenue 141 operated. The primary purpose is to provide a realistic working environment for training students. The appellant broadly seeks to cover the cost of ingredients and at least some overheads, but no more. I make that finding on the basis of objective evidence, in particular:

(1) It is essential for the appellant to operate a training restaurant for the students to successfully complete their courses.

(2) The restaurant has limited opening hours.

(3) The supplies are made at very low prices for the quality of the food served.

(4) Prices are set with a view to covering the cost of ingredients. To the extent that there is a mark-up on cost, that is to cover the cost of overheads.

(5) Prices are also set with a view to maintaining sufficient customers to ensure a realistic working environment.

(6) The appellant's accounting systems make it difficult to identify whether the restaurant makes a surplus or a deficit. That is because the appellant is not concerned with whether the training restaurant produces a surplus or a deficit.

129. Taking into account all the evidence and my findings of fact I am satisfied that obtaining additional income from supplies made at Avenue 141 was not the appellant's basic purpose. Its basic purpose was to provide a realistic working environment for students to pursue their courses and qualifications.

130. It is not therefore necessary for me to consider whether supplies to customers from Avenue 141 were in direct competition with those of commercial restaurants. For the sake of completeness I shall consider that issue.

131. Mr Firth submitted that the appellant's supplies from Avenue 141 would only be in competition with commercial enterprises if they were viewed as similar from the point of view of a typical customer. That must be right, and Mr Mantle referred to *Rank Group Plc v HM Revenue & Customs* Case C-259/10 where the CJEU stated:

> 42. As observed in paragraph 32 of the present judgment, [the principle of fiscal neutrality] precludes treating similar goods and supplies of services differently for VAT purposes.
>
> 43. In order to determine whether two supplies of services are similar within the meaning of the case-law cited in that paragraph, account must be taken of the point of view of a typical consumer (see, by analogy, Case C-349/96 *CPP* [1999] ECR I-973, paragraph 29), avoiding artificial distinctions based on insignificant differences (see, to that effect, *Commission* v *Germany*, paragraphs 22 and 23).
>
> 44. Two supplies of services are therefore similar where they have similar characteristics and meet the same needs from the point of view of consumers, the test being whether their use is comparable, and where the differences between them do not have a significant influence on the decision of the average consumer to use one such service or the other (see, to that effect, Case C-481/98 *Commission* v *France*, paragraph 27, and, by analogy, Joined Cases C-367/93 to C-377/93 *Roders and Others* [1995] ECR I-2229, paragraph 27, and Case C-302/00 *Commission* v *France* [2002] ECR I-2055, paragraph 23).

132. In the context of the exemption for medical care by different categories of healthcare professionals, the CJEU held in *Solleveld v Staatssecretaris van Financien* Case C-443-04 that medical care can be regarded as similar only to the extent that it is of equivalent quality from the point of view of recipients:

> 41. It follows that the exclusion of a profession or specific medical-care activity from the definition of the paramedical professions adopted by the national legislation for the purpose of the exemption from VAT laid down in Article 13A(1)(c) of the Sixth Directive is contrary to the principle of fiscal neutrality only if it can be shown that the persons exercising that profession or carrying out that activity have, for the provision of such medical care, professional qualifications which are such as to ensure a level of quality of care equivalent to that provided by persons benefiting, pursuant to that same national legislation, from an exemption.

133. I accept, as Mr Mantle says, that this was a quite different context to the present appeal involving exclusion from exemption in Article 134. However, it seems to me that depending on the context, a typical customer might differentiate between a supply provided by students learning the necessary skills, and a supply provided by a commercial operator who might be expected to have acquired those skills. The fact a supply is to be provided by a student may have a significant influence on the decision of the average consumer to use one service or another.

134. In relation to the training restaurant, Mr Firth submitted that the services provided by the appellant were not similar to commercial restaurants because the service and food were being provide by students who were learning the necessary skills. The pricing indicates that what was being supplied was not similar to a commercial restaurant.

135. I note that Avenue 141 was open to members of the public generally, albeit with limited opening hours. It has a rating on Tripadvisor and is ranked 19 out of 181 restaurants in Fareham. In broad terms, customers would be served with their meal in a similar manner to a commercial restaurant and enjoy a similar experience. However, customers will adjust their expectations given that it is a training restaurant. Overall, I have concluded that supplies from Avenue 141 are not in direct competition with commercial enterprises.

136. Turning now to the training salons. It is an agreed fact that relevant supplies from the salon are services provided to members of the public by the appellant using the students. Not all supplies from the salons are made by students. I must focus on the particular supplies, not the operation of the salons as a whole.

137. Based on the evidence as a whole and my findings of fact, I am satisfied that one purpose of the appellant in making the relevant supplies was to provide students with realistic work experience and to provide vocational training. Ultimately, the question is not whether the salon operates at a profit, but whether the supplies in question produce additional income for the appellant.

138. The position in relation to the training salons is different to that in relation to the training restaurant. There is very little evidence available as to how the salons operated. I take into account, in particular:

(1) It is essential for the appellant to operate at least one training salon for the students to successfully complete their courses. There was no evidence as to why two salons were operated.

(2) The salons operate normal opening hours throughout the year.

(3) The only evidence of low pricing was the reference to a 10% discount for hair trainees. There was no evidence as to the basis on which that discount was determined.

(4) There was no evidence as to how prices were set by reference to costs.

(5) The appellant's accounting systems make it difficult to identify whether the salons themselves make a surplus or a deficit, but that is not a relevant question in relation to whether the supplies produce additional income.

139. Overall, there is insufficient evidence for me to conclude whether or to what extent student supplies are profitable. I am unable to say whether supplies using student services produce additional income for the appellant. I cannot be satisfied that the appellant did not have a basic purpose of obtaining additional income from relevant supplies in the salons.

140. In relation to competition, I had little evidence as to how the relevant supplies were made and how they might differ from those in a commercial salon, other than the fact that they are made by students. Overall, I am not satisfied that the relevant supplies from the salons were not in direct competition with those of commercial enterprises.

141. Finally I should deal with the position of the performing arts centre. The appellant made no submissions in relation to the performing arts centre. It was an agreed fact that the relevant supplies are made to members of the public by the appellant operating a performing arts centre. The supplies are made using students attending the appellants relevant courses and they are essential to those courses. Beyond that I know nothing about the circumstances in which those supplies were made. I cannot be satisfied that it was not the appellant's basic purpose to obtain additional income from the supplies, or that the supplies were not in direct competition with those of commercial enterprises.

CONCLUSION

142. For the reasons given above I determine Issue A as follows:

> In favour of the respondent, Item 4 Group 6 Schedule 9 VATA 1994 is to be construed as excluding from exemption supplies where the basic purpose of the supply is to obtain additional income for the body through transactions which are in direct competition with those of commercial enterprises subject to VAT.

143. In relation to Issue B, I must determine it separately for supplies in relation to the training restaurant, the training salons and the performing arts centre:

> (1) In favour of the appellant, I am satisfied that the basic purpose of the appellant's supplies from the training restaurant was not to obtain additional income for the appellant through transactions which are in direct competition with those of commercial enterprises subject to VAT.
>
> (2) In favour of the respondents, I am not satisfied that the basic purpose of the appellant's supplies from the training salons was not to obtain additional income for the appellant through transactions which are in direct competition with those of commercial enterprises subject to VAT.
>
> (3) In favour of the respondents, I am not satisfied that the basic purpose of the appellant's supplies from the performing arts centre was not to obtain additional income for the appellant through transactions which are in direct competition with those of commercial enterprises subject to VAT.

144. It will be necessary for the parties to consider the effect of this decision on the quantum of the claim, taking into account the third issue which is being dealt with by reference to another lead case. The parties should consider whether it is appropriate to stay this appeal pending the determination of the third issue and shall inform the Tribunal accordingly within 60 days of the date of this decision.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

145. This document contains full findings of fact and reasons for the preliminary decision. Any party dissatisfied with this preliminary 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. However, either party may apply for the 56 days to run instead from the date of the decision that disposes of all issues in the proceedings, but such an application should be made as soon as possible. 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.

JONATHAN CANNAN
TRIBUNAL JUDGE

Release date: 21st FEBRUARY 2023