WHEN IS A CHARITY CARRYING ON A "BUSINESS" FOR VAT PURPOSES?

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1 Introduction

1.1 The British Experience

There has developed since the Reformation a long and noble tradition in the United Kingdom[2] whereby non-governmental bodies and associations carry on activities, not with a view to profit, but for the public benefit and whereby individuals gratuitously devote their time and money to such bodies. In England, they normally qualify as "charities". United Kingdom fiscal law recognises their public utility, *inter alia*, by exempting them from most taxes on income and gains, on capital transfers and from taxes on gifts and inheritances, as well as by conferring tax incentives on donors to charity.

1.2. The European Dimension

Value added tax, however, is not a United Kingdom tax. It is a European tax, the creation of the EEC,[3] and was invented in the days when the members of the EEC were countries (predominantly countries where the Reformation had been successfully resisted) where the concept of charity, as we know it, had never developed, where it was generally considered that the conferring of public benefit

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2 which has been successfully exported to the USA and, to a lesser extent, to other present or former possessions of the British Crown.

3 Now the EU.

was the role of government rather than of private initiative and where charity in general not only began but ended at home. Our present system of value added tax was part of the price the United Kingdom had to accept in return for the supposed benefits of our membership of the EEC. It is, therefore, scarcely surprising that the system contains no general exemption for charities, simply a very limited number of piece-meal relieving provisions which may or may not apply in a particular situation.

1.3 Charities as Oddities within the Value Added Tax System

Charities and other not-for profit bodies do not fit easily into the scheme of value added tax. Value added tax is intrinsically a charge on consumption and the charge falls, as a matter of economic reality, if not of strict law, on the final consumer. Where the various persons or bodies concerned (at whatever stage in what is referred as "the supply chain") in the creation of the final product are each predominantly concerned with the maximisation of profit, the situation is relatively straight forward. Each will, if they are successful at their business, add value to the product at each stage in the supply chain and the final consumer will pay a price which represents the total cost of production, including the profit margin of the producers. Although in principle, Revenue authorities can lose out when producers trade at a loss, on the whole they need have no real concerns, as those who consistently trade at a loss will not remain in business for long.

Charities are in an unusual position in that, unlike traders, their ultimate aim is not to make money. They may make charges for goods or services they provide in the course of carrying out their primary functions, but they do so in order to enable them to carry out those functions, which are an end in themselves. Unlike traders, they do not carry out their functions in order to make money. The supplies they make may be subsidised by their endowment income, by private donations or by state subsidies and hence may be made at an under-value. That is one reason why the value added tax treatment of charities can be highly capricious in its incidence and why, within limits, charities can sometimes, by careful planning, do a great deal to improve their overall value added tax position.

1.4 The Alleged Neutrality of Value Added Tax

A much-vaunted strength of the system of value added tax, as compared with primitive systems such as purchase tax or sales tax, is that is supposed to be neutral in terms of the nature of the supply chain which leads to tax being levied on the final consumer. That is the case, however, only if all supplies in the supply chain are taxable. The misleadingly styled "exemptions" in fact produce gross distortions in the system and give rise to precisely those problems which value added tax is supposed to avoid! When a supply is exempt, no value added tax is

charged on it, but, conversely, no value added tax suffered earlier in the supply chain is recoverable. As charities very often make exempt supplies, this adversely impinges on them and their beneficiaries.

We in the United Kingdom have a concept of zero-rating, or "exemption with credit" as it is referred to in Europe. Where a supply is zero-rated, no value added tax is charged on it but the supplier is able to recover his input tax in full. That has the advantage over so-called exempt supplies in that (assuming the zero-rated supply to be made to the final consumer) all the value added tax is recoverable, the exemption from value added tax is complete and the same amount of tax, namely zero, is charged no matter how the supply chain is structured.

Whereas from a logical point of view, zero-rating should be the norm and exempt supplies should not exist at all, the possibility for a Member State to zero-rate supplies is regarded as an exception and permitted only subject to stringent conditions during what is called the "transitional period". That, of course, is quite irrational, but then no man of the world is surprised at the illogicality of anything which comes out of Europe. And we in the United Kingdom are limited by EEC law as to the extent to which we can zero-rate supplies. For example, the European Court of Justice ruled in *EC Commission v United Kingdom* (Case 416/85) [1988] STC 456 that zero-rating for construction services was warranted only where the supply is made to a person who does not use the exempted goods or services "in the course of an economic activity". United Kingdom domestic law was modified accordingly.

2 The Interpretation of United Kingdom Value Added Tax Legislation

The general rule is that, as United Kingdom value added tax legislation is intended to give effect to EC value added tax legislation, and in particular the Sixth Council Directive of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes-common system of value added tax: uniform basis of assessment (77/388/EEC) ("the Sixth Directive"[4]), it is to be construed as far as possible so as to give effect to that legislation. This is sometimes called the canon of "sympathetic" interpretation.[5]

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4 References below to EC VAT legislation are to articles of the Sixth VAT Directive. Note, however, that on 28th November 2006 the EU Council of Ministers adopted a revised EC VAT Directive (Directive 2006/112/EC, OJ L 347/1, 11th December 2006), which has replaced both the First and the Sixth EC VAT Directives with effect from 1st January 2007.

5 For the lengths to which this can be taken, see *Greenalls Management Ltd v Customs and Excise Commissioners* [2005] UKHL 34 [2005] 1 WLR 1754.

That, of course, requires that the EC legislation is itself construed. In order that EC legislation should be interpreted and applied in as uniform a manner as possible throughout the EC, the European Court of Justice has power to give rulings, known as preliminary rulings, on the interpretation of that law, to the courts of Member States, who are often empowered and sometimes obliged to request such rulings. In addition, the Court opines on EC law in substantive cases brought before it. As a matter of United Kingdom law, the United Kingdom courts are in general obliged to follow the rulings of the European Court of Justice on the interpretation of EC law.

While it is true of any legal system that the decisions of its courts sometimes conflict and are not always easy to reconcile with each other, there are some peculiar difficulties with decisions of the European Court of Justice. It often sits in small Chambers of as little as five or even less judges, so that the persons making the decisions can vary. Judges are appointed for a limited term of office and not, as in the United Kingdom, until retirement, so that there is a fair turnover. Judges are appointed by their Members States for various reasons and not solely on legal merit. The intellectual quality of the judges varies enormously.

The Court does not regard itself as bound by its previous decisions and can thus change its mind. The deliberation of the judges is secret. Only one, collective, judgment is given and any dissent is ruthlessly suppressed, in a way which seems alien to those of us who enjoy the benefits of the Glorious Revolution, but which must seem less alien in those many parts of the EC which within living memory were either run or overrun by Fascist or other totalitarian regimes. The reasoning in the judgment is always pithy, often laconic and sometimes downright cryptic. This is no doubt due in part to the need for "diplomatic" drafting which represents different shades of opinion.

Badly drafted as is much United Kingdom legislation, the drafting of EC legislation is often even worse. In order to make good the incompetence of those responsible, the European Court of Justice has adopted a canon of interpretation known as "purposive construction". Instead of simply looking at what the legislation says and what it means as a matter of plain language,[6] the Court looks to what it ought to have meant and construes it accordingly. While it pays lip-service to the principal of legal certainty, it is often very difficult indeed for a man of intelligence, even an experienced lawyer, to tell in advance how the Court will interpret legislation.

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6 or, rather, languages, as EC legislation is to be found in many languages, each version having the same authority as the rest, even though the translations do not always fully agree!

3 Relevance of Charity Carrying on a "Business"

If a charity carries on a "business", within the meaning of the value added tax legislation, it will normally need to charge and account for value added tax ("output tax") on any taxable supplies it makes. If and to the extent to which it incurs value added tax ("input tax") for the purpose of making such supplies, it will be able to deduct it. If the deductible input tax paid is greater than the output tax for which it is accountable, the charity will actually be entitled to a refund. This can occur where the charity makes zero-rated supplies[7] (which are technically taxable supplies on which tax is charged at a nil rate). It can also occur if the consideration charged by the charity for its outputs is less than the cost of making them - a situation which is rare in a successful enterprise established for profit but which could often occur in the case of a charity.

If supplies of construction works, land or buildings are made to a charity, those supplies could be zero-rated if the charity occupies the building for its charitable purposes other than those which amount to a "business". Even if a charity occupies the building for the purposes of a business in the course of which it makes only exempt supplies, zero-rating will not, as a matter of strict law[8] be available.[9]

In some cases, it will benefit charity to be carrying on a business and in other cases it will not. Some of the United Kingdom cases concerned with the meaning of "business" involve charities and other not-for-profit bodies. Understandably, the United Kingdom courts have been largely sympathetic to charities and have

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7 These are listed in Schedule 8 to the Value Added Tax Act 1994.

8 See Extra Statutory Concession 3.29, which provides:

"1-(1) For the purposes of Groups 5 and 6 of Schedule 8, Group 1 of Schedule 9 and Schedule 10 to the Value Added Tax Act 1994 (VATA), and subject to the conditions set out in Part III below, the non-qualifying use of a building can be ignored if the entire building will be used solely for a qualifying purpose for more than 90 per cent of the total time the building is available for use.

(2) Alternatively, the non-qualifying use of an identifiable part of a building can be ignored if that part of the building will be used solely for a qualifying purpose for more than 90 per cent of the total time that part of the building is available for use.

(3) Alternatively, the non-qualifying use of a building can be ignored if 90 per cent or more of the floor space of the entire building will be used solely for a qualifying purpose.

(4) Alternatively, the non-qualifying use of a building can be ignored if the entire building will be used solely for a qualifying purpose by 90 per cent or more of the people using the building (on a head count basis)."

9 If the charity uses the building for the purpose only of making zero-rate supplies, it will not be concerned that any supply to it were standard-rated, as it would be able to recover the value added tax charged.

tried, so far as they can, to relieve them from the worst excesses of the system of value added tax, particularly where they are not involved in activities which are comparable to, and directly compete with, trades carried on for profit.

Unfortunately, value added tax law is so complex and capricious in its incidence that while that may be to the advantage of a particular charity in one case, it may be to the disadvantage of another charity in another case.

4 What is a "Business"? - The Ambiguous State of the Law

It has long been accepted by the Courts that, as a matter of English, the word "business" is very wide indeed, so wide that there can scarcely be a charity which does not have or carry on a "business", in its usual sense. However, in the context of value added tax legislation, "business" carries a much more restricted meaning.

The word "business" is scarcely defined at all in the Value Added Tax Act 1994 (or its predecessors, Value Added Tax Act 1983 and Finance Act 1972). For over twenty-five years, the English (and Scottish) courts tried to construe "business" with scant reference to the Sixth Directive and the interpretations put on the corresponding phrase therein by the European Court of Justice. Even now, there is still a tendency to hark back to the earlier United Kingdom case law, the authority of which is in some cases frankly doubtful. The European Court of Justice cases are more helpful, but there remain large areas of ambiguity.

This very ambiguity can be useful to charities. Not only the United Kingdom Courts, but Her Majesty's Commissioners of Revenue and Customs (formerly the Commissioners of Customs and Excise) can be extremely benevolently inclined towards *bona fide* charities. Provided they do not see themselves as conceding a point which might be used against them in other, less charitable, contexts, the Commissioners can sometimes take a very liberal view of the law, especially where it is complex and unclear.

5 United Kingdom Statute Law

The United Kingdom statute law is of virtually no assistance. Value Added Tax Act 1994 provides:

> "4 Scope of VAT on taxable supplies
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> (1) VAT shall be charged on any supply of goods or services

made in the United Kingdom, where it is a taxable supply made by a taxable person in the course or furtherance of any business carried on by him.

(2) A taxable supply is a supply of goods or services made in the United Kingdom other than an exempt supply."

Value Added Tax Act 1994 section 5(2)(a) provides that ""supply" in this Act includes all forms of supply, but not anything done otherwise than for a consideration".

There is no definition of "business", but Value Added Tax Act 1994 provides, *inter alia*, that it includes any trade, profession or vocation.

6 The Sixth Directive

6.1 The Directive

Title II: Scope, Article 2, of the Sixth Directive provides:

"The following shall be subject to value added tax:

1 the supply of goods or services effected for consideration within the territory of the country by a taxable person acting as such;

…"

The concept of a "taxable person"[10] is dealt with in Title IV: Taxable persons, Article 4, which provides:

"1 "Taxable person" shall mean any person who independently carries out in any place any economic activity specified in paragraph 2, whatever the purpose or results of that activity.

2 The economic activities referred to in paragraph 1 shall comprise all activities of producers, traders and persons supplying services including mining and agricultural activities and activities of the professions. The exploitation of tangible or intangible property for

10 It is unfortunate that some key words and expressions, including "taxable person" and "supply" have a different meaning in (a) United Kingdom domestic law and (b) the Sixth Directive

the purpose of obtaining income therefrom on a continuing basis shall also be considered an economic activity.

3 [Deals with persons who carry out, on an occasional basis, a transaction relating to the activities referred to in paragraph 2 and is not material in the present context]

4 [Deals with employees and connected persons and is not material in the present context.]

5 States, regional and local government authorities and other bodies governed by public law shall not be considered taxable persons in respect of the activities or transactions in which they engage as public authorities, even where they collect dues, fees, contributions or payments in connection with these activities or transactions.

However, when they engage in such activities or transactions, they shall be considered taxable persons in respect of these activities or transactions where treatment as non-taxable persons would lead to significant distortions of competition.

In any case, these bodies shall be considered taxable persons in relation to the activities listed in Annex D, provided they are not carried out on such a small scale as to be negligible.

Member States may consider activities of these bodies which are exempt under Article 13 or 28 as activities which they engage in as public authorities."[11]

6.2 "Taxable Person"

Now the main purpose of the definition of "taxable person" is to enable one to determine whether a supply made for a consideration is to be subject to value added tax. For it is only if such a supply is made "by a taxable person acting as such" that it can be subject to value added tax. However, the concept of "taxable person" is inextricably bound up with that of "economic activity". It is well established that a person will carry on a "business" within the meaning of the United Kingdom value added tax legislation only if carries on an "economic activity" such as to make him a "taxable person" within the meaning of the Sixth

11 I return later to article 4.5 (which contains a derogation from the basic definition) and its possible relevance in the present context.

Directive.[12] Hence, article 4 of the Sixth Directive is also relevant to the construction of Value Added Tax Act 1994 Schedule 8 Group 5.

The core of the definition of "taxable person" is contained in article 4.1 and 4.2. In order to discover whether a propositus is a "taxable person", we need to know whether he or it is carrying out (otherwise than as an employee) "any economic activity specified in paragraph 2". Paragraph 2 tells us "The economic activities referred to in paragraph 1 shall comprise all activities of producers, traders and persons supplying services including mining and agricultural activities and activities of the professions."

6.3 "Economic Activity"

The key is to determine what is meant by the core and vital concept of "economic activity". In this regard, the Directive offers no definition and provides but scant clues! It is quite clear that one cannot read article 4.2 literally. For example, if I paint a picture as a hobby and later sell it, I am literally a "producer", but no one would claim that I am a taxable person. It is thus not conclusive that a charity is a taxable person merely because it is a "person supplying services".

The words "whatever the purpose or results of that activity" at the end of paragraph suggest that the motive, purpose or intention of the propositus is completely irrelevant in determining whether he is a taxable person. Now it is true that the lack of a profit motive is not per se relevant. Yet it is equally clear that, at least in some contexts, motive, purpose and intention are relevant. What is a matter of debate is when motive, purpose and intention are relevant.

The European Court of Justice stresses in case after case the enormous width of the concept of "economic activity" in article 4.

In *EC Commission v United Kingdom* [2000] ECR I-6355 (Case C-359/97), Alber A-G said at paragraph 26: "The question whether there is an economic activity must be appraised objectively in the light of the actual economic situation." The Court said at paragraph 39-41:

> "39. It should be noted that the Sixth Directive attributes to VAT a very wide scope by including amongst the taxable transactions defined in art 2 not only the importation of goods but also the supply of goods or services effected for consideration within the territory of a country and by defining 'taxable person' in art 4(1) as any person who independently carries out an economic activity,

12 See, for example, see the decision of the House of Lords in *Institute of Chartered Accountants in England and Wales v Customs and Excise Comrs* [1999] STC 398).

whatever the purpose or results of that activity (see *EC Commission v Netherlands* (Case 235/85)[1987] ECR 1471 at 1487, para 6).

"40. 'Economic activities' are defined in art 4(2) as comprising all activities of producers, traders and persons supplying services. In particular, the exploitation of tangible or intangible property for the purpose of obtaining income therefrom on a continuing basis is also to be considered an economic activity.

"41. **An analysis of those definitions shows that the scope of the term 'economic activities' is very wide, and that the term is objective in character, in the sense that the activity is considered per se and without regard to its purpose or results**[13] (see *EC Commission v Netherlands* (Case 235/85) [1987] ECR 1471 at 1487, para 8)."

*EC Commission v Netherland*s was followed on this point by the Court in *Stichting Uitvoering Financiële Acties v Staatssecretaris van Financiën* (Case 348/87)[1989] ECR 1737 at 1752, para 10.

Van Tiem v Staatssecretaris van Financiën (Case C-186/89) [1990] ECR I-4363 is to the same effect. See per Van Gerven A-G at paragraph 7 and per the Court at paragraph 17. *Rompelman v Minister van Financiën* (Case 268/83)[1985] ECR 655, ECJ, was also followed in this regard.[14]

To the same effect is *Sofitam SA (formerly Satam SA) v Ministre chargé du Budget* [1993] ECR I-3513 Case C-333/91 per Van Gerven A-G at paragraph 11 and per the Court at paragraph 10: "It is settled case law (see, inter alia, *EC Commission v France* (Case 50/87)[1988] ECR 4797 at 4817, para 15) that the deduction system is meant to relieve the trader entirely of the burden of VAT payable or paid in the course of all his economic activities. The common system of VAT consequently ensures that all economic activities, *whatever their purpose* or results, provided

13 Emphasis added by the author.

14 The scope of "economic activity" is so wide that there can be an economic activity even at a time when no supplies are being made, provided such supplies are intended to be made in future: see *Rompelman v Minister van Financiën,* followed in *Lennartz v Finanzamt München III* (Case C-97/90) [1991] ECR I-3795, ECJ. Nor is the position any different if the intended supplies are never in fact made: see *Intercommunale voor Zeewaterontzilting (in liq) ["INZO"] v Belgium* (Case C-110/94) [1996] ECR I-857, ECJ, and *Belgium v Ghent Coal Terminal NV* (Case C-37/95), [1998] ECR I-1.

they are themselves subject to VAT, are taxed in a wholly neutral way."[15]

The Court reiterated its view on the scope of value added tax in *Harnas & Helm CV v Staatssecretaris van Financiën* [1997] ECR I-745 (Case C-80/95) at paragraph 13[16]. Fennelly A-G said at paragraph 23:

> "It must be recalled, in the first instance, that the court has consistently held that art 4 of the Sixth Directive confers 'a very wide scope on value added tax (VAT), comprising all stages of production, distribution and the provision of services'(see, inter alia, *van Tiem* [1990] ECR I-4363 at 4386, para 17 of the judgment). … I share the view, expressed by the Advocate General (P VerLoren van Themaat) in relation to the concept of a taxable person under art 4 of EC Council Directive 67/228 of 11 April 1967 on the harmonisation of legislation of member states concerning turnover taxes-structure and procedures for application of the common system of value added tax (JO L71 14.4.67 p 1303 (S Edn 1967 p 16))(the Second Directive) that '*it is not the aim but rather the nature of the activities in question which is relevant'* when determining what constitutes an economic activity (see *Staatssecretaris van Financiën v Hong Kong Trade Development Council* (Case 89/81)[1982] ECR 1277 at 1293)."[17]

In *BLP Group plc v Customs and Excise Commissioners* (Case C-4/94) (Case C-4/94) [1995] ECR I-983, the Court held at paragraph19:

> "Paragraph 5 [of article 17 of the Sixth Directive] lays down the rules applicable to the right to deduct VAT where the VAT relates to goods or services used by the taxable person 'both for transactions covered by paragraphs 2 and 3, in respect of which value added tax is deductible, and for transactions in respect of which value added tax is not deductible'. The use in that provision of the words 'for transactions' shows that to give the right to deduct under para 2, the goods or services in question must have a direct and immediate link with the taxable transactions, *and that the ultimate aim pursued by the taxable person is irrelevant in this respect*." [18]

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15 Italics supplied.

16 "Furthermore, as the court has repeatedly held (*see van Tiem v Staatssecretaris van Financiën* (Case C-186/89) [1990] ECR I-4363 at 4386, para 17), art 4 of the Sixth Directive confers a very wide scope on value added tax, comprising all stages of production, distribution and the provision of services."

17 Italics supplied.

18 Italics supplied.

All these cases were cited by me in *BUPA Hospitals Ltd v Commissioners of Customs and Excise* [2006] STC 967, which was heard by the European Court of Justice together with *Halifax plc v Commissioners of Customs and Excise* [2006] STC 919. The Court went so far as to hold that transactions constitute an "economic activity" even when they are effected for the sole purpose of obtaining a tax advantage, without any other economic aim.

The Court said:

> "55. As the Court held in para 26 of its judgment in *EC Commission v Greece* (Case C-260/98) [2000] ECR I-6537, an analysis of the definitions of taxable person and economic activities shows that the scope of the term economic activities is very wide, and that the term is objective in character, in the sense that the activity is considered per se and without regard to its purpose or results (see also *EC Commission v Netherlands* (Case 235/85) [1987] ECR 1471, para 8, and, to that effect, in particular *Rompelman v Minister van Financiën* (Case 268/83) [1985] ECR 655, para 19, and *Zita Modes Sàrl v Administration de l'Enregistrment et des Domaines* (Case C-497/01) [2005] STC 1059, [2003] ECR I-14393, para 38).
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> 56. That analysis and that of the terms 'supply of goods' and 'supply of services' show that those terms, which define taxable transactions under the Sixth Directive, are all objective in nature and apply without regard to the purpose or results of the transactions concerned (see, to that effect, *Optigen Ltd v Customs and Excise Comrs* (Joined cases C-354/03, C-355/03 and C-484/03) [2006] STC 419, [2006] 2 WLR 456, para 44).
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> 57. As the Court held in para 24 of its judgment in *BLP Group plc v Customs and Excise Comrs* (Case C-4/94) [1995] STC 424, [1996] 1 WLR 174, an obligation on the tax authorities to carry out inquiries to determine the intention of the taxable person would be contrary to the objectives of the common system of VAT of ensuring legal certainty and facilitating the application of VAT by having regard, save in exceptional cases, to the objective character of the transaction in question."

6.4 Limits on Scope of "Economic Activity": Need for Organisation and Continuity

Now there are some clearly accepted limits on the meaning of "economic

activity". One requirement appears to be that an economic activity requires a degree of organisation and continuity. For example, a person who sells second-hand furniture on a systematic basis will be carrying on an economic activity whereas an individual who sells off surplus furniture will not. As Advocate General Poiares Maduro said in *Banque Bruxelles Lambert SA (BBL) v Belgium* (Case C-8/03) [2004] STC 1643 at paragraph 10, referring to the decision in *Floridienne SA v Belgium* (Case C-142/99) [2000] STC 1044:

> "According to that judgment, 'economic activity' must therefore be construed as meaning an activity likely to be carried out by a private undertaking on a market, organised within a professional framework and generally performed in the interest of generating profit".

An analysis of the Floridienne decision is also given in the Opinion of Advocate General Leger in *Empresa de Desenvolvimento Mineiro SGPS SA (EDM) v Fazenda Pública* (Ministério Público, intervening) (Case C-77/01) [2005] STC 65:

> "41. As to the first of those conditions [loans in themselves constituting an economic activity of the operator], the Court described the circumstances in which the granting of such loans could, in itself, be considered an economic activity within the meaning of Article 4(2) of the Sixth Directive.
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> 42. According to the Court, that activity must not be carried out merely on an occasional basis and must not be confined to managing an investment portfolio in the same way as a private investor. On the contrary, it must be carried out with a business or commercial purpose characterised, in particular, by a concern to maximise returns on capital investment. (*Floridienne and Berginvest* [2000] ECR I-9567 para 28)
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> 43. The Court did not explain specifically what is meant by 'business or commercial purpose'. It is not easy to give a more specific definition of that concept on a theoretical approach. (In Case C-230/94 *Enkler* [1996] ECR I-4517, paragraphs 28 and 29, the Court held that where, by reason of its nature, property can be used for both economic and private purposes, it is necessary to examine all the circumstances in which the person concerned uses the property and to compare those circumstances, where appropriate, with those in which the corresponding economic activity is usually carried out. It also held that criteria based on the results of the activity in question cannot in themselves be a decisive factor but that the actual length of the period for which

> the property is hired, the number of customers and the amount of earnings may be taken into account).
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> 44. The business purpose, as I see it, involves a holding company introducing permanent human and logistical resources arranged in the same way as the resources of a credit institution and on a greater scale than the resources belonging to a private investor which are used merely for his own needs."

In so far as these statements indicate that there must be "permanent human and logistical resources arranged in the same way as" an undoubted trader, and an organisation with a professional framework, they may not be helpful to large or more organised charities, the activities of which will clearly be carried on on a systematic, business-like basis.

6.5 Limits on Scope of "Economic Activity": Relevance of Motive

6.5.1 Where Motive is Relevant

In so far as the statements of Advocate General Leger indicate that the aim of generating profits will be the normal situation in any economic activity, they will be helpful, in that such will not be the aim of any charity. However, in my own view, it would unwise to place too much reliance on them as they were clearly made in a context where the concern was to distinguish between investment activities of private investors and those of a business.

For motive can be important in determining whether the sale of investments, such as shares, which produce passive income, is an economic activity. United Kingdom income tax law draws a distinction between a mere investor and a trader. Motive is here very important. The European Court of Justice appears to draw much the same distinction. The trader, whose motive is to make an income out of buying and selling shares, will be carrying on an economic activity, whereas the mere investor will not. See, for example, *Wellcome Trust Ltd v Customs and Excise Commissioners* (Case C-155/94) [1996] STC 945.

As a matter of principle, purpose is to an extent relevant in determining whether a person is carrying on a *trade*. For carrying on an activity in the hope or expectation of profit is the hallmark of a trade. It is the profit motive which determines the commercial nature of the profits and thus, in most systems, brings them within the charge to tax on income, which they would escape were they, say, casual profits arising from the purchase and sale of a capital asset by a private individual.

6.5.2 Value Added Tax As A Tax on Consumption

Value added tax, by contrast, is a tax on consumption which is only at a technical level levied on the person making the supply and is in reality levied on the recipient of the supply. See the First Directive Article 2, which provides:

> "The principle of the common system of value added tax involves the application to goods and services of a general tax on consumption exactly proportional to the price of the goods and services, whatever the number of transactions which take place in the production and distribution process before the stage at which tax is charged." [19]

The motive of the supplier in making the supply should thus in principle make no difference to the taxability of the supply. Any system of tax on consumption, such as value added tax, needs to ascertain who is accountable for the tax and to fix a reference point at which "consumption" occurs. As it is not practicable to enforce payment from the ultimate consumer, the person accountable for the tax is the last commercial supplier, i.e. the immediate supplier to the consumer.

This is borne out by the language of the Sixth Directive, Article 4 of which provides:

> "1 "Taxable person" shall mean any person who independently carries out in any place any economic activity specified in paragraph 2, *whatever the purpose* or results *of that activity*.
>
> "2 The economic activities referred to in paragraph 1 shall comprise all activities of producers, traders and persons supplying services including mining and agricultural activities and activities of the professions. The exploitation of tangible or intangible property for the purpose of obtaining income therefrom on a continuing basis shall also be considered an economic activity. …" [20]

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19 See also the Sixth Directive article 2 and the following recital to the First Directive: "Whereas a system of value added tax achieves the highest degree of simplicity and of neutrality when the tax is levied in as general a manner as possible and when its scope covers all stages of production and distribution and the provision of services"

20 Italics supplied. Article 4.5 of the Sixth Directive, which provides that certain persons are not taxable persons in so far as they carry on governmental functions, is also indicative that "economic activity" is very wide, in that it *prima facie* covers state services, the provision of which will not be by way of trade or even commercial. Supplies can be made on a subsidised basis. There is no need for a profit motive. All that matters is that the supply has been effected for a consideration.

Motive is thus as a matter of principle in general irrelevant. Article 4.1 stresses "whatever the purpose". If there is an economic activity, then purpose is irrelevant. This is consistent with the substance of value added tax as being a tax on consumption.

The Court in *BLP Group plc v Customs and Excise Commissioners* (Case C-4/94) (Case C-4/94) [1995] once again emphasised, at paragraph 24, the objective nature of value added tax:

> "Moreover, if BLP's interpretation were accepted, the authorities, when confronted with supplies which, as in the present case, are not objectively linked to taxable transactions, would have to carry out inquiries to determine the intention of the taxable person. Such an obligation would be contrary to the VAT system's objectives of ensuring legal certainty and facilitating application of the tax by having regard, save in exceptional cases, to the objective character of the transaction in question."

6.5.3 *Morrison's Academy*

Customs and Excise Commissioners v Morrison's Academy Boarding Houses Association[21] was a case decided by the Inner House of the Court of Session of Scotland.[22] The taxpayer ('the association') was a charity, the principal objects of which were to maintain boarding house for the accommodation of resident pupils at Morrison's Academy'. The association owned and operated boarding houses in which, pupils of the academy were accommodated. The association charged fees in respect of the goods and services provided for the pupils accommodated. The association's affairs were managed so that neither a profit was made nor a loss incurred in the conduct of its activities.

The association was admittedly a taxable person. There was no argument that it did not make supplies. It contended that it did not make supplies of accommodation to pupils "in the course or furtherance of a business". It argued unsuccessfully that a profit motive is an essential feature of any form of 'business'.

Lord Emslie said:

> "I can discover nothing in the natural meaning of the word 'business' so to restrict its scope and there is nothing in the context of the taxing provisions as a whole to require one to read 'business' in such a narrow way. *The tax is, after all, not a tax on profit or income but on taxable supplies by*

21 [1978] STC

22 the highest court in Scotland below the House of Lords

> *taxable persons and to make liability to tax depend on the motive with which activities were continuously carried on would lead to the unreasonable result that where two taxable persons make identical taxable supplies in course of carrying on an identical activity or occupation, in which each makes the same loss, or neither a profit nor a loss, and one has sought to make profit and the other has not, only the former would be accountable for value added tax.*"[23]

Lord Cameron agreed:

> "*Neither the purpose for which the supplies are made nor the expectation or hope of gain or profit arising therefrom are matters which prima facie are relevant to the issue of liability to tax. …*"

It has been said that "it is quite clear that a business is being carried on where activities are the direct, permanent and necessary extension of a taxable activity of another person (see *Floridienne SA v Belgium* (case C-142/99) [2000] STC 1044 at para 27) and that that was the case in *Morrison's Academy,* as the provision of accommodation was a direct, permanent and necessary extension of the taxable activity of the school. Accordingly, it might be argued, the decision that the absence of a profit motive could not prevent something which was otherwise clearly a business was unsurprising. Hence, it might be argued that the case did not decide that a person whose principle concern was making taxable supplies must be carrying on a business, and his motives for so doing could be ignored." I have to state, however, that in my own view, these arguments are misconceived.

6.5.4 *Lord Fisher*

Another English case which might be relied on as showing that motive is important is *Customs and Excise Comrs v Lord Fisher* [1981] STC 238. It is one of the older English cases, decided without reference to the Sixth Directive or to the case law of the European Court of Justice. It has survived remarkably well, and was even approved by the House of Lords in 1999 in the *ICAEW* case, discussed below. Moreover, these criteria appear to be applied by Her Majesty's Revenue & Customs in determining whether an activity amounts to a business (see Internal Guidance V1-6 Business/Non-business at 2.6).

In *Lord Fisher*, the issue was whether, in requiring a contribution from guests amounts towards the costs of a pheasant shoot, Lord Fisher was carrying on a business activity for the purposes of VAT. In considering the above statement of the Lord President in Morrison's Academy Gibson J stated:

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23 Italics supplied.

> "In my judgment it is essential to have in mind, in seeking to apply these statements to any other case, that their Lordships in the Morrison's Academy case were, as I have said, dealing with an activity which was in all respects indistinguishable from the business of a boarding house keeper save for the matter of profit; they had, I believe, no intention of dealing with, or of laying down propositions applicable to, an activity as in this case which was in all respects indistinguishable from the private pleasures of a private shoot save for the matter of contributions to expenses.
>
> I am moreover confident that Lord Cameron did not intend to say that in all cases the absence of the purpose of gain is irrelevant to the issue whether the potential taxpayer is carrying on a business. It seems to me that there are many activities in which a potential taxpayer may supply services for a consideration within the meaning of s 5(8) of the [Finance Act 1972] and which will be so different from the ordinary concept of 'business' that the presence or absence of the purpose of gain would be highly relevant to the determination of the question whether he was carrying on a business".

Gibson J rejected the argument that a business was being carried on. He considered that any activity which is not more than an activity of pleasure and enjoyment is not a business, and in any event the taking of contributions was not the predominant concern of the taxpayer in organising the pheasant shoot. No doubt, in the case of some charities, e.g. cultural charities, there could well be some measure of pleasure and enjoyment on the part of those involved. Yet I doubt that they would be held not to be carrying on a business on that account, any more than I would be held not to be carrying on a business in the course of my profession as a barrister, simply because I derive an enormous amount of pleasure and enjoyment from it.

The judgment is more important in that the judge referred to six indicia or criteria

for determining whether an activity is a business.[24] These were as follows:

> "(a) whether the activity is a 'serious undertaking earnestly pursued', … or 'a serious occupation, not necessarily confined to commercial or profit-making undertakings', …;"

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24 It is to be noted that in referring to these criteria Gibson J was merely making a note of the Commissioners' submissions. He was not laying down a test. However, in later cases he has been treated as doing so. And the fact that it was the Commissioners of Customs and Excise (now Her Majesty's Commissioners of Revenue and Customs) who advance the test is helpful on a pragmatic level in negotiating with them.

> "(b) whether the activity is an occupation or function actively pursued with reasonable or recognisable continuity…;"
>
> "(c) whether the activity has a certain measure of substance as measured by the quarterly or annual value of taxable supplies made…;"
>
> "(d) whether the activity was conducted in a regular manner and on sound and recognised business principles…;"
>
> "(e) whether the activity is predominantly concerned with the making of taxable supplies to consumers for a consideration…;"
>
> "(f) lastly, whether the taxable supplies are of a kind which, subject to differences of detail, are commonly made by those who seek to profit by them…"

A general caveat: it has been suggested that these criteria would only seem to be of use in determining absolutely that there is a business because they are all satisfied and that it is possible that five of the six criteria can be satisfied, but an activity is still not regarded as a business. I would not place too much reliance on that.

6.5.5 *Morrison's Academy v Lord Fisher*

The reference in *Morrison's Academy* to activities which are "predominantly concerned with the making of taxable supplies to consumers for a consideration" (criterion (e)) has been advanced as providing the central test as to whether there is a business for VAT purposes. While that could be the case, I have certain important reservations. The first reservation is that the reference to consumers is misleading. A wholesaler who deals only with retailers is clearly carrying on a business. The second is that the test involves circularity. For if a person is not making supplies in the course or furtherance of a business, then they cannot be taxable supplies. Hence, one has to expand the criterion to read "predominantly concerned with the making of supplies which would be taxable supplies if made for a consideration by a taxable person in the course or furtherance of a business". The third is that the word "taxable" should be omitted, as a person is still carrying on a business even though he makes only exempt supplies.[25] My fourth

25 In most cases, it would be academic whether he was carrying on a business, as, if he did not make sufficient taxable supplies, he would not be required to register and hence would not be a taxable person. It is no doubt for that reason that the word "taxable" crept into the criterion. However, in some contexts, and in particular, in the context of Value Added Tax Act 1994 schedule 8 Group 5, a charity which is going to use premises for making exempt supplies e.g. of education, in the course of a business will be denied the benefit of zero-rating.

reservation is that while in most cases (as in the present) it is quite clear that other important conditions, such as continuity, organisation and scale, are satisfied, so that it is understandable that this criterion is thought to be central, there may well be cases where those other conditions are not satisfied.

Criticism has been made of criterion (e), quite apart from the reservations I have mentioned. It is said that much depends how that criterion is interpreted and it is claimed that the criterion has been applied in two very different ways. On the one hand, it is said, the concern is to identify what, if any, supplies are made by the taxable person for a consideration. In the absence of either supplies being made or consideration (which does not include donations and certain grant) being received, there is no business activity (see e.g. *Whitechapel Art Gallery v HMCE* [1986] STC 156, one of my early cases). I agree that that is one legitimate use to which the test may be put.

It is also said that the test is used in this way to establish that a business exists by firstly establishing that supplies are made for a consideration; if the making of those supplies is what the person is predominantly concerned with, then it is concluded that he is predominantly concerned with making supplies for a consideration and so is operating in a business. I would not disagree with this, except that I would not agree that the converse necessarily holds, i.e. I would not agree that it follows that if he is not predominantly concerned with making supplies, then he is not carrying on a business. For example, a charity which owns a museum to which the public are permitted access free of charge will be carrying on a business in so far as it runs a shop or restaurant on the premises, even though these activities are ancillary and not its predominant concern.

It is said that "the second means by which the test is said to be applied is by considering the nature of the activities themselves, and why the supplies are being made. If they are being made principally to ensure that the consideration is received, then a business is being operated. If, however, the supplies are being made principally for a different reason, and the receipt of consideration is simply to facilitate their being made, then there is not a business." I would not myself set great store by this argument as, in my view, *Morrison's Academy* is authority directly against this view.

6.5.6 The Alleged Predominant Concern Test

I mentioned above that the so-called predominant concern test has been in my view discredited. It was advanced before the European Court of Justice in *Wellcome Trust Ltd v Customs and Excise Comrs* (Case C-155/94) [1996] STC 945 where the Court rejected it, stating at paragraph 40:

> "… in view of the foregoing, whether or not the sale of shares and other securities is the predominant concern of the activity in the course of which the sales in question took place cannot affect the classification, for the purposes of art 4 of the Sixth Directive, of the investment activity of the claimant in this case".

It is said that this comment was made in view of the conclusion that the sale of the shares by the trust must "be regarded as confining its activities to managing an investment portfolio in the same way as a private investor" and that the Court was therefore more concerned with the nature of the activities themselves, rather than the fact that their result was the making of supplies for a consideration. That is not my reading of the judgment.

Advocate General Lenz (at paragraph 39) also rejected the predominant concern test:

> "The Commission, in contrast, points out that the notion of 'predominant concern' is not used in the directive. Under the directive, it is the inherent nature of the activity itself that is the vital consideration, not whether that activity is or is not predominant. I also take the view that, in order to determine whether an activity is an economic activity for the purposes of art 4(2), it is not appropriate to consider whether the activity is of predominant concern. To illustrate this point, I would refer to the activities of the Wellcome Trust in respect of which it is registered as a taxable person. These relate to the sale of books, photographs and so forth, none in any event an activity which is of predominant concern. That notwithstanding, these activities must be regarded as being economic activities for the purpose of the Sixth Directive, whereas the principal occupation of the trust, namely the management of assets, cannot be regarded as an economic activity within the meaning of the Sixth Directive".

I would myself respectfully agree. It is said, however, that, while, on the basis of this paragraph, the relevant test is regarded as one of determining the inherent nature of the activity in question, it is not clear the practical extent to which the 'inherent nature' of an activity differs from the 'predominant concern' of the same activity unless one regards the 'predominant concern' test as looking at results[26] of the activity (i.e. the making of taxable supplies). It is admitted that the different formulation requires an objective consideration of the matter, rather than by reference to the subjective intent of the taxable person, yet it is claimed that this does not require one to ignore the reasons, objectively determined, for the activity

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26 The words "results" is here used in a different sense than in Article 4.1 of the Sixth Directive, where is clearly refers to financial results, i.e. profit or loss.

in question in favour of its results.

This is an interesting argument, which I find quite unconvincing, but then that is partly because I cannot understand it.

6.5.7 *ICAEW*

The high-water mark of United Kingdom judicial authority which might be adduced in favour of the proposition that a charity which makes supplies in the course of the actual carrying out of a primary purpose of the charity (and not simply to make money to be applied for its charitable purposes) is not thereby carrying on a business is the decision of the House of Lords in *Institute of Chartered Accountants in England and Wales v Customs and Excise Comrs* [1999] STC 398. The authority is rather more authoritative than most in that the lead speech was given by Lord Slynn, who had previously been a judge of the European Court of Justice. In that case the issue was whether the ICAEW in carrying out its regulatory functions of licensing accountants was acting in the course of business for the purposes of VAT. In finding that there was no business, Lord Slynn made the following observations:

> "If read literally, it can be argued as Mr Andrew Thornhill QC on behalf of the institute has done, that in granting these licences for a fee, the institute is supplying services in the course of a business, or is supplying services for consideration in the carrying on of an economic activity. But so far as the Sixth Directive is concerned, the Court of Justice of the European Communities has made it clear that it is not enough merely to point to the fact that there is a supply of services in return for a money payment and some loose economic connection, but that the activities must be of an 'economic nature' (see *Polysar Investments Netherlands BV v Inspecteur der Invoerrechten en Accijnzen, Arnhem* (Case C-60/90) [1993] STC 222 at 238, [1991] ECR I-3111 at 3136-3137, para 11)[27]
> …
>
> For the purposes of the Sixth Directive, it is thus not sufficient that what is done can be described as an activity of the professions for the purposes of art 4(2), nor that it was a supply of services for consideration for the purposes of art 2(1). It must still be an economic activity."

Lord Slynn went on to draw a distinction between cases where "the persons concerned were carrying out activities for their own account in the way that professional men ordinarily do, even if the activities were carried out on behalf of

27 *Polysar* was an investment case, similar to *Wellcome Trust* and hence some way from ICAEW.

the state"[28] which could amount to business or economic activities, and cases where a person was carrying on activities which were "the activities of a public authority and not of an economic nature which fell within the competition provisions of the EC Treaty". The result of the case was that the regulatory activities of ICAEW were not considered to be sufficiently economic in nature to constitute a business.

There is clearly a line to be drawn between *ICAEW* and *Morrison's Academy*. In the one case, the ICAEW was entrusted with functions which were quasi-governmental. It was not possible for anyone who chose to set up a business of licensing accountants for profit. In the other case, the Academy was providing a service which could be provided by anyone from the Barclays at the Ritz to Old Mother Riley at her boarding house.

6.5.8 Recent High Court Authority

Two recent judicial decisions to have considered the matter related to nursery and day-care facilities which were subsidised and operated on a non-profit basis. In both cases the High Court, having considered the decisions above, reached the conclusion that there was no business, these decisions are clearly very relevant. It is questionable to what extent they are sound.

In *Commissioners of Customs and Excise v Yarburgh Trust* [2002] STC 207 Patten J was concerned to determine whether the activities of a charity providing day-care facilities for children in return for a charge were made in the course of a business.

Having regard to the *Wellcome Trust* and *ICAEW* decisions he rejected any test for treating a transaction or activity as economic merely because it results in a consideration or produces income (paragraph 22). That is fine, provided one appreciates that each case turned on a special exception from the normal rule.

While accepting that the motive of the person making the supply of goods or services could not be relevant, he considered that:

> "… the exclusion of motive or purpose in that sense does not require or in my judgment allow the tribunal to disregard the observable terms and features of the transaction in question and the wider context in which it came to be carried out. This is because the transaction if looked at in isolation will not usually enable the court to decide whether it was carried out in the course or furtherance of a business … This test necessitates an inquiry by the tribunal into the wider picture. It will need to ascertain the

28 For example, independent contractors providing security services to the prison service.

> nature of the activities carried on by the person alleged to be in business, the terms upon which and manner in which these activities (including the transaction in question) were carried out and the nature of the relationship between the parties to the transaction".

Perhaps the reader of this article will be able to appreciate the subtlety of a distinction which undermines the very foundations of the general rule. I cannot.

He went on to state, at paragraph 29:

> "I accept, as I have indicated earlier in this judgment, that the fact that an essentially business operation is intended to further the charitable objects of the body which carries it out does not of itself alter the nature of the operation for VAT purposes. A charity shop run to make a profit for the charity is a business even though its object is to benefit that charity. But in that case the shop itself is not as such a charitable activity. It is merely a form of fund raising run on a commercial basis. The operation of the playgroup by contrast is itself charitable. This may not prevent it being treated as a business but its charitable nature does have to be taken into account in deciding whether in the words of Lord Slynn in the Institute of Chartered Accountants case the playgroup operation has an economic content.
>
> [30] Although it might be said in the present case that the playgroup was a serious undertaking earnestly pursued with reasonable continuity and that it was conducted regularly it is evident to me as it was to the tribunal that it is not predominantly concerned with the making of taxable supplies for a consideration. The overwhelming impression which one gets from considering the evidence before the tribunal is that this is a co-operative venture run by trained staff with the benefit of help provided by parents under the control of a committee on which parents predominate. The evidence before the tribunal included a pre-school information sheet which states that the playschool is not profit led and struggles to maintain the balance between remaining affordable and meeting its operating costs. Playschool fees are fixed on this basis. This seems to me to be a very different arrangement from that subsisting in the case of a commercial playgroup run for a profit which was an example which Miss Whipple put to me. An intention to trade at a profit is not of course an essential feature of a business but it is 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. I think that the tribunal was entitled to conclude from the evidence before it that no business user was involved in this case."

The case of the charity shop is not in point. There is no charity whose primary purpose is to provide retail therapy. The real difficulty with the judgment is that is proves too much. How is it consistent with *Morrison's Academy* and with the analysis of value added tax being a tax on consumption? And how does one reconcile the many characterisations in the Sixth Directive of supplies as being exempt, which would be entirely otiose if they were not supplies (for value added tax purposes) at all, because they were not made by a taxable person acting as such, i.e. in the course of a business / economic activity?

This decision was followed by Evans-Lombe J in *HMCE v St Paul's Community Project Ltd* [2005] STC 95. That was a case involving a nursery in which all parents were charged fees, but which was ran on a non-profit basis. Having considered the above cases, he agreed with the analysis of Patten J in the Yarburgh case, concluding (emphasis added):

> "Like Mr Justice Patten in the *Yarburgh* case, I take the view that none of this detracts from the principle of tax neutrality which was much urged upon me by Mrs Hall. That principle seeks to bring about a situation in which the treatment of businesses, for the purposes of levying VAT throughout the European Community, is the same. However it does not arise, in respect of a particular undertaking, until it has been determined that that undertaking, constitutes a taxable person. I accept that the overall policy of the Sixth Directive requires that the word 'business' must be given a very wide meaning so that it is not confined to profitable enterprises or enterprises intended to be conducted at a profit at some point. The intention or apparent intention, of those conducting the enterprise in question must be disregarded. ***It is the intrinsic nature of the enterprise, as established by evidence of what is actually being performed in order to advance it, that is important in arriving at a conclusion whether or not a particular undertaking constitutes a business***. It does not seem to me that the principle of tax neutrality assists in that process".

In considering the intrinsic nature of the enterprise Evans-Lombe J was persuaded by the approach of the ECJ in *EC v France* C-50/87 [1988] ECR 4797, infringement proceedings against France in respect of legislation restricting the deductibility of input tax in relation to certain lettings. In response to an argument by the French Government that the restrictions on input tax were necessary in cases where low rents were granted by local authorities for social reasons, the Court considered that the provisions of Article 20 sufficiently dealt with the matter. This was on the basis that there would be an adjustment under that Article "where, because of the amount of rent, the lease must necessarily be regarded as involving a concession and not as constituting an economic activity". While

Evans-Lombe J was clearly impressed with the formulation of the ECJ, it would seem to be merely acknowledging that not every supply for a consideration will amount to an economic activity, and where the consideration is incidental, it is unlikely to do so.

Having particular regard to the following facts, the judge was able to conclude that the nursery was not a business:

> "(i) The documentary evidence before the tribunal and the evidence of Dr Halliday demonstrated that St Paul's, at the material time, was undertaking its nursery activities, amongst other activities, for social reasons, namely to support disadvantaged families in the Balsall Heath area of Birmingham, itself a deprived area, and as part of the government's Sure Start programme. In so doing it had an admissions policy skewed in favour of disadvantaged and problem children.
>
> (ii) The fees charged were significantly lower than those charged by commercial nurseries notwithstanding that St Paul's was paying the higher salaries necessary to obtain the services of a higher proportion of trained staff, trained to a higher level of expertise than would normally be required.
>
> (iii) Those fees were pitched at levels designed only to cover the costs of the nursery after grants and donations. In any event the memorandum of association of St Paul's would have prevented distribution of any profit made.
>
> (iv) It follows from (ii) and (iii) above that the level of fees charged to parents of children using the facilities of St Paul's nursery amounted to a 'concession' see *EC Commission v France,* [1988] ECR 4797, cited above".

Her Majesty's Revenue & Customs do not necessarily accept that the reasoning in these two recent cases, is of general application (see Business Brief of 10 February 2005). This is not entirely surprising.

6.5.9 *University of Southampton*

A recent High Court decision in which the meaning of "business" was considered in the context of the VAT legislation namely *University of Southampton v Her Majesty's Revenue & Customs* [2006] EWHC 628 (Ch). That case involved a claim to deduct input tax referable to research which was funded by way of grants

provided by public sponsors (publicly funded research or PFR).

Although *Yarburgh* was considered by Warren J, he did not consider it relevant in cases where it was necessary to determine whether activities which do not produce a supply are economic activities (paragraph 31) although he did agree that it was necessary to look at matters in their wider context.

It is said that it is of some relevance that in considering whether the publicly funded research was an economic activity Warren J refused to give any significant weight to the fact that the public research was carried on in an identical fashion to commercial research which, it was accepted, had a business purpose; rather he preferred to look at the context in which the activities took place, saying:

> "Nor does it follow, in my view, from the finding that research, whether commercial or PFR, is carried on by the same people using the same infrastructure and to the same standards, that commercial research and PFR are therefore to be treated in the same way for VAT purposes. The context of each type of research is entirely different, not least because commercial research itself involves a supply and is for a consideration, whereas PFR has neither characteristic. The finding is, I do not dispute, a factor to be taken into account, but is certainly not conclusive and not, to my mind, particularly persuasive".

7 Charities as Bodies Governed by Public Law

I stated above that I would return to a consideration of Article 4.5 of the Sixth Directive, which provides:

> "5 States, regional and local government authorities and other bodies governed by public law shall not be considered taxable persons in respect of the activities or transactions in which they engage as public authorities, even where they collect dues, fees, contributions or payments in connection with these activities or transactions.
>
> However, when they engage in such activities or transactions, they shall be considered taxable persons in respect of these activities or transactions where treatment as non-taxable persons would lead to significant distortions of competition.
>
> In any case, these bodies shall be considered taxable persons in relation to the activities listed in Annex D, provided they are not carried out on such a small scale as to be negligible.

> Member States may consider activities of these bodies which are exempt under Article 13 or 28 as activities which they engage in as public authorities."

Thus, if a charity is a body "governed by public law", then it would not be carrying on a business at all.

The problem is to ascertain what is meant by a body "governed by public law".[29] In many continental countries, the Rule of Law as we in these islands know it does not exist. The idea that all ministers and government officials should be accountable before the normal, civil courts and that no one is above the law was seen as a heresy by the French Revolutionaries, who consequently forbad civil judges to "trouble the administration", under pain of forfeiture. That is still the case today in France and in all those Continental countries where the Tyrant of Corsica imposed French law. The only way one can challenge the actions of the administration is before the administrative courts, which, technically, merely give advice. In these countries, these is a consequently a distinction between private law and public law which is unknown in a democratic country such as the United Kingdom. A further difficulty is that, as I mentioned earlier, most Continental countries do not have a concept of charity as we know it.

There must at the least be an argument that charities are "governed by public law" within the meaning of article 5.4. Charitable trusts are sometimes referred to by the courts as "public trusts", in contra-distinction to private trusts. Charities are enforced by the Attorney-General, on behalf of the Crown as *parens patriae*. These features are much more indicative of public law than of private law. And charities must be established for purposes which are for the public benefit.

If this is the case, then the number of "businesses" carried on by charities may be rather less than is generally supposed.

8 Conclusion

It may be many years before the question when a charity is carrying on a "business" or economic activity can be answered in every case with any degree of

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29 There is a paucity of case law. In *Customs and Excise Commissioners v Isle of Wight Council* [2004] EWHC 2541 (Ch) [2005] STC 228, it was accepted by both sides that the Council was a public authority. Similarly, in *Edinburgh Telford College* [2006] CSIH 13, the Commissioners accepted in the Court of Session that the college was a "body governed by public law". However, that concession was in the circumstances not surprising, as it was pursuing an activity under a special legal regime applicable to it. In *Riverside Housing Association Ltd. v Revenue and Customs Commissioners* [2006] EWHC 2383 (Ch), Collins J did not find it necessary to adjudicate on the point.

certainty. In many cases, however, much can be done by careful planning to help ensure that a charity falls the side of the line it wishes to fall.