EXEMPT SUPPLY – Sporting services – Eligible body – Proprietary fitness club – Supplies of sporting services to members – Percentage of turnover paid to Appellant as licence fee – Licence fee assessed to tax on supplies to members – Whether supplies made by Appellant and not by proprietary club – No – Sixth EC Directive Art 13A.1(m)
ABUSIVE PRACTICE – Halifax principle – Adoption of scheme to make supplier of sporting services an eligible body – Whether abusive practice – No, because scheme failed to avoid tax anyway – Whether in any event transactions could be redefined to support assessment – No – Appeal allowed

LONDON TRIBUNAL CENTRE

THE ATRIUM CLUB LTD **Appellant**

- and –

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS Respondents

Tribunal: SIR STEPHEN OLIVER QC (Chairman)

Sitting in public in London on 1,2, 3 and 7 and 8 December 2008

Roger Thomas, counsel, instructed by Eversheds, solicitors, for the Appellant

Owain Thomas, counsel, instructed by the general counsel and solicitor for HMRC, for the Respondents

DECISION

1. The Atrium Club Ltd ("Atrium") appeals against a decision (in a Decision Letter of 29 April 2004). The decision is that Atrium made supplies of taxable sporting services.

2. The decision is expressed in two ways. The first is that Atrium has at all material times, and notwithstanding the purported interposition (since March 2000) of another company called AAB Sports Ltd ("AAB"), been making the supplies to individuals who were members of the Atrium Health and Fitness Club ("the Club"). The second way the decision is expressed is this: the creation and interposition of AAB, and of Atrium Health Ltd ("Atrium Health") before AAB, was an abusive practice in the sense that that expression is explained by the Court of Justice in *Halifax v Customs and Excise Commissioners* (Case C-255/02) [2006] STC 919. The *Halifax* argument, as formulated in paragraph 13 of the Amended Statement of Case of the Respondents ("HMRC") is expressed as follows:

> "... the attempt to avoid VAT on the supply of sporting services by the creation of AAB and its insertion in the supply chain is an abuse of law such that the advantage sought to be obtained (exemption from VAT) should be denied. The Commissioners contend that the particular provision of the Sixth Directive which has been abused is the sporting exemption."

HMRC "redefine" the "transactions involved in [the] abusive practice" (to use the Court's expressions in paragraph 94 of the *Halifax* decision) as a situation in which for VAT purposes Atrium supplies the taxable sporting services to the members of the Club; in consequence Atrium is liable for the VAT on the income received for such services with the right to recover input tax attributable to the sporting services.

Brief summary of the circumstances to which the Decision relates

3. Until 1996 Atrium, a company owned by Mr and Mrs Bradney, ran the Club as a health and fitness club. Atrium owned the premises and operated the business for profit and accounted for VAT on the supplies it made of sporting services. In December 1996 Atrium entered into agreements with Atrium Health, a company under common control; by those agreements Atrium granted Atrium Health, for a fee, the right to use the premises and other facilities for the purposes of providing sporting services. Atrium Health had been designed and created to qualify as a non-profit making organisation providing exempt sporting services in the public interest. Atrium Health never registered for VAT. Following a change relating to, among other things, sporting services in the legislation taking effect on 1 January 2000, AAB (a company limited by guarantee) was created and entered into various agreements. The design was for AAB to rank as a non-profit making body and for its supplies to qualify for exemption under the changed provisions.

4. Neither Atrium Health nor AAB accounted for or paid VAT in respect of the period from January 1976 until April 2006. AAB was liquidated in May 2006 and its place was taken by a new company (FAB Ltd). FAB Ltd registered for and accounted for VAT on the supplies of sporting services.

The evidence

5. Oral evidence was given by Ms Jo Forman (who had joined Atrium Health as administrative manager in 1999 and became director of and guarantor of AAB in 2000), by a Mr S Bradley (who became a director of AAB in 2003) and by Mr R K E Bradney (director of Atrium who, with Mrs Bradney, owned all the shares in Atrium).

The legislation

6. Part A of Article 13 of the Sixth Directive exempts from VAT certain activities in the public interest including (by Article 13A.1(m)):

> "... certain services closely linked to sport or physical education supplied by non-profit making organisations to persons taking part in sport or physical education."

Article 13A.2(a) provides as follows (so far as material):

> "Member States may make the granting to bodies other than those governed by public law of each exemption provided for in 1...(m) ... of this Article subject in each individual case to one or more of the following conditions:
>
> – they shall not systematically aim to make a profit, but any profits and nevertheless arising shall not be distributed, but shall be assigned to the continuance or improvement of the services supplied,
> – they shall be managed and administered on an essentially voluntary basis by persons who have no direct or indirect interest, either themselves or through intermediaries, in the results of the activities concerned, ..."

7. Finance Act 1994 section 31 and Schedule 9 sought to implement Article 13. Section 31 of the 1994 Act provides that a supply of goods or services is an "exempt supply" if it falls within Schedule 9.

8. Group 10 in Schedule 9 is headed "Sports, Sports Competitions and Physical Education". Prior to 1 January 2000 Item 3 in Group 10 was in the following terms:

> "The supply by a non-profit making body to an individual, except, where the body operates a membership scheme, an individual who is not a member, of

services closely linked with and essential to sport or physical education in which the individual is taking part."

9. Group 10 was substantially amended with effect from 1 January 2000 by VAT (Sports, Sports Competitions and Physical Education) Order 1999 (SI 1999/1994). As so amended, Item 1 in Group 10 reads as follows:

> "The supply by an eligible body to an individual, except, where the body operates a membership scheme, an individual who is not a member, of services closely linked with an essential to sport or physical education in which the individual is taking part."

A number of Notes then follow. Note (2A) defines "eligible body" as meaning (so far as material):

> "... a non-profit making body which –
>
> (a) is precluded from distributing any profits it makes, or is allowed to distribute any such profits by means only of distributions to a non-profit making body;
> (b) applies in accordance with Note (2B) any profits it makes from supplies of a description within Item ... 3; and
> (c) is not subject to commercial influence.

Note (2B) provides as follows (so far as material):

> "For the purposes of Note (2A)(b) the application of profits made by any body from supplies of a description within Item ... 3 is in accordance with this Note only if those profits are applied for one or more of the following purposes, namely –
>
> (a) the continuance or improvement of any facilities made available to or in connection with the making of the supplies of those descriptions made by that body; ..."

The issues

10. The first issue is whether, as HMRC contend, Atrium has made the supplies of sporting services despite entering into agreements designed to make Atrium Health and subsequently AAB the supplier of those services.

11. The second issue is whether, as HMRC contend, the creation of AAB (and before it Atrium Health) and Atrium's divesting itself of the liability to account for output tax in those circumstances was an abusive practice. If the transactions were an abusive practice, should they be redefined in the manner of the decision of HMRC upon which the assessment under appeal is based. The decision is expressed in paragraph 13 of HMRC's Amended Statement of Case as follows:

"[HMRC] contend that the way in which the supplies should be re-characterised is that the abusive arrangements should be disregarded and the activities of carrying on the business of health club which are said to have been undertaken by AAB should be treated as having been undertaken by [Atrium] for VAT purposes. As such the transactions which AAB is said to have entered into in respect of the disputed supplies should be treated as having been entered into by [Atrium] and not AAB for VAT purposes. [HMRC] have accordingly raised assessments on [Atrium] which are intended to reflect this to the best of their judgment. The effect of the re-characterisation of the supplies is that [Atrium] is treated as having made the disputed supply and is hence liable for the underdeclared tax in accordance with the assessments. They have been formulated on the basis of the sales declarations of AAB. In addition credit has been given for output VAT wrongly accounted for by [Atrium] on supplies to AAB under the arrangements. As aforesaid, [Atrium] is also entitled to deduct input tax which is attributable to the disputed supplies."

The position until December 1996

12. Atrium started business in September 1991. It has at all material times been owned by Mr and Mrs Bradney, both of whom have been directors. Until December 1996 Atrium's business was running a gym and sporting facilities located on its premises at 39 Newnham Street, Ely. Its trading income consisted in the main of fees paid by members for membership of the Club (known as the Atrium Health Club), a proprietary club.

13. An individual's membership of the Club lasted for twelve months. The member paid either a single "paid in full" membership fee or entered into a direct debit arrangement to pay by monthly instalments. Members were able to introduce guests for a separate fee. Members had the right to renew their membership at the rate in force at the time of expiration of their existing period of membership. The contract between the Club and the member could be varied at any time by the proprietor of the Club which, at least until December 2006, was Atrium.

14. Mr and Mrs Bradney ran the entire undertaking. They were responsible for the administration, for the management of budgets, of payroll and human resources matters, for membership retention, for ensuring that all licences were in place and for marketing and promotion. They were supported by a staff of twelve who performed individual tasks ranging from providing fitness tests and workouts to cleaning and security.

15. Atrium accounted for VAT on the supplies of sporting services through the Club. The membership fees and guest fees were the consideration for Atrium's taxable supplies of sporting services.

The position from December 1996 until February 2000

16. Late in 1996 advice was obtained from VAT consultants known as AIC leading to the setting up of a structure designed to transform the supplies relating to the Club activities from standard-rated into exempt. Mr Bradney explained that the advice had been implemented in order to make them competitive with local authorities whose supplies of sports and fitness services were exempt.

17. AIC, in a letter of 18 December 1996, provided a "User Agreement" to be entered into between Atrium and, to use AIC's words, "the non-profit making organisation Atrium Health Club Ltd". AIC provided a notice to be given to all existing members of the Club, to be put on a Club notice board and sent to members. The letter of 18 December states that "the user fee charged" to be paid to Atrium by the operating company, Atrium Health (the so-called non-profit making organisation), has been set "at £245,000 which is just under the expected turnover of the non-profit making company. The surplus in Atrium Health can be used to pay those charges that specifically relate to" Atrium Health. The letter stresses that Atrium Health's supplies to members must be accounted for separately from any supplies that Atrium continues to make and that the insurers must be notified of the change.

18. The User Agreement is dated 1 December 2006. It recites that Atrium Health is a wholly owned subsidiary of Atrium. Mr Bradney said in evidence that it was in fact owned by Mr and Mrs Bradney. I accept that. By Clause 1 Atrium grants to Atrium Health "the right to use the Facilities for a period of five years" to enable Atrium Health to provide these to its own customers "all in accordance with normal good health club practice". Clause 2 entitles Atrium to a "user fee" of £245,000 (plus £310 per member in excess of 826 individuals) exclusive of VAT each year.

19. The User Agreement is to last until 1 December 2001 unless determined for cause before then. It is expressed in Clause 4.1 to be "a personal contract and licence of the whole or any part of the Facilities but not an interest in the land or freehold and therefore grants rights to use only the Facilities."

20. "The Facilities" are described in Recital B as follows:

> "All areas of the land (39 Newnham Street) used solely for the purposes of sport and physical education and all equipments, fixtures and fittings utilised in such activities ("the Facilities") are presently operated by Atrium for the benefit of ... the Club".

21. Atrium remains obligated under the User Agreement to make capital improvements and changes to the Facilities at its expense.

22. Atrium Health was duly incorporated with memoranda and articles that prevented it from distributing its profits.

23. The AIC letter of 18 December 1996 informs Mr Bradney that after 1 December 1996 "you are able to legitimately treat money received after the User Agreement as exempt of VAT".

24. AIC wrote to HMRC asking for confirmation of the exempt status of Atrium Health's supplies to Club members and received the qualified reply that exempt status would be available provided the conditions of Item 3 of Group 10 of Schedule 9 to the VAT Act were fulfilled. There is no record of any follow-up from HMRC. HMRC do not now accept that the conditions of Item 3 were ever fulfilled. Atrium Health proceeded on the basis that its supplies to members were exempt. My understanding is that Atrium treated the supplies of facilities as an exempt grant of a licence to occupy land (within Item 1 of Group 1 of Schedule 9).

25. Atrium placed a typed notice on the Club notice board. This stated that from 1 December 1996 responsibility for the management of the facilities of the Club "would be taken over by" Atrium Health which "will have full responsibility for the upkeep of all aspects of the facilities ...". Atrium Health, the notice said, would collect all fees from members.

26. Throughout 1997, 1998 and 1999 and until March 2000 (i.e. throughout the Atrium Health regime) Atrium Health kept its own books and statutory accounts. There was no suggestion that they did not record as "sales" of Atrium Health all membership fees and other payments for use of facilities of the Club; on the same basis I infer that expenditure covered costs of running the Club including the Club staff salaries and the user fee charges paid to Atrium

Relevance of Atrium Health to the decisions under appeal

27. The decisions under appeal do not impact on the arrangements from 1 December 1996 until 1 March 2000. Atrium has not been assessed to VAT on the fees paid by members during that period. The assessment under appeal relates to the fees received by AAB. HMRC's case, based on *Halifax* principles, is that the creation and use of AAB and before it the creation and use of Atrium Health amounted to an "abusive practice" in the sense that that expression has been explained by the Court in *Halifax*. The inclusion of Atrium Health in the abusive practice requires me to reach certain conclusions.

28. First, assuming that the User Agreement can properly be characterised as the letting of immoveable property (with the result that Atrium's supplies to Atrium Health were exempt as being the "leasing and letting of immoveable property"), the implementation of the User Agreement resulted in the accrual of a tax advantage the grant of which would be contrary to the purposes of the relevant provisions of the

Sixth Directive. See the words in paragraph 86 of the *Halifax* decision. The "relevant provisions" of the Sixth Directive are Article 13A.1(m) which, as mentioned, affords exempt status to services closely linked to sport or physical education supplied by non-profit making organisations where the further conditions imposed by the Member State in pursuance of Article 13A.2(a) are satisfied. The creation of Atrium Health with a memorandum and articles of association that prevented any distribution of profits coupled with the execution of the User Agreement which stripped out £245,000 from Atrium Health each year (i.e. just under its expected turnover, see AIC's letter of 18 December 1996) were the two essential parts of the design. The design was for Atrium Health to make the exempt supplies as a non-profit making organisation and for Atrium to obtain an exempt annual fee of just under the aggregate of the membership subscriptions received by Atrium Health. The result of implementing the design was to achieve the object of the scheme. The formation of Atrium Health and the membership fee strip effected by the User Agreement divided into two stages what had previously been a single supply of sporting services by Atrium to its members. Atrium keeps as its income the £245,000, being an amount just under the aggregate of the membership fees for the year; assuming the £245,000 really is income from the letting or leasing of immoveable property, the £245,000 is treated as an exempt supply to Atrium Health. Atrium Health makes the supplies of sporting services to the members; it is a non-profit making organisation because all profit has been stripped out in favour of Atrium and anything left over is subject to the restrictions in the memorandum and articles.

29. The result (assuming the AIC scheme was effective) was a "tax advantage" in the relevant sense. Moreover it is clear from the evidence that the obtaining of the tax advantage was the essential aim of the transactions involved in the implementation of that scheme. See paragraph 87 of the *Halifax* decision. The AIC letter of 18 December 1996 spells this out explicitly and Mr Bradney explained in evidence that he need to implement the scheme to eliminate the competitive disadvantage that Atrium suffered as compared with local authority health clubs whose similar supplies were exempt. For those reasons the conditions for application of the abusive practice principle were present throughout the Atrium Health regime.

30. Second, as already indicated, I am satisfied that the members were duly notified that from 1 December 1996 onwards the obligations to provide the membership facilities were being assumed by Atrium Health. This was the first requirement laid down in the AIC letter. It was a new departure for both Atrium and for Mr & Mrs Bradney. Mr Bradney said that the notice was duly displayed in the Club and sent to members. I accept that it was displayed. Consequently, in my view, there was sufficient notice to members to novate their contracts and to make them parties to contracts with Atrium Health for the supply of Club services. In this connection I note from Mr Bradney's evidence that from the end of 1996 Club membership forms were changed so as to remove a condition (regarded as "not best practice" in the fitness industry) allowing the Club's proprietor to accept or decline members. The membership forms were, from them and until at least 2000, headed either "The Atrium Health Club" or "The Atrium Health and Fitness Club".

31. Third, Mr Bradney stated in evidence that, in order to pass the goodwill in the Club to Atrium Health and to protect the trading name, "we" (which I take to refer to Mr & Mrs Bradney and to Atrium) decided to allow Atrium Health to associate itself with Atrium's trading name, i.e. The Atrium Club. From 1996 onwards Atrium Health had the right to use the trading names Atrium Club, Atrium Health Club and Atrium Health and Fitness Club for that purpose.

32. Fourth, Atrium Health employed its own staff (jointly with Atrium). There is no suggestion that Atrium Health failed to comply with its responsibilities, such as tax, NIC, employment liability insurance and health and safety obligations with regard to those employees. The staff, which by 1999 included Jo Forman and a Mr Stuart Flude (who remained as a senior manager and director of AAB until 2003) were there to manage the Club.

33. Fifth, Atrium Health had a bank account and received all "paid in full" membership fees from members who did not enter into direct debit arrangements. Direct debit members continued to use direct debit facilities operated by Atrium. This was because Atrium and not Atrium Health owned an "originator number" with the bank. The direct debit fees were collected for the benefit of the Club activity run by Atrium Health. Atrium Health, as a separate transaction, discharged its obligation under the User Agreement to pay the £245,000 user fee to Atrium.

34. With those points in mind I am satisfied that Atrium Health and not Atrium was providing the services of Club membership to the members and their guests. The consideration for such services was received for the benefit of Atrium Health. Atrium Health had its own staff, equipment and premises from which to make the supplies. Atrium Health had its own employment liability, public liability and business interruption insurance cover. Atrium Health had the right to use the name the Atrium Health Club to enable it to carry on business making the supplies to members and their guests. I cannot conclude from the evidence that Atrium Health traded as either agent, trustee or nominee for Atrium. The contractual provider of the supplies of sporting services to members was at all times Atrium Health. The real nature of the supplies is in line with the contractual position. I am satisfied therefore that Atrium Health and not Atrium made the sporting supplies during the period December 1996 until the end of February 2000.

35. Precisely how, for VAT purposes, the arrangement between Atrium and Atrium Health is to be determined was not in issue. There must be a case for regarding the user fees as consideration for Atrium's supply of a five year licence to Atrium Health to enable Atrium Health to make use of Atrium's business goodwill in the Club business making use of the Club facilities. So regarded, Atrium's supplies might not qualify (or might not wholly qualify) as the leasing or letting of immoveable property. This was never an issue and I take it no further.

36. Finally in this connection, for reasons given above I am satisfied that the transactions put in place in December 1996, i.e. the transfer of the Club business by Atrium to Atrium Health and Atrium Health's undertaking to pay the annual user fee of £245,000, can properly be regarded as an abusive practice. No decision as to the tax implications has been given by HMRC. I do not therefore need to address the question of how the abusive transactions are to be redefined.

The WJB Chiltern scheme

37. By 1999 Jo Forman was administrative manager and Stuart Flude was club manager. Mrs Bradney's health was deteriorating. Mr and Mrs Bradney were involved in the opening of another health club in Cambridge. While at an industry conference Mr Bradney discussed changes to the sporting exemption contained in SI 1999/1994. He learned that a tax consultancy called WJB (later to become WJB Chiltern) had devised a scheme of preserving the benefits of exemption for sporting supplies.

38. SI 1999/1994 Articles 2-5 introduced an elaborate set of provisions as Notes (2A)-(2C) and (4)-(17) to Group 10 of Schedule 9. The construction of these is not in issue in the present appeal. But I now summarise their effect as an introduction to the planning behind the WJB Chiltern Scheme.

39. First, the profits of the body making the "exempt" sporting supplies, always assuming (as was likely to be the case of the Atrium Club supplies) that profits would be made, must be stripped out.

40. Second, if the means of stripping them out involves (as was part of the Scheme) the use of a licence granted by the landowner for a fee related to turnover, the body making the supply of the sporting services must (to preserve its "eligible body" status) be in no way associated with the landowner.

41. Third, the licence must be an exempt supply, i.e. a supply falling within Item 1 of Group 1 to Schedule 9. It must therefore be the grant of a licence to occupy land. Otherwise the body making the exempt sporting supplies will have irrecoverable input tax attributable to the consideration given by it for the right to enjoy the facilities afforded by the licence. For the same reason the consideration given by that body for other services (e.g. to use the trade name Atrium Club or the equipment) must, where those services are standard rated, be kept to a minimum.

Implementing the WJB Chiltern project

42. On 14 February 2000 Mr James, a member of WJB Chiltern, visited the Atrium premises and discussed the proposals. He discovered that Jo Forman and Stuart Flude had already indicated to Mr and Mrs Bradney that they were interested in taking up the running of the Atrium Club activity. They were suitable candidates for the roles of directors of the new company that would succeed to the business then being carried on by Atrium Health; having them as directors of the new company

would separate it and make it independent of Atrium, Atrium Health and Mr and Mrs Bradney. An attraction of the proposal, Mr Bradney said, was that neither Jo Forman nor Stuart Flude would be required to put up any capital, which neither of them had anyway. Jo Forman did not herself recall any details of what had been discussed at that visit. But she said she understood that a special structure was needed to achieve exempt status for the sporting supplies. She had, she said, been happy to leave the arrangements to WJB Chiltern and Mr and Mrs Bradney knowing that she and Mr Flude could have opted out.

43. There was some urgency in getting the project implemented. By the end of March 2000 Atrium Health's turnover for the first period to which the changed law applied would have gone through the VAT threshold and its registration would have been required.

44. Mr James' first move was to send details of the new company. The Objects Clause of the Company's Memorandum contained the following:

> "The objects for which the Company is established are to provide sports and physical education facilities; to carry on all or any of the businesses of proprietors and operators of health and physical recreation centres ... ."

The Memorandum goes on to say:

> "The income and property of the Company shall be applied solely towards the promotion of its objects as set forth in this Memorandum of Association and no portion thereof shall be paid or transferred directly or indirectly by way of dividend, bonus or otherwise howsoever by way of profit, to members of the Company to the intent that any surplus arising from the activities of the Company shall in due course be applied in the carrying out of the objects and in particular (but without prejudice to the scope of other objects there mentioned) the provision of sports and physical educational facilities."

45. Mr James wrote a letter on 17 February to each of Mr and Mrs Bradney to make them aware of "all issues". The letter included a short summary of the conditions that had to be met if exemption was to be obtained for the new company's sporting services. The letter explained that Atrium, which was to make supplies of land to the non-profit making company running the Club business must be in no way connected with the new company. The necessary separation, so the letter records, could be "readily achieved" because Jo Forman and Stuart Flude "will take full control of the new profit making company while Katherine and Ron Bradney and anyone associated with them will stand back from the operation of a sports club and take much more of the role of landlord".

46. On 15 February 2000 Mr James had sent to Mr Bradney the necessary forms 288a for Appointment of Directors to AAB (and the memorandum and articles of association). The letter asks Mr Bradney to arrange for the forms 288a to be

completed as appropriate and returned. Also sent were draft contracts for appointment of the directors. A handwritten date of 1 March 2000 was added to these.

47. The terms of engagement of WJB Chiltern were agreed in writing on 14 February 2000. This was before Jo Forman and Stuart Flude could have been appointed as directors of AAB; the strong inference is that the scheme was set up in advance by the Bradneys and WJB Chiltern. The services to be provided by WJB Chiltern was "the structure developed by Chiltern to allow certain sports clubs to take advantage of the exemption from VAT in Schedule 9 Group 10". Specific services included the setting up of one corporate entity with "tailored memorandum and articles" and a "tailored licence agreement".

48. The start date for the new structure was fixed for 1 March 2000. The drafts of the paperwork supplied by WJB Chiltern came later but, said Jo Forman, the terms had been agreed between Mr and Mrs Bradney and WJB Chiltern and she trusted them.

49. Most of the scheme paperwork arrived from WJB Chiltern in early March. A letter from WJB Chiltern of 2 March explains that Atrium supplies to AAB the right to use the Atrium name, premises and equipment in return for which separate fees are to be levied. The "licence fee", the letter says, will be exempt from VAT. It states that NIC contributions should be made "by the person carrying on the business" and that the business should be dealt with separately for "income tax purposes". The paperwork included a "Warning" which opens with a direction that "these rules" should be followed otherwise "the structure established by" WJB Chiltern would be invalidated. The Warning explained that AAB was established as a non-profit making organisation "consequently any wealth must be accumulated" in Atrium. The Warning recommended that the assets, such as property rights, equipment and title to the name, should be held in Atrium. The Warning stressed that as AAB would be making exempt supplies, VAT charges from Atrium to AAB should be minimised in order to minimise irrecoverable VAT arising to AAB.

50. A paper headed "Education-Operation Checklist", sent by WJB Chiltern on 3 March contained a list of the legal and practical steps required to make the proposals work. Shortly summarised, these included:

(i) a properly incorporated company with a duly appointed board of directors and duly convened board and company meetings;
(ii) the opening of a bank account;
(iii) arrangements for standing orders and direct debits relating both to the supplies to the new company and its own sporting supplies;
(iv) a licence from the landlord to operate the business;
(v) a change to paperwork showing the new company as "the operator";
(vi) notification to insurers of employment liabilities and public liabilities of the fact that the new company is to be the provider;
(vii) new contracts of employment for staff involved in the provision of sporting services (and arrangements for the new company to pay those

staff) and proper notification to staff that the change does not affect their continuation of employment and their pensions;

(viii) a new PAYE scheme for the new company;

(ix) proper accounting, cash control and banking records;

(x) staff training in the new procedure and

(xi) agreement as to the amount of the licence fee and of the apportionments between standard rated and exempt items.

51. In at least two respects the implementation of the WJB Chiltern proposals failed to carry out those instructions. First, because AAB was unable to get an "originator number" for direct debits it had to continue to use Atrium Health's number. For this purpose Atrium Health, which then had an originator number, continued until late 2003 to collect direct debit subscriptions from Atrium Club members. Mr Bradney later set up an organisation called "Eazipay" which then collected memberships subscriptions on behalf of AAB in return for an administration charge. Second, the insurance arrangements were imprecise. AAB did not become a named insured until 6 February 2003; there was no evidence of cover, other than that effected by Atrium before then.

The agreements used in the WJB Chiltern project

52. A "Non-Exclusive Turnover Licence Agreement" dated 31 March 2000 and signed by Atrium and AAB granted to AAB a non-exclusive right to occupy the premises specified in an attached plan in return for a "licence fee" of, £2,000 per month plus 50% of the turnover of AAB or such other amount as [Atrium] may determine on giving 90 days notice. (The fee became 52% with effect from 1 July 2001 to reflect Atrium's installation, at its own cost, of a new lift.) The agreement purported to formalise an agreement that had been in place between the parties since 1 March 2000. The agreement states that Atrium grants to AAB a non-exclusive licence to occupy the premises. The agreement states that the benefit of the licence is non-exclusive and gives AAB "no right or interest in the premises". The agreement enables AAB to promote and carry on the Atrium Club business on the premises and AAB undertakes to use all reasonable endeavours to develop and further the business. AAB may recruit and dismiss all employees in the business. AAB may use the premises during "designated hours", i.e. the hours that Atrium may "from time to time in his absolute discretion determine on 90 days notice to" AAB.

53. The Turnover Licence Agreement entitles Atrium to terminate the licence on giving 90 days notice. AAB is entitled to terminate the licence on 1 March 2003 on 90 days notice, otherwise the licence continues on the same terms. Should AAB terminate the licence, it is required to sell its business to Atrium for an agreed price or a price determined by a valuer.

54. An equipment hire agreement dated 31 March 2000 between Atrium and AAB provided for Atrium to hire certain specified equipment to AAB in return for a flat monthly hire charge of £500 plus VAT (subsequently increased to £1,000 per month plus VAT by letter of 31 January 2001). The equipment so hired consists of the entire

hardware required to run the gym and comprised a substantial number of machines and other equipment. There were lists of equipment in the documents which included various items of studio equipment, kitchen equipment, members' changing room equipment and poolside equipment.

55. An agreement dated 31 March 2000 relating to the right to use a trading style between Atrium and AAB was entered into and signed. Under this AAB received the right to use the trading style "The Atrium Club" in return for a monthly royalty of £1 plus VAT. This entitled AAB to use the name in all kinds of advertising. It was to continue unbroken "until terminated".

56. A transfer of business agreement was entered into between Atrium Health and AAB on 31 March 2000. This was signed by the parties and was said to operate to transfer "part of the business of ... Atrium Health ..." in return for a payment of £1 plus a further payment for stock. The "part" in question was "the activity of providing services closely linked with and essential to sport or physical education in which members or casual visitors take part". Atrium Health also transferred to AAB "the benefit of the contracts of employment for the staff formerly employed by" Atrium Health. The business was that conducted by Atrium Health prior to the agreement. (In addition to transferring the running of the business to AAB, Atrium Health also remitted subscription income held by it in respect of supplies to be made to members in the future by AAB.)

57. An agency agreement between Atrium Health and AAB for the provision of banking services was entered into. Under this Atrium Health agreed to provide to AAB the use of an account for the purpose of collecting direct debits, banking cheques or cash and collecting any receipts due to AAB. (As explained earlier, the banking arrangements of AAB are said to have been operated in accordance with this agreement. AAB had not been able to get a bank to provide it with an originating number to enable it to collecting standing orders.)

58. A "rescission of Licence Agreement" between Atrium and Atrium Health (which was undated but signed by Mrs Bradney for Atrium and Mr Bradney for Atrium Health) refers to two earlier agreements said to have been entered into by the two companies in December 1996 under which, first, Atrium transferred the sports services business to Atrium Health and, second, granted Atrium Health a licence to use the premises and equipment of Atrium. The "rescission of Licence Agreement" was said to have taken effect from 1 March 2000. It recites that Atrium and Atrium Health "wish to terminate the Licence Agreement and to transfer the Business to [Atrium] with effect from 1 March 2000". This "agreement" is on the face of it inconsistent with the transfer of business agreement referred to above. The inconsistency is, I think, the result of too much haste rather than design. I see the transfer of business agreement as preserving the employment rights of Atrium Health's staff while the Rescission of Licence Agreement deals with and asserts Atrium's proprietary rights over the entire framework of the Atrium Club business.

59. From March 2000 Atrium continued to have an office in the Club premises; sometime in 2001 Mr and Mrs Bradney moved into and lived in the upper floors of the Club premises. The Club continued to operate under its existing name and its rules and regulations remained unchanged. The advertising material remained substantially the same and the logo remained the same. Jo Forman, Stuart Flude and the Club's existing staff became employees of AAB, their employments having been transferred from Atrium Health in pursuance of the Transfer of Business Agreement. Newly engaged staff were employed by AAB. AAB assumed responsibilities, as employer, for PAYE and NIC, for employment liabilities and for other statutory obligations.

60. The Club premises housed the Club business. This was run by AAB as principal under the direction and management of Jo Foreman and Stuart Flude, subject always to the constraints imposed by the Turnover Licence Agreement. AAB was committed to develop and further the interest of the business. AAB contracted with the members and with third party (i.e. non-Atrium) suppliers; in this respect AAB was directly liable, to the exclusion of Atrium, for all "debts obligations and all liabilities of whatsoever nature or kind which may arise or otherwise be incurred in the carrying on of the business" (see Clause 2.5 of the Turnover Licence Agreement).

61. The Club premises also housed the "sunbed" business and the retail operations that had been retained by Atrium and by Mr and Mrs Bradney.

62. There were overlaps between the operations of Mr and Mrs Bradney and Atrium on the one hand and those purportedly conducted by AAB. Insurance cover, as already noted, remained for two to three years in the name of Atrium. The Club was advertised as being linked to another club associated with Mr and Mrs Bradney in Cambridge and combined stationery showing the name of the Cambridge Club, also trading under the style of "The Atrium Club" was in use before and after the transfer. Atrium Club, as noted, continued to collecting direct debit subscriptions from club members. AAB ran the sunbed business, apparently for no charge.

63. AAB kept separate books and business records. It presented its own statutory accounts for five years (until liquidation) showing all receipts from members as its "turnover" or sales income and the licence fees and other payments due to Atrium were included as its "cost of sales" or expenditure. The liquidator's report acknowledged that the goodwill of the Club business, assessed at £15,000, was the property of AAB.

64. Atrium's business for 2000 onwards was confined to the non-sporting activities such as the letting out of sunbeds, and providing equipment to AAB. Its accounts were presented on the basis that it had no proprietary interest in the club business save to the extent that it was entitled to participate through the licence fees.

65. The evidence shows that those involved in the WJB Chiltern project set it up and operated the new structure as an enduring arrangement. Their expectation was

that the scheme worked and that the supplies of sporting services to members and other club users were and will continue to be exempt. Those expectations had been founded on what was then perceived to be the well-established principle that, in the VAT environment, each step in the scheme was to be considered individually. Reliance in this connection was placed on the observations of Lord Hoffman in *Customs and Excise Commissioners v Robert Gordon's College* [1995] STC 10943 at 1099. The HMRC challenge to the *Messenger Leisure Developments Ltd Arrangements* [2005] STC 1078 (CA) did not become apparent until the VAT and Duties Tribunal hearing in the appeal held in March 2002.

66. It will be recalled that until the end of February 2000, the Club members were contracted to Atrium Health. There was some dispute as to whether any proper notification had been given to those club members that AAB was to take over the running of the Club from Atrium Health. A notice, said to have been exhibited in the Club, was provided in evidence. HMRC questioned whether this had in fact been drawn to the members' attention. I accept Mr Bradney's evidence that it was duly exhibited. It will be recalled that it was the top priority in the list of requirements for the AIC proposal in 1996. Mrs Bradney had taken responsibility for it. The WJB Chiltern programme did not specifically provide for such notification. Nonetheless, I have concluded that notification was duly made in the manner explained. In any event, even if notification had not been made by AAB, I would not accept that the membership contracts had moved from Atrium Health to Atrium. It was totally alien to the WJB Chiltern scheme that Atrium should ever become the operator of the Club and the party contracting with the members. Finally in this connection I should mention that a large proportion of the individuals to whom supplies were made during the period under assessment were never members of the Club at the time when the business was actually operated by Atrium. They never had any contractual relationship with Atrium. The evidence shows that, of the sums assessed on Atrium (some £440,000), only some £66,000 was attributable to the individuals with whom Atrium originally contracted for the supply of services.

67. In 2002 the WJB Chiltern project, as used by Atrium and AAB, caught the eye of HMRC. Evidence was given by Mr R J Youngs, a Customs officer, about the subsequent enquiries and information obtained. As a result of their enquiries (paragraph 6 of the Amended Statement of Case records) HMRC "concluded that VAT had not been correctly accounted for on the supplies made at the Club and that, in particular (1) Atrium had continued to make supplies of sporting services at the Club despite the arrangements with Atrium Health and then with AAB and (2) even if AAB had, with effect from March 2000, made the supplies at the Club, those supplies were not (as AAB contended) exempt but were taxable. The decision to assess was based also on HMRC's adoption of the abusive practice principle as summarised above.

68. AAB was also assessed to tax on the basis that its supplies of services to members should be standard rated and not exempt. As the Turnover Licence Agreement had had the intended effect of stripping AAB of all surplus income and of all reserves, AAB faced insolvency as the result of the assessment, assuming it was

correct. AAB took separate advice. The advice was that AAB had less than a 50% chance of resisting the assessments. In February 2006 AAB was placed in liquidation with HMRC as by far its biggest creditor. AAB's business was transferred to FAB Ltd and by May 2006 FAB Ltd was registered as the taxable supplier of services to members of the Club. FAB Ltd operates under a licence from Atrium and it is managed by Jo Forman and Stephen Bradley. Neither Mr nor Mrs Bradney are members or directors of FAB Ltd.

Were the supplies of sporting services to members the supplies of Atrium or of AAB?

69. I approach this question first as a blackletter exercise and ask whether, as HMRC submit, the agreements that came into being to implement the WJB Chiltern scheme do not properly represent the nature of the supplies that have been made to the members. For this purpose it is necessary to construe the nature of the supplies in the light of all the facts of the case and to take account of the fact that the VAT analysis may not follow the contractual analysis. It is necessary to bear in mind that the prevention of possible tax evasion, avoidance and abuse is an objective recognised and encouraged by the Sixth Directive: see paragraph 71 of the Court's decision in *Halifax*. In this connection I record the opinion of the Advocate General in *Temco Europe SA* (Case C-284/03) [2005] STC 1451 where, in paragraph 36, he says:

> "The national courts are obliged to be even more rigorous when confronted with ingenious legal manoeuvres devised with the intent of evading the application of a provision and must enforce the neutrality rule which governs the common system of VAT".

70. The WJB Chiltern scheme was indeed "an ingenious legal manoeuvre". The object was to create an "eligible body" falling within Note (2A) to Group 1 of Schedule 9. AAB was designed as such and for this purpose and to eliminate profit its turnover was stripped out by means of the Turnover Licence Agreement. I do not however consider that this feature enables me to "enforce the neutrality rule" by concluding that the supplies to members were made by Atrium rather than by AAB. Atrium never contracted with the members to provide sporting services. AAB did not have the wherewithal to do so. It had no staff, other than Mr and Mrs Bradney whose time and attention were taken up with other matters. Atrium had licensed AAB to carry on the Club activities and to use the Atrium Club name. The terms of the licence were so one-sided, in the sense that Atrium had the unilateral rights to terminate the Turnover Licence Agreement and to uplift the licence fee, that AAB's proprietorship of the Club business hung by a thin thread. But that feature does not displace the fact that AAB committed itself to the members year after year to provide the services of Atrium Club membership in the form of access to all its sporting facilities. To enable it to provide those services AAB engaged and paid its staff and accounted to HMRC for tax and NIC.

71. Things did not, as already mentioned, go entirely to plan. The insurance arrangements were unclear, at least for the first two to three years, and it appears that

Atrium may have been the insured person. AAB never obtained an originating number and the direct debit payments for members were therefore collected by Atrium Health which had one. But neither of those factors nor the one-sided feature of the Turnover Licence Agreement nor Atrium's dominant position can in my view displace the fact that AAB had committed itself to each of its members and supplied the sporting services to them.

72. For those reasons I am against HMRC on the traditional strict law approach to the issue.

The application of the Halifax principle

73. HMRC argue that the *Halifax* "abusive practice" doctrine applies in the present circumstances. The transactions concerned, argued Mr Owain Thomas for HMRC, resulted in a tax advantage the grant of which was contrary to the relevant provisions of the Sixth Directive; moreover, they say, the essential aim of the transactions was to obtain a tax advantage. HMRC's decision on the redefinition required by paragraphs 96-98 of *Halifax* is as stated in paragraph 13 of their Amended Statement of Case. See paragraph 11 above. The transaction which AAB is said to have entered into in respect of the disputed supplies is to be treated, they say, as having been entered into by Atrium for tax purposes. HMRC's decision has been to assess accordingly and they have done this to the best of their judgment.

74. The response for Atrium, presented by Mr Roger Thomas, is to say that there has been no tax avoidance. The scheme never worked. The *Halifax* doctrine was not therefore engaged.

75. The following passages from the decision of the Court of Justice in *Halifax* are relevant to the present considerations:

> "85. ... the Sixth Directive must be interpreted as precluding any right of a taxable person to deduct input VAT where the transactions from which that right derives constitute an abusive practice.
>
> 86. For it to be found that an abusive practice exists, it is necessary, first, for the transactions concerned, notwithstanding formal application of the conditions laid down by the relevant provisions of the Sixth Directive and of national legislation transposing it, result in the accrual of the tax advantage the grant of which would be contrary to the purpose of those provisions. Second, it must also be apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain a tax advantage ...
>
> 94. ... Transactions involved in an abusive practice must be redefined so as to re-establish the situation that would have prevailed in the absence of the transactions constituting that abusive practice."

76. Lord Neuberger's judgment in *WHA v R&CC* [2007] STC 1695 identifies, in paragraph 12, the 4-stage approach as follows:

> "The abuse issue can usually be considered by answering four questions ... . First, does the Scheme, or an aspect of the Scheme, result in the accrual of a tax advantage which, as HMRC assert, is contrary to the purpose of the provisions of the Sixth Directive? Secondly, if so, was it, as HMRC contend, the essential aim of the Scheme, or of the relevant aspect, that a tax advantage be obtained? Thirdly, if so, are there any special features of the scheme itself, or of the law relating to it, which should nonetheless prevent the abuse argument succeeding? Fourthly, if not, can (must) the Scheme, or the relevant part, be redefined?"

77. Addressing the initial question of whether the Scheme (or an aspect of it) results in the accrual of a tax advantage contrary to the provisions of the Sixth Directive, it is necessary to identify what tax advantage the scheme sought to achieve and whether that tax advantage resulted. The tax advantage sought from the WJB Chiltern scheme was to make exempt the supplies of sporting services to customers. These would have been standard rated had they been made by Atrium because Atrium was a non-profit making organisation; they would have been standard rated had they been made by Atrium Health because Atrium Health did not qualify as an "eligible body" under the provisions of SI 1999/1994. The Scheme had two inter-related features, both installed to make the supplier an eligible body. AAB was created as a company limited by guarantee with a constitution that prevented distributions of surpluses. The Turnover Licence Agreement was put in place as an essential part of the scheme to strip out any surpluses arising to AAB thereby effectively removing AAB's capacity to make profit and to pass these surpluses on to Atrium in the form of exempt licence fees.

78 Did the tax advantage sought from the WJB Chiltern scheme result? In my view (and for the reasons that I will give in paragraphs 81 and 82 below) it did not. AAB's supplies were all, contrary to the plans and expectations of WJB Chiltern, of Mr and Mrs Bradney and of Atrium, standard rated. The liquidation of AAB in 2006 was not part of the scheme. It follows that the initial condition for the operation of the *Halifax* principle has not been satisfied. The fact that the obtaining of the tax advantage was the "essential", albeit misplaced, aim of the scheme does not reinstate the operation of the *Halifax* principle.

79. That AAB failed to qualify as an eligible body was in a sense common ground. HMRC have assessed it to tax, presumably on best of judgment grounds, on the basis that its supplies to members were all standard rated. Mr Owain Thomas for HMRC in this appeal was reluctant to concede the correctness of the assessment in the absence of any appeal by AAB or the liquidator. Mr Roger Thomas for Atrium argued that AAB had been correctly assessed and was indeed liable for the tax which HMRC was now seeking to recover from Atrium.

80. In my opinion AAB was correctly assessed. The decision of the Court of Appeal in *Messenger Leisure Developments v R&CC* [2005] STC 1078 adopted the reasoning of the Court of Justice in *Kennemer Golf & Country Club* (Case C-174/00) [2002] STC 502 in determining whether the sporting supplies of a non-profit making company that was the subsidiary of a profit making company were exempted by Article 13A.1(m). The judgment of Jonathan Parker LJ (with which the rest of the Court of Appeal agreed) contains the following passage:

> "... Whether or not an organisation is non-profit making for the purposes of Article 13A.1(m) must, as the Court of Justice tells us, depend on the "aim which it pursues". ... [In] determining what is the "aim" which the organisation is pursuing when it makes the supply in question it is necessary to look at the transactions in question in their full factual context. Thus, the fact that an organisation systematically achieves surpluses which it retains for its own purposes may, depending on the context, demonstrate an aim which is far removed from "non-profit making"."

81. Here, the Turnover Licence Agreement was an integral part of the WJB Chiltern scheme. The scheme required AAB to be incorporated with a constitution that prohibited distributions of profits; AAB had to be separated in all relevant respects from Mr and Mrs Bradney, from Atrium and from Atrium Health. The Turnover Licence Agreement was the essential part of the scheme machinery designed to pass over to Atrium the profits that would otherwise have been earned and enjoyed by AAB. All those things happened. But for the Turnover Licence Agreement, AAB would have systematically achieved surpluses. Thus, looking at the transactions in question in their full factual context, AAB failed to qualify as a non-profit making organisation within Article 13A.1(m) its supplies were not therefore exempt. AAB was the taxable person in relation to the supplies to members and no tax advantage accrued. I recognise that HMRC have been deprived of the tax for which AAB should have been accountable. But, as I observed earlier, the WJB Chiltern scheme was expected to work; consequently no amount representing the tax was kept in reserve in case the scheme failed. Moreover, liquidation of AAB was no part of the scheme.

82. For those reasons I do not think that the *Halifax* abusive practice principle is engaged. For what it is worth I record that I would have been satisfied on the second question. The essential but mistaken aim of the transactions was to obtain the tax advantage that I have identified above. This is evident from the explanations given by WJB Chiltern in their letter of February 2000 and from the contents of the "Warning" provided by them. The Scheme was designed to navigate a way through the anti-avoidance provisions introduced by SI 1999/1994. I can see no special features of the Scheme itself that could prevent the *Halifax* abuse doctrine from applying.

83. I do not therefore need to go on and redefine the relevant transaction for tax purposes. But in case I were wrong in my decision that *Halifax* does not apply here, I need to address the question whether HMRC's decision as to the redefined transaction

can stand. The basis for their decision is that the routing of supplies to members via AAB is the abusive practice. They redefined the transactions involved in the abusive practice by re-routing these supplies from Atrium to the club member, that being the situation that would, they claim, have prevailed in the absence of the transactions constituting the abusive practice. On that basis HMRC have assessed all the membership fees and guests fees as standard rated income.

84. I am not satisfied that HMRC's redefinition can stand. It does not "re-establish the situation that would have prevailed in the absence of the transactions constituting the abusive practice". That situation must at least be a real world one. Here the real world situation consisted of Atrium which from December 1996 to the present time has not operated the gym and has had no staff. Atrium had nothing to offer the members. By contrast AAB had the means of providing the services to members. It was set up to last. Everyone involved, from Mr and Mrs Bradney to the actual Club members, expected this state of affairs to continue and it did so until called to a halt at the initiative of HMRC. And even then the Club activities did not revert to Atrium; they were passed on to FAB Ltd which has continued until this day to carry them on as principal under the management of Jo Forman, Stephen Bradley and other members of the staff.

85. To redefine effectively, in the manner of HMRC's decision, would involve disregarding the contracts between AAB and its members and disregarding the transfer of the engagements of the staff from Atrium Health to AAB (and particularly the activities of the key players responsible for running the Club such as Jo Foreman and Stuart Flude). Atrium had nothing to offer to the members and the staff had no reason for being re-engaged by Atrium.

86. The present situation is, in my view, one that would be incapable of redefinition in the manner of HMRC's decision. It is unlike the situation in *Halifax* where the construction services would in the real world have been supplied to *Halifax* itself until the scheme was implemented and those construction services were diverted to CWPI. It is unlike the state of affairs in *Lime Avenue Sales and Services* [2007] V&DTR 55 (2007) No.20140 where the construction services were to have been made to Benenden School and the scheme diverted these to Lime Avenue (the school shop) to enable it to provide the school with the new study centre. In both those cases the redefinition reinstated the real world. The decision in issue here does not. There may be other ways in which the arrangements involving Atrium and AAB could be redefined. The six agreements of March 2000 between those two companies might be aggregated together. If taken as part of a single agreement the Turnover Licence Agreement element might, in light of the principles found in paragraphs 17 to 20 of the decision of the Court of Justice in *Belgium v Temco Europe SA* supra, lose its status as a letting or leasing of immoveable property and the fees could become consideration for a standard rated supply. But that was not the decision of HMRC under appeal in the present proceedings.

Conclusion

87. For all the reasons given above, I allow Atrium's appeal. I award Atrium their costs.

SIR STEPHEN OLIVER QC
CHAIRMAN

RELEASED:

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