# *Longridge on the Thames v HMRC*: A charitable role for economic activity and VAT?

### *Introduction*

The meaning of "economic activity" for the purposes of VAT has been considered by various courts on several occasions and some divergence between the decisions of the UK courts and the Court of Justice of the European Union (CJEU) was apparent. The determination of whether an economic activity has taken place is critical for VAT purposes, and particularly relevant for charities which often operate very much on the borderline. The Court of Appeal decision in *Longridge on Thames v HMRC (Longridge)*[1]. In a decision that has potentially wide reaching impacts on charities, the decision of the Court of Appeal in *Longridge on Thames v HMRC (Longridge)*[2] has provided some welcome clarity on the issue.

### *The Facts in Longridge*

Longridge on the Thames was a charity which offered water-based activities (for both recreational and education purposes) to the public. As well as providing resources for the activities themselves, Longridge also offered related tuition. Its activities were available to all, although the centre primarily targeted young people. It did not provide these services without charge, but prices varied according to the ability of the consumer to pay. Any shortfall was met from donations and other receipts.

Longridge was not registered for VAT and so did not charge VAT on its activities. However, following the construction of a new building, it had been required to pay £135,000 of VAT in respect of the building services. Longridge argued that, as the building was intended for use solely for charitable purposes, the building services should be zero-rated under schedule 8 of the VATA 1994.[3] If the building services were zero-rated, Longridge would be able to recover any input taxes attributable to the construction of the building. HMRC decided that Longridge were not able to rely on schedule 8, since their activities constituted an "economic activity" (the building will only be zero rated if it is used solely for a relevant charitable purpose, and this is not the case if an economic activity is also taking place) and Longridge appealed.

### Legislative background

Article 9(1) of the European Community Council Directive 2006/112/EC (hereafter the "Principal VAT Directive") provides for VAT to be charged on the supply of goods for consideration by a taxable person. A "taxable person' "shall mean any person who, independently, carries out in any place any **economic activity**, whatever the purpose or results of that activity."[4] (emphasis added). VAT was implemented in the UK by what is now the Valued Added Tax Act 1994 (VATA) which, in section 4(1), provides that VAT shall be charged on "a taxable supply by a taxable person in the course or furtherance of any business carried on by him."[5]

The difference in wording between UK and the European versions of the law might explain in part the fact that there were, leading up to *Longridge*,[6] two different interpretations in the case law of when there is a taxable person for VAT purposes: one in EU law, and one in domestic law. However, the difference in wording is dealt with swiftly in *Longridge*, which makes the obvious point that the VATA must be interpreted in line with the Principal VAT Directive and so "furtherance of any

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[1] *Longridge on Thames v HMRC (Longridge)* [2016] EWCA Civ 930 (CA).
[2] Above fn.1; [2016] EWCA Civ 930 (CA).
[3] Value Added Tax Act 1994, Note 6, Group 5 of Schedule 8. This provides that the supply of building services is zero-rated if the building is intended for use solely as a relevant charitable purpose.
[4] Council Directive 2006/112/EC on the system of value added tax [2006] OJ L347/1, article 9(1).
[5] VATA 1994, section 4(1).
[6] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA).

business" is interchangeable with "economic activity" (in the sense that they should both achieve the same result).[7] The appeal compares and considers the two lines of case law; one concerned with "business" and the other with "economic activity".

**Background**

*CJEU jurisprudence*

*Longridge* placed considerable reliance on the 2009 decision of the European Court of Justice (ECJ), *European Commission v Finland (Finland).*[8] Earlier ECJ decisions had already considered the meaning of economic activity, so we already knew that there is economic activity where a supply is continuous and for remuneration[9] or consideration,[10] and there is a direct link between the service provided and the consideration given.[11] However, more detailed consideration was given to these matters in *Finland*.

In this case, the Finnish Government argued that the legal aid services that it suppled were not an economic activity and therefore not subject to VAT. Although a contribution was payable towards legal aid depending on the income of the recipient, such contributions did not come close to covering the costs of the provision of the legal services provided. The ECJ noted that an activity is an economic activity where it is "permanent and is carried out in return for remuneration which is received by the person carrying out the activity".[12] This the ECJ referred to as the "general rule". However, it also noted that there must be a *direct* link between the service and the payment received[13] and it was decided that there was no such link as the legal aid contribution was not dependent solely on the cost of the service but also on the income of the recipient. Consequently, there was no economic activity.[14] The implication of *Finland* is that the mere fact that a person receives income from an activity does not on its own make that activity "economic".

*Domestic jurisprudence*

It is evident that the UK courts have adopted an interpretation of economic activity which is wider than the approach adopted by the ECJ in that it allows additional factors to be taken into consideration. The Court of Appeal considered four decisions of the UK courts. The first case it referred to was *Customs and Excise Commissioners v Morrison's Academy Boarding Houses Association (Morrison's Academy)*,[15] which considered the marks of a business activity:

> "[H]ow would this activity be properly described without any reference to the issues of tax liability? I think the answer would be that it is essentially a business activity of a very usual and normal kind. It has every mark of a business activity: it is regular, conducted on sound and recognised business principles, with a structure which can be recognised as providing a familiar constitutional mechanism for carrying on a commercial undertaking, and it has as its declared purpose the provision of goods and services which are of a type provided and exchanged in course of everyday life and commerce."[16]

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[7] Above fn.1; [2016] EWCA Civ 930 (CA) at [14].
[8] *European Commission v Finland (Finland)* (Case C-246/08) [2009] ECR 1-10605 (ECJ).
[9] *Landesanstalt für Landwirtschaft v Franz Götz (Götz)* (Case C-408/06) [2007] ECR I-11298 (ECJ) at [18].
[10] *Tolsma v Inspecteur der Omzetbelasting Leeuwarden (Tolsma)* (Case C-16/93) [1994] ECR I-743 (ECJ) at [14].
[11] *Apple and Pear Development Council v Customs and Excise Commissioners* (Case 102/86) [1988] ECR 1443 (ECJ).
[12] *Finland* (C-246/08), *a*bove fn.8; [2009] ECR 1-10605 at [37].
[13] *Finland* (C-246/08), *a*bove fn.8; [2009] ECR 1-10605 at [45].
[14] *Finland* (C-246/08), *a*bove fn.8; [2009] ECR 1-10605 at [51].
[15] *Customs and Excise Commissioners v Morrison's Academy Boarding Houses Association (Morrison's Academy)* [1978] STC 1.
[16] *Morrison's Academy,* above fn.15; [1978] STC 1 at [10].

These marks of a business activity were then collated in the case of *Customs & Excise Commissioners v Lord Fisher (Fisher),*[17] which highlighted six factors paraphrased as follows:[18]

1. A 'serious undertaking earnestly pursued';
2. A reasonable or recognisable continuity;
3. A measure of substance in regards to the annual taxable supplies – i.e. the volume of the supplies;
4. An activity that is conducted regularly on sound business principles;
5. A predominant concern for making taxable supplies for consideration;
6. The supplies are of a kind that are usually made for profit.

These factors allow the context surrounding the activity to be explored and go beyond the test applied in *Finland*.[19] *Fisher* was built upon in *HMRC v Yarburgh Children's Trust (Yarburgh)*[20] which went further and considered the charitable purpose as "relevant to a consideration of whether the organisation in question can seriously be regarded as doing anything more than the carrying out of its charitable functions."[21] This approach was approved and followed in *HMRC v St Paul's Community Project Limited (St Paul's)*,[22] in the sense that the economic activity was determined by reference to the charity's predominant concern: i.e. that there was a charitable purpose. Following these domestic cases, it was therefore possible for a charitable activity to not be a business activity if a charitable purpose was the charity's predominant concern.

The practical effect of these decisions, of course, is that relative to EU law, the UK approach indicates a wider understanding of the scope of activities that fall outside the definition of an economic activity for VAT purposes and which are consequently not subject to VAT.

*Decision of the FTT*

The question put before the FTT was whether Longridge was carrying out an economic activity in its general activities. First, the FTT referred to the case of *Commission v Netherlands*,[23] which states that whether there is an economic activity is an objective test, and consideration of the additional factors of the purpose or results of the activity is irrelevant. However, the FTT then applied the considerations that were applied in *Yarburgh*,[24] and so looked objectively at whether there was an economic activity with reference to the entirety of the activity and the context surrounding the activity. The factors in *Fisher*[25] were also considered, and the tribunal specifically considered the fact that Longridge was receiving consideration for the services that it provides; that there was a business-like manner in its running; the charges made were according to commercially recognisable terms and conditions; and, Longridge had a significant turnover. These factors, however, were not enough to label the activities as economic activities. Instead, the FTT considered (amongst other things)

- the discounts offered to those who could not afford the full price;
- the charges set with a view to cover operational expenses only;
- the possibility of waiving or reducing charges where there is a charitable interest to do so;

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[17] *Customs & Excise Commissioners v Lord Fisher (Fisher*) [1981] STC 238.
[18] *Fisher*, above fn.17; [1981] STC 238 at [245].
[19] *Finland* (C-246/08), above fn.8; [2009] ECR 1-10605.
[20] *HMRC v Yarburgh Children's Trust (Yarburgh)* [2002] STC 207.
[21] *Yarburgh*, above fn.20; [2002] STC 207 at [30].
[22] *HMRC v St Paul's Community Project Limited (St Paul's)* [2005] STC 95.
[23] *Commission v Netherlands* (Case-C-235/85) [1987] ECR 1471 (ECJ).
[24] *Yarburgh*, above fn.20; [2002] STC 207.
[25] *Fisher*, above fn.17; [1981] STC 238.

- that all capital projects are financed by donations;
- that volunteers run the activities.[26]

In the FTT's view, "these are not factors which are indicative of a business".[27] After balancing the *Fisher*[28] criteria and *Yarburgh*,[29] the FTT decided that Longridge's "predominant concern" is charitable[30] and, as such, it is not carrying on an economic activity.

*Decision of the Upper-Tribunal (UT)*[31]

Before the UT, HMRC relied heavily on *Finland*, which was not cited to the FTT. It argued that there is an economic activity if there is a permanent activity carried out for remuneration. HMRC also argued that motive for profit was not relevant to the concept of an economic activity; and, as a result, that no analysis of the costs charged by Longridge for its services should take place. It was also submitted that *Yarburgh*[32] and *St Paul's*[33] were no longer good law, following the decision in *Finland*.

The UT considered domestic and CJEU cases. It noted that a distinction had to be made between two types of activities: first, those that amounted to the furtherance of a business even though there was no motive for profit (following *Morrison's Academy*[34]) and, second, activities which were not conducted as a business even though there was consideration (following *Finland*[35]). It noted that it was a question of fact for the FTT to decide which of these types of activities were being conducted here. As the FTT has looked at the totality of the features of the activities, it had not erred in law. In addition, the UT decided that *Finland* had not narrowed the test for economic activity to the point that *Yarburgh*[36] and *St Paul's*[37] were no longer applicable.

HMRC appealed to the Court of Appeal.

*Decision of the Court of Appeal*

Counsel for Longridge continued to argue that the wider context of the activity was relevant in the determination of whether it was an economic activity. It was accepted that the meaning is an objective one, but, nonetheless, the court should take into account the wider context seen within *Yarburgh*[38] and *St Paul's*.[39] In other words, "to decide whether a person supplying services is engaged in economic activity one is entitled to take into account those terms and features which lead one to conclude that the manner in which the activities are undertaken is different from that which would be undertaken by someone engaged in activity in that activity in the ordinary course of the market."[40]

On the other hand, and the important point of the appeal, counsel for HMRC argued that unless it can be proven that there is no direct link between the service and the consideration, there will be an

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[26] *Longridge on the Thames v Revenue and Customs Commissioners (Longridge (FTT))* [2013] UKFTT 158 (TC) at [99]- [101].
[27] *Longridge (FTT),* above fn.27, [2013] UKFTT 158 (TC) at [100].
[28] *Fisher,* above fn.17; [1981] STC 238.
[29] *Yarburgh,* above fn.20; [2002] STC 207.
[30] *Longridge (FTT),* above fn.27, [2013] UKFTT 158 (TC) at [103].
[31] *Revenue and Customs Commissioners v Longridge on the Thames* [2014] UKUT 504 (TCC), [2015] STC 672.
[32] *Yarburgh,* above fn.20; [2002] STC 207.
[33] *St Paul's,* above fn.22; [2005] STC 95.
[34] *Morrison's Academy,* above fn.15; [1978] STC 1.
[35] *Finland,* above fn.8; [2009] ECR 1-10605.
[36] *Yarburgh,* above fn.20; [2002] STC 207.
[37] *St Paul's,* above fn.22; [2005] STC 95.
[38] *Yarburgh,* above fn.20; [2002] STC 207.
[39] *Longridge,* above fn.1, [2016] EWCA Civ 930 (CA) at [47].
[40] *Longridge,* above fn.1, [2016] EWCA Civ 930 (CA) at [49].

economic activity.[41] HMRC also argued that the general rule (where a supply is continuous and for remuneration it will constitute an economic activity) needed to be applied. Finally, and perhaps most importantly, it was also argued that the domestic law and the criteria in *Fisher*[42] were only guidance, and could not override the principles established in both *Götz*[43] and *Finland*.[44]

*Longridge* was decided in favour of the HMRC. In coming to this decision, Arden LJ and Morgan J worked through the ECJ and domestic case law, balancing them to come to the meaning of economic activity. This need for interpretation at CA level highlights the previous difficulties encountered in attributing a meaning to these words.

There is no special rule for charities.[45] An activity can also be deemed an economic activity even if the activity is not profitable.[46] Arden LJ reiterated that the test for an economic activity is an objective one;[47] and it is generally assumed that an activity is an economic one if "it is permanent and is carried out in return for remuneration by the person carrying out the activity".[48] In addition, there must be a direct link between the remuneration received and the activity.[49] In this case, the fact that Longridge had charitable concerns were irrelevant to the objective test, and were not enough to convert what would otherwise be an economic activity into a non-economic activity. In terms of a direct link, the CA agreed with the findings of fact of the FTT – that the amount charged by Longridge for the services was "more than nominal", and as such there is a direct link.[50] Arden LJ considered that the domestic jurisprudence outlined above now diverges from these European law principles. A clear example of this is seen in the focus on a direct link in *Finland,*[51] which is nowhere to be seen within the *Fisher*[52] criteria.[53]

Morgan J considered the role of "predominant concern" as applied in *Yarburgh*[54] and *St Paul's*[55]. Again, the domestic law is considered in a negative light following CJEU jurisprudence and is labelled as "unhelpful" and "misleading".[56] This demonstrates yet another move away from the domestic jurisprudence, and an acceptance of the objective test in *Finland*.[57] A list of general propositions is also created by Morgan J which provides a useful if not particularly innovative summary of the points within *Finland*.[58]

**Comment**

What this case brings to the 'economic activity table' appears to be an application of *Finland*[59] which limits the role of domestic jurisprudence. Arden LJ's stated that factors developed by domestic case

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[41] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [29].
[42] *Fisher*, above fn.17; [1981] STC 238.
[43] *Götz* (C-408/06) above fn.9; [2007] ECR I-11298.
[44] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [35] and [41].
[45] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [70].
[46] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [72].
[47] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [73].
[48] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [75]; *Finland*, above fn.8; [2009] ECR 1-10605 at [37].
[49] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [76]; *Finland*, above fn.8; [2009] ECR 1-10605 at [44]- [45].
[50] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [92].
[51] *Finland* (C-246/08), above fn.8; [2009] ECR 1-10605.
[52] *Fisher*, above fn.17; [1981] STC 238.
[53] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [85].
[54] *Yarburgh*, above fn.20; [2002] STC 207.
[55] *St Paul's,* above fn.22; [2005] STC 95.
[56] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [121].
[57] *Finland*, above fn.8; [2009] ECR 1-10605.
[58] *Longridge*, above fn.1; [2016] EWCA Civ 930 (CA) at [109].
[59] *Finland* (C-246/08), above fn.8; [2009] ECR 1-10605.

"cannot displace the approach required by CJEU jurisprudence". Whilst the decision adds little to what has already been stated in *Finland* it does add clarity in terms of the approach to be taken. The correct approach is that there is an economic activity if there is a direct link between the consideration and the service, with direct link construed narrowly – it does not allow for the consideration of motives, or wider contextual considerations. As such, any criteria that existed before in the domestic jurisprudence, have now been subsumed into a general rule: a permanent supply for consideration. Other definitions in VAT law, for instance consideration,[60] have already been defined in CJEU jurisprudence, and this area of domestic law might be regarded as having being overdue in its consideration of EU law. *Fisher*,[61] for example, did not apply the ECJ meaning of economic activity, but instead considered a number of factors which indicated the presence of a business activity. *Longridge*[62] could be considered as a clean-up operation to bring the domestic law into line with the European jurisprudence.

The practical impact of this decision is that it is difficult to see when a permanent activity of supply for consideration would not be an economic activity, unless one is faced with factual circumstances that are akin to *Finland*.[63] It was argued by Arden LJ that "there will be cases where the activities of an organisation such as a charity, providing services at a concessionary rate, do not amount to economic activity".[64] Yet, this writer finds it difficult to imagine how this would be the case unless the concessions represented a very small amount of the costs of the service, and were indexed to external factors (such as means testing in *Finland*). As such, most charities will not find any charitable favour within *Longridge'*s interpretation of the meaning of economic activity.

Amy Lawton*

[60] *Tolsma* (C-16/93), above fn.10; [1994] ECR I-743 at [14].
[61] *Fisher,* above fn.17; [1981] STC 238.
[62] *Longridge,* above fn.1; [2016] EWCA Civ 930 (CA).
[63] *Finland* (C-246/08), above fn.8; [2009] ECR 1-10605.
[64] *Longridge,* above fn.1; [2016] EWCA Civ 930 (CA) at [88].