[2019] UKUT 0002 (TCC)

Appeal numbers: UT/2016/0201 & UT/2017/0119

VAT – Exemption for welfare services – Item 9 Group 7 Sch 9 VATA – Respondents providing day care services in England and not state-regulated – whether Item 9 breaches fiscal neutrality on basis that providers of day care services in Scotland and Northern Ireland are state-regulated and their supply of services exempt – whether Respondents' supply of services exempt – no breach of fiscal neutrality

UPPER TRIBUNAL (TAX AND CHANCERY CHAMBER)

UT/2017/0119

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS — **Appellants**

- and -

THE LEARNING CENTRE (ROMFORD) LTD — **Respondent**

UT/2016/0201

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS — **Appellants**

- and -

L.I.F.E. SERVICES LTD — **Respondent**

TRIBUNAL: Mr Justice Nugee
Judge Timothy Herrington

Sitting in public at the Rolls Building, London EC4A 1NL on 4 and 5 December 2018

Jonathan Davey QC and Natasha Barnes, instructed by the General Counsel and Solicitor for HM Revenue and Customs, for the Appellants

Eamon McNicholas, instructed directly, for The Learning Centre (Romford) Ltd

Jonathan Bremner QC, instructed by Gerald Edelman LLP, for L.I.F.E. Services Ltd

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DECISION

Introduction

1. There are two appeals before the Upper Tribunal (**"the UT"**) from decisions of the First-tier Tribunal (**"the FTT"**). They raise the same issue, which is whether provisions of the Value Added Tax Act 1994 (**"VATA 1994"**) which provide an exemption for VAT for certain welfare services infringe the EU principle of fiscal neutrality. The particular context is the provision of day care services by bodies that are neither public bodies nor charities but are private entities providing such services for profit.

2. We give the detail of the legislation below but in essence VATA 1994 has the effect that the supply of services by such a body is only exempt for VAT purposes if the body is *"state-regulated"*. In England and Wales there is no regulation of the provision of day care services as such. But in Scotland there is devolved legislation which means that the provision of day care services is regulated; and the same is true in Northern Ireland under separate devolved legislation. That means that day care services provided by commercial providers in England and Wales are not exempt and are liable to VAT at the standard rate, whereas such services in Scotland and Northern Ireland are exempt.

3. The first appeal (UT/2017/0119) concerns a company called The Learning Centre (Romford) Ltd (**"TLC"**) which provides day care services in England to vulnerable adults with learning difficulties. TLC applied to de-register for VAT on the grounds that its supplies were exempt. The Commissioners for Her Majesty's Revenue and Customs (**"HMRC"**) refused to permit TLC do so on the grounds that TLC's supplies were taxable. TLC appealed to the FTT against HMRC's decision. By a decision released on 13 June 2017 ([2017] UKFTT 0492 (TC)) the FTT (Judge Barbara Mosedale) allowed TLC's appeal on the grounds that the UK's welfare services exemption did not correctly transpose the relevant EU Directive because the UK did not have regard to the need for fiscal neutrality and the need for all private bodies in the UK providing the same service to be treated in the same manner for VAT purposes. HMRC appeal to the UT against this decision. Permission was given by the FTT (Judge Mosedale) on 17 August 2017.

4. The second appeal concerns a company called L.I.F.E. Services Ltd (**"LIFE"**) which also provides day care services in England, in this case to adults with a broad spectrum of disabilities. LIFE appealed to the FTT against a determination of HMRC that its services were taxable. By a decision released on 23 June 2016 ([2016] UKFTT 444 (TC)) the FTT (Judge Charles Hellier and Mr William Haarer) allowed LIFE's appeal on the grounds that the relevant provisions of VATA infringed the principle of fiscal neutrality because they exempted charities and not providers such as LIFE. The question of fiscal neutrality as between the various nations of the UK (which we will call **"the devolved nations issue"**) was not raised at this hearing.

5. HMRC appealed to the UT, with permission granted by Judge Hellier on 20 September 2016. An initial hearing of the appeal in the UT (Mann J and Judge Herrington) took place in October 2017. Shortly before that hearing LIFE sought to introduce the argument that there had been a breach of fiscal neutrality caused by different treatment across the devolved nations, relying on the FTT decision in the TLC case. The UT decided that the appropriate course was for argument on the devolved nations issue to be adjourned and heard at the same time as the TLC appeal, and proceeded to hear argument on the other issues. By a decision released on 18 December 2017 ([2017] UKUT 0484 (TCC)) the UT found in favour of HMRC on those issues, with the result that HMRC's appeal would be allowed unless LIFE were successful on the devolved nations issue.

6. By directions given on 11 January 2018 the UT (Judge Herrington) therefore directed that HMRC's appeal in the TLC case should be heard together with the remaining issues in the LIFE case (that is the devolved nations issue). This is that hearing.

EU legislation

7. The current EU Directive on VAT is Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax, commonly known as the Principal VAT Directive (**"the Principal Directive"**).

8. Title IX of the Principal Directive is headed "Exemptions".

9. Chapter 1 of Title IX, headed "General Provisions", consists of Art 131 which provides:

> "The exemptions provided for in Chapters 2 to 9 shall apply without prejudice to other Community provisions and in accordance with conditions which the Member States shall lay down for the purposes of ensuring the correct and straightforward application of those exemptions and of preventing any possible evasion, avoidance or abuse."

10. Chapter 2 of Title IX (Arts 132 to 134) is headed "Exemptions for certain activities in the public interest". Art 132(1)(g) provides as follows:

> "1. Member States shall exempt the following transactions:
>
> …
>
> (g) the supply of services and of goods closely linked to welfare and social security work, including those supplied by old people's homes, by bodies governed by public law or by other bodies recognised by the Member State concerned as being devoted to social wellbeing."

11. The Principal Directive replaced the previous VAT directive, namely the Sixth Council Directive of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes (77/388/EEC), commonly known as

the Sixth VAT Directive (**"the Sixth Directive"**). This contained a similar exemption in Art 13A(1)(g) in almost, but not quite, identical terms to Art 132(1)(g) of the Principal Directive.

UK legislation

5 12. The current UK statute in relation to VAT is VATA 1994.

13. By s. 31(1) VATA 1994, a supply of goods or services is an exempt supply if the supply is of a description specified in Schedule 9.

14. Schedule 9 refers to a number of different types of supply of goods and services, arranged in Groups. Group 7 is headed "Health and Welfare".

10 15. Item 9 of Group 7 (**"Item 9"**) in its current form (which it has been in since 31 January 2003) is as follows:

> "The supply by –
>
> (a) a charity,
>
> (b) a state-regulated private welfare institution or agency, or
>
> 15 (c) a public body,
>
> of welfare services and of goods supplied in connection with those welfare services."

16. By s. 96(9) VATA 1994, Schedule 9 is to be interpreted in accordance with the notes contained in the Schedule.

20 17. Note (6) to Group 7 of Schedule 9 (**"Note (6)"**) provides as follows:

> "In item 9 "welfare services" means services which are directly connected with –
>
> (a) the provision of care, treatment or instruction designed to promote the physical or mental welfare of elderly, sick, distressed or disabled 25 persons,
>
> (b) the care or protection of children and young persons, or
>
> (c) the provision of spiritual welfare by a religious institution as part of a course of instruction or a retreat, not being a course or a retreat designed primarily to provide recreation or a holiday,
>
> 30 and, in the case of services supplied by a state-regulated private welfare institution, includes only those services in respect of which the institution is so regulated."

18. Note (8) to Group 7 of Schedule 9 (**"Note (8)"**) provides as follows:

"In this Group "state-regulated" means approved, licensed, registered or exempted from registration by any Minister or other authority pursuant to a provision of a public general Act, other than a provision that is capable of being brought into effect at different times in relation to different local authority areas.

Here "Act" means –

(a) an Act of Parliament;

(b) an Act of the Scottish Parliament;

(c) an Act of the Northern Ireland Assembly;

(d) an Order in Council under Schedule 1 to the Northern Ireland Act 1974;

(e) a Measure of the Northern Ireland Assembly established under section 1 of the Northern Ireland Assembly Act 1973;

(f) an Order in Council under section 1(3) of the Northern Ireland (Temporary Provisions) Act 1972;

(g) an Act of the Parliament of Northern Ireland."

The facts – TLC

19. Although the FTT in the TLC case heard oral evidence, there was no substantial dispute of fact. We can summarise the facts by reference to the FTT decision as follows (numbers in square brackets referring to paragraphs of the FTT decision):

(1) TLC is a company owned by Mr and Mrs Spence, who are its directors and shareholders [6]. Both have relevant qualifications and experience [8].

(2) TLC provides day care to vulnerable adults with learning difficulties, referred to as "students". This consists of education (geared towards teaching the students independent living), activities and entertainment; it also provided meals and, where required, assistance with eating, administering medication and personal care, and transport for the students between their homes and the facility [8]. HMRC accepted that these services were "welfare services" within Item 9 and Note (6) [9].

(3) The directors' evidence of the high level of care provided was not disputed [9]. TLC was situated in the London Borough of Havering (**"Havering"**) and Havering had provided a very positive report on its services following an inspection which TLC consented to, but which was not carried out under any statutory powers [9], [14].

(4) TLC would only accept students that had been assessed by their local authority and had a care plan. Most of TLC's students were residents of Havering although some were from neighbouring boroughs [19].

(5) Payment of TLC's fees mostly came from the local authorities. In the case of Havering and some other boroughs, they made payments to the parent/carer of the students who would then pay TLC; one of the neighbouring boroughs paid TLC direct. A small minority of TLC's fees was paid out of the parent/carer's own funds [19]-[21].

(6) Under the Health and Social Care Act 2008 certain activities involving or connected with the provision of health or social care in England are regulated activities, the regulator being the Care and Quality Commission (**"CQC"**). But personal care is not a regulated activity unless it is provided at a place where the recipient of the care is living. That means that day care for vulnerable adults was not regulated by the CQC and TLC was therefore not regulated in relation to the services it provided [25]-[29].

20. The FTT also referred to the position in the other parts of the UK (Scotland, Northern Ireland and Wales), social care being a devolved issue. There was no dispute that the position was as follows:

(1) In Scotland a private care home providing day care to vulnerable adults was subject to regulation by the Care Inspectorate [35].

(2) In Northern Ireland the position was the same, the regulator being the Regulation & Quality Improvement Authority [36].

(3) In Wales however the position was the same as in England. Providers of day care to vulnerable adults were not subject to regulation by the Welsh equivalent of the CQC (the Care & Social Services Inspectorate Wales).

Decision of the FTT – TLC

21. We can summarise the decision of the FTT in the TLC case as follows:

(1) TLC contended that it was state-regulated because it was obliged to ensure that its staff had certificates from the Disclosure and Barring Service under the provisions of the Safeguarding Vulnerable Groups Act 2006. The FTT rejected this contention [51]-[57]. There is no appeal against this conclusion.

(2) TLC contended that in enacting Item 9 the UK had failed to properly implement the relevant directives. The argument was put forward under 6 heads [62]. The FTT rejected the first 4 of these, namely

(a) that it was sufficient that an entity was acknowledged by one arm of government or another to be supplying welfare services [63]-[76]; (b) that the UK should have amended the exemption for welfare services when the Principal VAT Directive replaced the Sixth Directive [77]-[85]; (c) that the UK must have exercised its discretion improperly [86]-[104]; and (d) that there was a breach of fiscal neutrality in that supplies made by local authorities such as Havering were exempt [105]-[114]. TLC has not sought to re-open any of these points on appeal.

(3) The FTT however accepted the fifth way in which TLC put its case, namely that there was a breach of fiscal neutrality in that providers of day care services in Scotland and Northern Ireland would be regulated and hence the supply of their services would be exempt whereas providers of day care services in England, even if supplying services which were identical, could not be regulated and hence their supplies would be taxable (in other words, the devolved nations issue) [115]-[159].

(4) The final way in which TLC put its case was that there was a breach of fiscal neutrality as compared with charities (as decided by the FTT in the LIFE case). The FTT in the TLC case did not find it necessary to reach a conclusion on this [165]-[181]. TLC has not sought to reopen this issue on appeal.

22. The overall result was that the FTT allowed TLC's appeal and held that its supplies were and always had been exempt. We should cite two passages where the FTT stated its conclusions. The first is at [158] (a paragraph which Mr McNicholas, who appeared for TLC, placed particular emphasis on) and [159] where the FTT gave its conclusions on the devolved nations issue as follows:

> "158 HMRC's point is that there is an objective difference between the services provided in Scotland to the services provided in England, in that the former can only be made by the regulated entities, and the latter only by unregulated entities. I do not accept that this is a valid distinction because the services provided could be identical: a day care provider in England providing care of the same quality as a regulated provider in Scotland nevertheless is not exempt. Indeed, TLC's evidence on the high quality of the services it provided was not disputed and it has been informally successfully vetted by Havering Healthwatch (§14) and no doubt it considers it would carry on providing exactly the same services if it was regulated. But what matters is that there is in law discrimination because in England day care providers do not have the possibility of being regulated and therefore cannot qualify for exemption, whereas they do in Scotland and Northern Ireland.
>
> 159 My conclusion is that the UK has unlawfully exercised the discretion conferred on it by Art 132(1)(g) in choosing the regulation of welfare

facilities as the criteria by which suppliers devoted to social wellbeing are 'recognised' for exemption and that is because the law on regulation is devolved, leading to discrimination in VAT treatment between different suppliers offering identical services but situated in different regions of the UK."

23. The other is at [182]-[183] where the FTT stated its overall conclusion as follows:

> "182 This appeal is allowed. Reverting to the common or related issues of law mentioned at §4, my conclusion on the question of 'state-regulation' is against the appellant but my conclusion on the second issue is in favour of the appellant. The UK's welfare services exemption did not correctly transpose Art 132(1)(g) of the Directive because the UK did not have regard to the need for fiscal neutrality and the need for all private bodies in the UK providing the same service to be treated in the same manner for VAT purposes. In particular, by choosing 'state-regulation' as the criterion by which to 'recognise' certain bodies devoted to social wellbeing, it chose a criterion that led to discrimination between suppliers within the UK because some of the devolved regions have more strict regulation requirements.
>
> 183 As the UK's implementation of the welfare services exemption was unlawful, the appellant is entitled to rely on the direct effect of Art 132(1)(g) and as a body devoted to social wellbeing its supplies were and always have been exempt."

The facts – LIFE

24. As with the TLC case, although the FTT heard oral evidence, there was no dispute of fact. We can take the facts from the summary given by the UT in its first decision in the appeal as follows:

> "9 LIFE is a limited company which is not a non-profit-making organisation. It provides day services for adults with a broad spectrum of disabilities. Services are provided at various locations provided by LIFE away from the residences of the relevant clients. Services include providing forms of exercise, and teaching how to cope with everyday living.
>
> 10 Gloucestershire County Council monitors and inspects the provision of the services which are provided under a formal care plan agreed with the social services department of Gloucestershire County Council. LIFE is approved and registered with Gloucestershire County Council to provide the services on its behalf to the clients and is paid by the Council to do so. In some cases, the recipient of the services contracts for their provision directly with LIFE and LIFE is paid by the recipient out of the budget provided by the Council. The Council was involved in setting the terms of the care and inspected LIFE regularly."

To that summary we add that the FTT referred to the guidelines under which Gloucestershire County Council monitored and inspected LIFE's service provision as "similar to, and possibly more exacting than" those applied by the CQC; and that LIFE's outcomes were reviewed regularly by the Adult Social Care Directorate of the Council (FTT decision at [11]).

Decisions of the FTT and the UT – LIFE

25. We can summarise the decision of the FTT in the LIFE case as follows:

(1) LIFE contended that it was "state-registered" either because it was exempted from registration, or on the basis that it was approved or registered by Gloucestershire County Council. The FTT rejected these contentions and held that LIFE's supplies were not exempted by Item 9 [30]-[39]. LIFE did not seek to reopen this point on appeal.

(2) LIFE next argued that Art 132(1)(g) did not require the supplies to be by any particular type of supplier. That construction was rejected by the FTT which held that the services exempted by Art 132(1)(g) are limited to those supplied by public bodies or those recognised by the State as devoted to social welfare [43]-[50]. LIFE did not seek to reopen this point either.

(3) The FTT however accepted LIFE's argument that Item 9 breaches the principle of fiscal neutrality by recognising charities and not recognising LIFE [51]-[98].

26. HMRC appealed to the UT. In the UT's first decision, it decided that the FTT was wrong on the fiscal neutrality point. At [53] it said that the UK had adopted two criteria for determining which non-public bodies should be entitled to the exemption, being regulated or being a charity, and that to be able to claim that its exclusion from the class breached the principle of fiscal neutrality LIFE had to be able to demonstrate that it fell within the same class as one or other of those classes. At [55]-[57] it held that LIFE could not bring itself within the same class as either a regulated body or a charity, and hence that LIFE could not demonstrate a breach of the principles of fiscal neutrality.

27. In the present hearing Mr Davey QC, who appears on behalf of HMRC, relied on what the UT said at [55]. This was as follows:

> "55 Applying that to the present case, the conferring of the exemption on a regulated body is plainly a rational choice open to the United Kingdom under the above criteria. It is sufficiently certain, and paragraph 57 of *Kingscrest* demonstrates the acceptability and rationality of regulation as a criterion. There is no way in which LIFE can equate itself with entities which are subject to the sort of regulation regime which is applied to regulated bodies. Those bodies are obliged to conform to certain standards. For LIFE that is optional, even if it chooses for the time being to do so."

28. The UT then considered, and rejected, a new argument by LIFE that it was state-regulated on the basis that Gloucestershire County Council approved or registered it under the Care Act 2014 [59]-[75].

29. As already referred to, the UT directed that LIFE's other new argument, the devolved nations issue, should be determined at this hearing. That is the only issue that remains for us to determine.

HMRC's Grounds of appeal

30. Mr Davey put forward 3 grounds of appeal on behalf of HMRC:

(1) **Ground 1**

Ground 1 is that Item 9 does not cause differing treatment. It implements Art 132(1)(g) uniformly across the UK: regulated private providers are exempt and unregulated private providers are not exempt.

(2) **Ground 2**

Ground 2 is that Item 9 does not cause differing treatment between supplies that are similar. This is because, for the purposes of fiscal neutrality, there is a clear distinction between welfare supplies that are regulated, and those that are not.

(3) **Ground 3**

Ground 3 is that there has been no impermissible exercise of the UK's discretion under Art 132(1)(g). EU law is not insensitive to Member States' internal constitutional structures and the UK was entitled to acknowledge its own devolved system in its implementation of Art 132(1)(g).

History of the legislation

31. We were taken by Mr McNicholas in some detail through the history of the legislation. This was an exercise of some interest that shed light on how the current wording of the legislation evolved, although in the end we do not think it is of much direct assistance to anything we need to decide.

32. We can summarise it as follows:

(1) Neither the Finance Act 1972 (**"FA 1972"**), which first introduced VAT into UK law, nor the Value Added Tax Act 1983 (**"VATA 1983"**), which replaced it, contained any exemption for welfare services.

(2) The FA 1972 did however contain an exemption for health services which included (at Item 4 of Group 7 of schedule 5) the provision of care and the like in:

> "any hospital or other institution approved, licensed, registered or exempted from registration by any Minister or other authority."

(3) In 1980 that was amended by adding at the end:

> "pursuant to a provision of a public general Act of Parliament or of the Northern Ireland Parliament or of a public general Measure of the Northern Ireland Assembly, not being a provision which is capable of being brought into effect at different times in relation to different local authority areas."

An Explanatory Note to the Order introducing this amendment explained that it qualified the exemption by excluding institutions approved etc under local legislation or general legislation applied locally.

(4) Save for adding a reference after the Northern Ireland Assembly to an Order in Council under Schedule 1 to the Northern Ireland Act 1974, VATA 1983 was in the same form.

(5) An exemption for welfare services was first introduced by the Value Added Tax (Welfare) Order 1985 SI 1985/1900 with effect from 1 January 1986. The then relevant directive was the Sixth Directive which (by Art 13A(1)(g)) referred to the supply of services by:

> "bodies governed by public law or by other organizations recognized as charitable by the Member State concerned."

The exemption introduced into VATA 1983 (as Item 9 of Group 7 of Schedule 6 to VATA 1983) was as follows:

> "The supply, otherwise than for profit, by a charity or public body of welfare services and of goods supplied in connection therewith."

That was no doubt a reasonable attempt to give effect to Art 13A(1)(g) of the Sixth Directive, although it later became clear that the EU meaning of charitable was not confined to not-for-profit bodies.

(6) VATA 1983 was replaced by VATA 1994, but the relevant exemption (now found in Item 9 of Group 7 of Schedule 9) was in the same form and so confined to public bodies and charities. The exemption for care provided in hospitals or other institutions approved, licensed, registered or exempted from registration (now found in Item 4 of Group 7 of Schedule 9) was also in the same form as it had been in VATA 1983.

(7) A new version of Item 9 was substituted by the Value Added Tax (Health and Welfare) Order 2002 SI 2002/762 with effect from 21 March 2002. The new Item 9 was as follows:

> "The supply by –
>
> (a) a charity,
>
> (b) a state-regulated private welfare institution, or
>
> (c) a public body,
>
> of welfare services and of goods supplied in connection with those welfare services."

At the same time Note (6) (definition of welfare services) was amended by adding at the end:

> "and, in the case of services supplied by a state-regulated private welfare institution, includes only those services in respect of which the institution is so regulated."

And a new Note (8) was introduced to provide a definition of "state-regulated". This was in the same form as it now stands (paragraph 18 above). It can be seen that it used language taken from the existing exemption for hospital care in Item 4 and the definition in Note (8) was used not only for the new Item 9 but for Item 4 (which was amended so as to refer to "hospital or state-regulated institution"). At the same time the opportunity was taken to overhaul the list of relevant legislative bodies by (i) adding reference to two bodies which had been established since VATA 1994, namely the Scottish Parliament and the Northern Ireland Assembly, both established in 1998, and (ii) by identifying with more precision the various previous bodies responsible for legislation in Northern Ireland.

(8) Finally, the Value Added Tax (Health and Welfare) Order 2003 SI 2002/24 amended Item 9 with effect from 31 January 2003. This was a minor amendment, of no relevance to the present appeals, which added the words "or agency" after "state-regulated private welfare institution" in paragraph (b) of Item 9.

33. Mr McNicholas drew our attention to the fact that Art 1 of the Sixth Directive required Member States to adopt the necessary laws to give effect to it by 1 January 1978 at the latest, but that it was not until 1986 that the UK introduced any exemption for welfare services, and not until 2002 that the exemption was extended beyond public bodies and charities, as he submitted over 24 years late. That may be so but it does not seem to us to affect the questions on the appeal which turn on the validity of the legislation once introduced regardless of whether it was late or not.

34. Mr McNicholas also made the point that the elaborate reference in Note (8), introduced in 2002, to the types of legislation which can qualify an institution as state-registered can be seen to be an evolution of a definition that had been introduced (for the purposes of the hospital care exemption) many years before – indeed dating back to 1980. We accept that that is so, and that it therefore cannot be said that Note (8) was introduced as a specific reaction to the devolution settlements for Scotland and Northern Ireland in 1998. The origins of the list of relevant legislative bodies can be shown to be the desire in 1980 to confine institutions qualifying for the hospital care exemption to those approved, licensed etc under some general public legislation rather than legislation applicable only locally. But even when first introduced it was recognised to be appropriate to refer not only to public general acts of the Westminster Parliament, but to the equivalent legislatures in Northern Ireland. There is nothing surprising in this given that the Westminster Parliament does not, and did not, in general legislate for Northern Ireland. For many years (from 1921 to 1972 we believe), Northern Ireland had its own Parliament at Stormont, followed by attempts, not always successful in practice, to establish a Northern Ireland Assembly with legislative powers, supplemented in practice by direct rule from London by Order in Council rather than by Westminster legislation. It was therefore necessary to refer to these sources of general law for the province as otherwise institutions approved in Northern Ireland would not qualify for the exemption despite being approved under general public legislation applying province-wide. It is scarcely surprising in those circumstances that the definition should have been extended to the Scottish Parliament and the 1998 iteration of the Northern Ireland Assembly once they had been established, the purpose being to identify the sources of public general law rather than legislation applicable only locally. What can be said is that in 2002 it was recognised that the devolved legislatures for Scotland and Northern Ireland were among the sources of such general law. Given the devolution of health and social care to each of those legislatures that seems obviously appropriate.

35. Otherwise we do not derive much assistance from the history, apart from the point that in March 2002 when Item 9 was first extended to state-regulated private welfare institutions, there was in fact no difference as to the regulation of day services in any of the constituent parts of the UK. We were told by Mr Davey (without dissent from the other counsel) that it was not until April 2002 that day care services were first regulated in Scotland, and not until 2005 in Northern Ireland.

EU cases on the welfare exemption

36. We were referred to three cases in which the welfare exemption in Art 13A(1)(g) of the Sixth Directive was considered by the European Court of Justice (**"the ECJ"**).

37. The first was *Ambulanter Pflegedienst Kügler GmbH v Finanzamt für Körperschaften I in Berlin* (Case C-141/00) [2002] ECR 16833 (***"Kügler"***).

Kugler was a German company that carried on an outpatient care service. It claimed that it should have been exempted pursuant to Art 13A(1)(g) of the Sixth Directive. The ECJ said that Art 13A(1)(g) of the Sixth Directive "grants the Member States a discretion for the purpose of according certain organisations such recognition" [54]; that so long as the Member States observe the limits of the discretion accorded to them by Art 13A(1)(g), persons cannot rely directly on that provision to acquire the status of charitable organisations [55]; that it is for national courts to examine whether the competent authorities have observed those limits while applying Community principles, "in particular the principle of equal treatment" [56]; and that it will accordingly be for national authorities, in accordance with Community law and subject to review by the national courts, to determine which organisations should be considered as charitable [57].

38. The next was *Kingscrest Associates Ltd v Customs and Excise Commissioners* (Case C-498/03) [2005] STC 1547 (***"Kingscrest"***). Kingscrest was an English partnership that carried on the business of residential care homes for profit. It was registered under the relevant UK legislation, most recently the Care Standards Act 2000. Being neither a public body nor a charity, its supplies were not exempt until Item 9 was amended in 2002 to include services supplied by a state-registered private welfare institution. The ECJ first dealt with questions as to the meaning of "charitable" in Art 13A(1)(g) of the Sixth Directive, holding that it was not limited to the English idea of charity but had to be given a uniform European meaning [26]-[27]; and that this was not limited to not-for-profit organisations [40]-[43]. It then considered whether Member States had a discretion to recognise as "charitable" a private profit-making entity which did not have charitable status under domestic law and held that it did, adding (at [53]):

> "In that regard, it follows from the case law that it is for the national authorities, in accordance with Community law and subject to review by the national courts, to take into account, in particular, the existence of specific provisions, be they national or regional, legislative or administrative, or tax or social security provisions, the general interest of the activities of the taxable person concerned, the fact that other taxable persons carrying on the same activities already have similar recognition, and the fact that the costs of the supplies in question may be largely met by health insurance schemes or other social security bodies."

39. The ECJ regarded the imposition of regulation as being a significant factor. It said at [57]:

> "For the purposes of determining whether the limits of the discretion have been exceeded in this case, the national court may, on the other hand, take into account in particular the fact that, under the amended VAT Act, entitlement to the exemptions provided for in Article 13A(1)(g) and (h) of the Sixth Directive extends to all organisations registered under the Care Standards Act 2000, as well as the fact that that Act and the amended VAT Act contain specific provisions which not only reserve entitlement to those

> exemptions to organisations supplying welfare services, the content of which is defined by those Acts, but also govern the conditions for providing those supplies, by making the organisations which provide them subject to restrictions and checks by the national authorities, in terms of registration, inspection and rules concerning both buildings and equipment and the qualifications of the persons authorised to manage them."

40. The third case was *Finanzamt Steglitz v Zimmermann* (Case C-174/11) [2016] STC 2104 (***"Zimmermann"***). Ms Zimmermann was a nurse who ran an outpatient care service. Under German law her supplies would only be exempt if the costs of care had been borne in at least two-thirds of cases in the previous calendar year wholly or mainly by the statutory social security or social welfare authorities, which they had not; whereas there were other bodies covered by private law (such as officially recognized voluntary welfare associations) which did not have to meet the same requirement. The ECJ reiterated that since Art 13A(1(g) does not specify the conditions for recognising organisations as charitable, it is for the national law to lay down the rules and that Member States have a discretion in that respect ([26]), taking into account the matters listed in *Kingscrest* at [53] ([31]); and that where a taxable person challenges the recognition, or lack of recognition, of an organisation for that purpose, it is for the national courts to examine whether the competent authorities have observed the limits of that discretion whilst applying the principles of EU law, including in particular the principle of fiscal neutrality [33]. On the facts, the ECJ held that there was nothing wrong in principle with the two-thirds requirement ([37]), but the neutrality principle precluded such a threshold being applied, in relation to goods or services that were essentially the same, in relation to some taxable persons governed by private law and not to others [59].

HMRC's Ground 1

41. We can now consider HMRC's Ground 1. This is in effect that the differential VAT treatment of day care providers as between England and Wales on the one hand and Scotland and Northern Ireland on the other is not caused by the VAT legislation but by something else, that is the choice of the devolved legislatures in Scotland and Northern Ireland to regulate such services.

42. The starting point is that the European cases repeatedly make it clear that what was Art 13A(1)(g) of the Sixth Directive (and is now Art 132(1)(g) of the Principal Directive) conferred a discretion on Member States. The article provides an exemption not for the supply of all welfare services but for the supply of welfare services either by public bodies or by other bodies "recognised" by the Member State concerned as being "charitable" (Art 13A(1)(g)) or "devoted to social wellbeing" (Art 132(1)(g)). That envisages that the Member State concerned will lay down rules as to what is required before a non-public body can be recognised.

43. That is what the UK did in 2002 in the shape of Item 9. It chose as one criterion for recognition the fact of being state-registered as defined. In doing

so it seems to us that it was properly exercising the discretion conferred on it by Art 13A(1)(g). The contrary was not we think suggested. Indeed so far as the LIFE case is concerned, the UT on the first hearing of the appeal has already expressly said that this was a rational choice open to the UK: it was sufficiently certain and *Kingscrest* demonstrates the acceptability and rationality of regulation as a criterion (see the citation from [57] of the judgment in paragraph 39 above, which is referred to in the citation from the UT's decision at paragraph 27 above). So far as the TLC case is concerned, Mr McNicholas expressly accepted that the adoption of regulation as a criterion in 2002 was a proper exercise of the discretion conferred on the UK as a Member State under what was then Art 13A(1)(g).

44. As Mr Davey pointed out however, that criterion did not apply differently to different private bodies. Leaving on one side public bodies and charities, it applied the same criterion, that of registration, to *all* other suppliers of services. It is not therefore like *Zimmermann* where the requirement for state funding in two-thirds of the cases in the previous year applied to some suppliers such as Ms Zimmermann, but not to others. When the criterion for recognition was introduced in 2002, it applied uniformly throughout the UK without distinction between different types of supplier: all regulated private providers of welfare services were exempt, and all unregulated private providers (with the exception of charities) were not exempt.

45. Mr Davey's point under Ground 1 is that nothing changed in this respect when the Scottish Parliament first decided to regulate private providers of day care services later in 2002. The VAT rules have not changed (nor indeed did the Scottish Parliament have any competence to change them). It remains the case, throughout the UK, that all regulated private providers of welfare services are exempt, and all unregulated ones (save charities) are not. The fact that in practical terms Scottish providers of day care services, being regulated, can now satisfy the criterion whereas English ones, not being regulated, cannot is not caused by the VAT rules but by something else, namely the decision of the Scottish Parliament to regulate day care services.

46. Mr Bremner QC, who appeared for LIFE, submitted that there were two reasons why Ground 1 could not be right. The first was that what European law was concerned with was the result: the principle of fiscal neutrality required similar supplies to be taxed similarly and the underlying reason why there was dissimilar treatment did not excuse a breach of neutrality. The second was that if it were necessary to show that Item 9 resulted in dissimilar treatment, that could be done as it was Item 9, albeit in combination with the Scottish and Northern Irish regulatory regime, which caused the dissimilar treatment.

47. Neither submission seems to us to answer Mr Davey's point which is that the VAT legislation does not distinguish between different private suppliers of welfare services. Leaving charities to one side, it applies the same criterion for recognition (that of being state registered as defined) to all. That criterion is

rational and lawful. It is not therefore the VAT legislation which causes any difference in treatment. It cannot therefore be said that the UK has failed properly to implement Art 13A(1)(g) (now Art 132(1)(g)).

48. We accept Mr Davey's submission which seems to us to be well founded. It is accepted that the UK had a discretion. It is accepted, or has already been found, that the way in which it exercised that discretion in 2002 was rational and lawful. We see no basis on which it could be said that as introduced in 2002 it breached the principle of fiscal neutrality as it applied uniformly across the UK to all private suppliers of welfare services. To the extent that there is now a difference between such suppliers in England and Wales on the one hand, and Scotland and Northern Ireland on the other hand, this is not caused by any lack of neutrality in the VAT legislation, but by the fact that the UK has devolved regulation of this sector to the devolved nations and they have made different decisions in that respect, as they are entitled to do.

49. Any other view would mean that the Scottish Parliament, by doing what *was* within its competence, namely deciding to regulate day care services, would be forcing on the UK Parliament an obligation either to enact a parallel system of registration in England, or to change the VAT rules for the UK as a whole, despite the fact that neither the regulation of day care services in England nor the VAT rules are matters for the Scottish Parliament. We do not accept that that can be right. It is inevitable in a devolved system that in certain matters the devolved nations will diverge; in our judgment that does not mean that VAT rules that apply uniformly across the entire UK are themselves invalid for breach of the principles of fiscal neutrality.

50. On this simple ground, which cannot be elaborated at any great length, we propose to allow HMRC's appeal in each case.

HMRC's Ground 2

51. We go on to consider Ground 2 in case we are wrong on Ground 1.

52. Ground 2 is effectively that there is a relevant difference between services supplied by a regulated entity and those supplied by an unregulated entity so that there is no breach of the principle of fiscal neutrality if supplies by the one are exempt and by the other are not, even if the content of the supplies is otherwise similar.

53. Mr Davey says that the UT has in fact already decided this point in the LIFE case in the first hearing of the appeal. That, he says, is determinative for the LIFE case, and should also be followed by us in the TLC case unless satisfied that the decision is wrong.

54. We accept this submission. At [55] of its decision on the first hearing of the appeal in the LIFE case, the UT said that:

> "There is no way in which LIFE can equate itself with entities which are subject to the sort of regulation regime which is applied to regulated bodies. Those bodies are obliged to conform to certain standards. For LIFE that is optional, even if it chooses for the time being to do so."

5 That seems to us to be a plain decision that there is a difference between regulated and unregulated entities. We do not think it can be read any other way. Mr Bremner said that it would be very odd if the UT, having decided to adjourn consideration of the devolved nations issue, had somehow already decided the point while addressing a different question, that of fiscal neutrality 10 as compared with charities. That may be so but it does sometimes happen, as Mr Davey said, that a court or tribunal decides something in dealing with one part of a case which is in fact determinative of another part of the case albeit the latter has been adjourned to a later hearing.

55. For this reason we do not think it is in fact open to LIFE to contend that its 15 supplies are similar to supplies made by regulated bodies. But we will go on to consider the point on its merits, both in case we are wrong and because the decision is not technically determinative of the TLC appeal.

56. Mr Davey accepted that the principle of fiscal neutrality can be taken from the decision of the ECJ in *Rank Group plc v Revenue and Customs* 20 *Commissioners* (Cases C-259/10 and C-260/10) [2012] STC 23 (***"Rank"***). At [32] the ECJ described the principle as follows:

> "the principle of fiscal neutrality precludes treating similar goods and supplies of services, which are thus in competition with each other, differently for VAT purposes"

25 and at [36] said this:

> "the principle of fiscal neutrality must be interpreted as meaning that a difference in treatment for the purposes of VAT of two supplies of services which are identical or similar from the point of view of the consumer and meet the same needs of the consumer is sufficient to establish an 30 infringement of that principle."

Mr Davey also accepted that since in general what the consumer is interested in is whether two supplies of services have the same characteristics and meet the same needs, such matters as the identity of the suppliers, the legal form by means of which they exercise their activities, and the fact they fall into 35 different licensing categories and are subject to different legal regimes relating to control and regulation are not in general relevant: see *Rank* at [42]-[51].

57. But he said that was not a universal rule, as recognised in *Rank* itself at [50]:

> "…in certain exceptional cases, the court has accepted that, having regard to the specific characteristics of the sectors in question, differences in the 40 regulatory framework or the legal regime governing the supplies of goods or services at issue, such as whether or not a drug is reimbursable or

whether or not the supplier of a service is subject to an obligation to provide a universal service, may create a distinction in the eyes of the consumer, in terms of the satisfaction of his own needs."

58. Mr Davey relied on four examples of such cases as follows:

5 (1) *R (oao TNT Post UK Ltd) v HMRC* (Case C-357/07) [2009] STC 1438

This concerned the exemption in Art 13A(1)(a) of the Sixth Directive for services supplied by the public postal services. TNT claimed a breach of fiscal neutrality in that Royal Mail's services were exempt whereas theirs were not. The Advocate-General said that the services 10 provided by TNT were not comparable with those provided by Royal Mail (even if certain services were identical) because of the nature of the universal service guaranteed by Royal Mail [62]-[63]. The ECJ agreed, saying that the assessment of the comparability of the services supplied hinges not only on the comparison of individual services but 15 on the context in which those services are supplied [37], and that an operator such as Royal Mail supplies postal services under a legal regime which is substantially different to that under which an operator such as TNT provides such services [38].

(2) *EC Commission v French Republic* (Case C-481/98) [2001] STC 919

20 This concerned the VAT rate on medicines in France. VAT was charged at a lower rate on medicines that were reimbursable under the French social security system than on those that were not. The ECJ held that there was no breach of fiscal neutrality as the two classes of products were not similar [25]; the inclusion of a product on the list of 25 reimbursable products was pursuant to objective criteria [26]; and in any event a reimbursable product had a decisive advantage for the final consumer. It was not therefore the lower rate of VAT which provided the reason for his decision to purchase [27].

(3) *Staatsecretaris van Financiën v Fiscale Eenheid X NV cs* (Case C- 30 595/13) [2016] STC 2230 (***"Eenheid"***)

This concerned an exemption in Art 13B(d)(6) of the Sixth Directive for the management of special investment funds. Undertakings for collective investment in transferable securities were regulated at EU level by virtue of a directive called the UCITS Directive; the question 35 was whether a collective investment in real property, which was not regulated by the UCITS Directive, could be regarded as a special investment fund. The Advocate-General said that it could, provided that it displayed features that were sufficiently comparable to be in competition with such undertakings; and that such competition could 40 essentially exist only between investment funds that were subject to specific state supervision, as only those kinds of investment funds

could be subject to the same standards of competition and appeal to the same circle of investors [27]. The ECJ agreed [48]-[49].

(4) *Solleveld and van den Hout-van Eijnsbergen v Staatsecretaris van Financiën* (Cases C-443/04 and C-444/04) [2007] STC 7 (***"Solleveld"***)

This concerned the exemption in Art 13A(1)(c) of the Sixth Directive for the provision of medical care in the exercise of the medical and paramedical professions as defined by the Member State concerned. Ms van den Hout-van Eijnsbergen was a psychotherapist who provided treatment but did not belong to one of the paramedical professions defined by the Dutch legislation exempting medical care from VAT; Mr Solleveld was a physiotherapist (which was one of the relevant professions) but provided treatments which did not come within the areas of expertise of a physiotherapist as defined by the relevant Dutch law. The ECJ said that Member States had a discretion to define not only the relevant paramedical professions and the qualifications required to carry them out, but also the specific medical-care activities covered by such professions [29]-[30]; that in order to determine whether medical care was similar for the purposes of fiscal neutrality, it was appropriate to take into account the professional qualifications of the care providers [40]; and [41]:

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

59. We accept the submission that this quartet of cases illustrates that although in general the consumer is not interested in the regulatory regime which governs a supplier of services, there can be particular contexts where the regulatory framework or legal regime governing the supplies in question may create a distinction in the eyes of the consumer. We have found the most helpful of the cases to be *Eenheid* and *Solleveld*. In *Eenheid*, the Advocate-General (with whom the ECJ agreed) evidently considered it self-evident that a collective investment in real property could not be regarded as comparable to a collective investment in transferable securities unless it was subject to state supervision. This could we think only have been because from the point of view of the consumer the protections and guarantees inherent in a system of state regulation make a regulated supplier of investment services dissimilar from an unregulated one. In *Solleveld* the question formulated by the ECJ at [41] was not whether the medical care provided was itself similar to that provided by an exempt profession but whether the system of regulation of the profession

concerned was such as to *ensure* an equivalent level of quality of care.

60. We accept that in the case of welfare services, which are necessarily personal, services provided by regulated providers are of their nature different from services provided by unregulated providers, because the system of regulation provides a system of protections and guarantees which is absent in the case of unregulated services. We therefore consider that the UT in the first appeal in the LIFE case was right to say that providers such as LIFE (and TLC) cannot be equated with regulated providers. This is so even though (i) they may in fact be providing similar services to those that would be provided in Scotland and Northern Ireland by regulated bodies; and (ii) they in fact provide services to the same standard of care as would be required if they were regulated. They are not subject to the same level of state supervision. Nor is it an answer to say that the local authorities (Havering and Gloucestershire) with whom they respectively deal inspect and monitor the quality of service. This is no more than one would expect a responsible local authority to do, but this cannot be regarded as the equivalent of a statutory system of regulation.

61. For these reasons, which are essentially those advanced by Mr Davey, we accept HMRC's Ground 2.

HMRC's Ground 3

62. Ground 3 is in effect that if Item 9 does treat similar services differently, there is nevertheless no breach of the principle of fiscal neutrality because it is for each Member State to decide how to give effect to EU law having regard to its own constitutional arrangements, and if, as is permissible, a Member State has a devolved structure there is nothing wrong in such a Member State giving effect to EU law differently in its different constituent parts.

63. On the view we have taken of Grounds 1 and 2, it is not necessary for us to decide the point. It is an interesting argument but would appear to be a novel one with potentially far-reaching consequences, and we are far from confident that we have been addressed on all the possible ramifications. In those circumstances we prefer to say nothing about it.

Conclusion

64. For the reasons given above we have decided that there was no breach of the principle of fiscal neutrality. It follows that:

(1) in the LIFE appeal, HMRC's appeal is allowed.

(2) in the TLC appeal, HMRC's appeal is allowed.

MR JUSTICE NUGEE **JUDGE TIMOTHY HERRINGTON**

RELEASE DATE: 23 January 2019