[2010] UKUT 463 (TCC)

Appeal number: FTC 10/2009

Value Added Tax – Land and Property – Holiday home – Associated companies supplying land and building services - Nature of supplies – Whether separate supplies of land and construction services – Yes – Whether abusive practice - Halifax [2005] STC 919 considered – Single supply of completed holiday homes - No - Proper Comparator – Appeal allowed

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

THE LOWER MILL ESTATE LTD **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **Respondents**

TRIBUNAL: MR JUSTICE WARREN
JUDGE THEODORE WALLACE

Sitting in public in London on 28-30 June 2010

Jonathan Peacock QC and Jolyon Maugham, instructed by Michael Welch & Co, for the Appellant

Malcolm Gammie QC and Vikram Sachdeva, instructed by the Solicitor for HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This is an appeal against the decision ("the Decision") of the Tax Chamber of First-tier Tribunal ("the Tribunal") (Judge Khan and Mr P Davda) dismissing the appeal of the Appellant, The Lower Mill Estate Limited ("LME"), against an assessment to VAT raised by the Respondents ("HMRC") notified in a letter from HMRC dated 18 February 2008 ("the Assessment"). Conservation Builders Limited ("CBL") had appealed against an equivalent assessment; we shall need to say more about that later.

2. The background is this. LME is the freeholder of land at Somerford Keynes, Cirencester with the benefits of planning permission for the construction of up to 575 residential homes subject (immaterial exceptions aside) to a condition that they shall not be occupied as principal places of residence. For VAT purposes they are therefore regarded as holiday or second homes.

3. The development of the land has taken place by LME granting Agreements for Lease of particular plots to third party customers. Leases for 999 years were then granted by LME pursuant to those Agreements and VAT was charged on those Leases. During the period covered by the Assessment – 1 January 2005 to 30 June 2007 – those customers also signed Build Agreements with CBL for CBL to construct a holiday or second home on each such plot. Those Build Agreements provided for stage payments to be made to CBL as various stages of the building works were completed. LME and CBL were at all material

times in the common ownership of a single shareholder, Mr Jeremy Michael Paxton ("JMP").

4. HMRC sought to uphold the Assessment on the provision of these holiday homes to customers. HMRC contended, in essence, that the Leases and Build Agreements should be treated as effecting single supplies of completed holiday homes. The Tribunal rejected that contention. However, they held that the transactions concerned constituted an abuse of rights such that the VAT treatment fell to be redefined in accordance with the principle in Case C-255/02 *Halifax plc v Customs & Excise Commissioners* [2006] STC 919 ("*Halifax*").

5. LME says that the Tribunal were right to reject the "single supply" contention. In relation to *Halifax*, LME says that there are decisive errors of law in the way in which the Tribunal approached both the first and second limbs of *Halifax* (as to which see below). Moreover, LME submits that the Tribunal's findings of fact disclose a catalogue of errors of law with the consequence that their conclusion on the appeal cannot stand.

6. In a Response under Rule 24 of The Tribunal Procedure (Upper Tribunal) Rules 2009 HMRC opposed the appeal on the grounds (1) that the Tribunal were entitled to find that there was an abusive practice and (2) that there were single supplies by LME of holiday homes to the purchasers or alternatively that there were joint supplies by LME and CBL of completed holiday homes.

Ground (2) was in effect a cross-appeal since the Tribunal had decided that apart from *Halifax* there were separate supplies by LME and CBL.

7. The supplies by LME of leases to customers were, taken by themselves, standard rated, being excluded from exemption under Schedule 9, Group 1 of the Value Added Tax Act 1994 ("the VATA") by virtue of item 1(e) as the grant of an interest in holiday accommodation. Supplies by CBL, whether to purchasers or to LME, were zero-rated, being supplies in the course of construction of dwellings within Schedule 8, Group 5, item 2(a); similarly supplies by sub-contractors to CBL were zero-rated. A supply of a completed holiday home is excluded from exemption because of item 1(e) of Group 1 of Schedule 9 and is not zero-rated under item 1 of Group 5 of Schedule 8 because of the restriction on residence which is covered by Note (13) to Group 5. The planning permission in the present case restricted occupation to 11 months of the year.

8. The Assessment was for the sum of £2,867,539 for the period 1 January 2005 to 30 June 2007. It is to be found at Annex 5 to the letter from HMRC dated 18 February 2008. This is a long and complex letter, setting out HMRC's reasons for rejecting LME's arguments that there should be no assessment. It provided for alternative approaches in case the preferred approach should be rejected by the Courts. HMRC reached a number of different alternative decisions: there was a Main Decision, an Alternative Decision and a Further Alternative Decision.

9. The Main Decision was that LME made single supplies to the purchasers of completed holiday homes which were standard rated and that CBL made zero-rated supplies of construction services to LME rather than to the purchasers. On this footing LME was assessed on sums equal to the stage payments received by CBL from purchasers and it was on this basis that the Assessment was made.

10. The Alternative Decision was that, if CBL did not make supplies of construction service to LME, then it made supplies to customers. But these supplies were of completed buildings rather than supplies of construction services. On this footing CBL was to be assessed on the sums received from purchasers which it had treated as zero-rated. Accordingly, an alternative assessment was made. It is to be found at Annex 6 to the letter. The letter stressed that the preferred assessment and the alternative assessment were mutually exclusive and that no action would be taken to enforce the latter unless and until the former was found to be incorrect. We have not heard full argument on the permissibility of making alternative assessments in this way and proceed on the basis that it was a valid course of conduct.

11. The basis of the Alternative Decision was altered in an amendment to paragraph 7 of HMRC's Statement of Case to a decision that if LME alone did not make a supply of the holiday home to the purchaser then both LME and CBL made a joint supply of the completed holiday home, the proportion of the

supply for which CBL was responsible being the value of the construction services. HMRC appeared, therefore, to have abandoned the contention that CBL alone made supplies of completed holiday homes to customers.

12. The Further Alternative Decision was that the arrangements amounted to an abusive practice and that the transactions must be redefined to re-establish the position that would have prevailed if LME as owner and developer had made standard rated supplies in respect of each holiday home of the completed building with the land.

The basic facts

13. LME was incorporated in 1997 and was and is the freeholder of 158 hectares of land known as Lower Mill Estate, Somerford Keynes, Cirencester. CBL was incorporated in 1999 and supplied construction services using sub-contractors. The shares in both companies were at all material times owned by JMP who is the sole director of LME and is one of two directors of CBL.

14. The Lower Mill Estate consisted of former gravel pits which had been turned into a large nature reserve. On 4 February 1999 outline planning permission was granted for up to 395 residential homes as holiday units, a country club, the use of lakes for recreational activity and associated leisure activities. Condition 16 specified:

> "the holiday units to be erected as part of the development shall be occupied for holiday accommodation only and for the avoidance of

doubt shall not be occupied as permanent unrestricted residential accommodation or as a principal or primary places of residence."

15. Condition 17 prohibited occupation from 6 January to 5 February inclusive in each year. An agreement was entered into with the local authority under section 106 of the Town and Country Planning Act 1970.

16. The infrastructure development, including roads, power, water, drainage and leisure facilities, was undertaken in phases through sub-contractors with private funding provided by a third party.

17. Outline consent for a further 160 holiday homes with similar conditions was given on 29 January 2001. The Decision recorded that there was planning permission for up to 575 residential homes in all.

18. The development was undertaken in phases and constructed around a network of small "villages". Mill Village was built between 1999 and 2003 with 78 holiday homes. There was planning permission for 95 holiday homes in Clearwater Village; by June 2007 approximately 90 of the plots had been sold and 74 homes had been built. Development in Howells Mere Village for 125 holiday homes started in June 2007 but was not covered by the assessments under appeal. Further phases involving two "villages" were to follow.

19. The houses were of different styles and designs. The Statement of Case stated that there were at least 30 different styles and sizes ranging from two bedroom

terraced houses to four bedroom detached houses. "Landmark" properties individually designed by leading architects achieved the highest prices for both plots and buildings. The detailed planning permission specified the external designs.

20. The Decision recorded this at paragraphs 11 to 15:

> "11. The infrastructure development was undertaken in phases, depending on the particular village which was being developed. The development of the infrastructure work and house building was carried out by CBL, using third party contractors. CBL engages the services of contractors under what can be described as over-arching agreements in anticipation of the completion of the sale of a specified number of plot of lands. CBL would engage contractors under a blank contract for a specified amount of labour and material and for a specified number of houses. However, contractors were only paid for work actually undertaken and invoiced by CBL, which may or may not be all the work specified in the contract. In this sense, the contract was similar to a tender document which sought to attract best prices from contractors. The contracts were not signed but allowed CBL to have an indication of the prices which the sub-contractor would charge for specified work without creating an obligation on the contractor to actually carry out the work.
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> 12. The holiday homes in each 'village' are marketed by LME before and during construction. Plots of land are allocated for sale to buyers before or during construction of holiday homes, depending on when the buyer purchases or signs up to purchase.
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> 13. There are two categories of sales. In the first category, 'Category One' which covered over 90% of sales, construction of a holiday home took place on a vacant plot of land. In such a case, the sale of a plot of land would be standard rated for VAT purposes and there would be no construction on the land at the time of the sale.
>
> 14. In 'Category Two', construction (under a licence to build granted by LME to CBL) of a holiday home would have started on the plot of land but would not have been completed before a long lease on the plot is purchased. The invoice for the purchase would show a sum of money for the purchase of the plot and a sum of money for the building works both of which would be standard rated. There was a third

category, 'Category Three' where two show houses were completed on plots of land and these were sold separately. They were standard rated sales.

15. It is important to explain how the sales were actually undertaken. This point by point explanation illustrates the sales process:

(a) The on-site sale operations were run by LME. Customers coming to the on-site sale shop would make enquiries of plots of land and would be informed, at the same time, of the construction services offered by CBL. The customer therefore agreed to purchase a holiday home but it is treated as two transactions — the sale of land and the purchase of construction services.

(b) The customer is asked to pay what is called a 'reservation fee' of approximately £2000-£5000 as a deposit on the holiday home purchased. After payment, the sales office would provide a letter to the customer outlining the terms and conditions of the sale together with a timetable for payment. Where the customer elects to use CBL, the letter would refer to the construction service agreement with CBL ('Build Agreement').

(c) The lawyers for the parties would then get involved in the transactions. The customers' lawyer would receive a proposed agreement for lease (and later a lease) which are to be entered into with LME. Since the letter requesting the deposit was subject to a contract, in principle, a customer could enter into the lease with LME and not the Build Agreement with CBL.

(d) While outline planning permission was given for the holiday homes customers often requested variations to the internal fixtures, fittings and decorations which meant that the construction price would have to be varied. The planning permission was given with respect to the structure and external appearance of the home. Customers frequently requested CBL to apply to change the permission which had been given. The planning permission was applied for by LME as freeholder. In this sense, many homes were custom-built for the customer and incorporated their own requirements into the holiday home.

(e) Once an agreement for a lease has been signed with LME, an invoice was issued for the price attributable to the premium paid for the Lease plus VAT and this sum was paid to LME on completion of the plot purchased.

> (f) Under the Build Agreement entered into with CBL, (after the completion of the agreement for a lease), CBL starts construction work on the basis of six defined stages of construction and payments for each of those defined stages on production of an architect's certificate of completion for that stage. Payment is made to CBL. No VAT is charged to the customer as the services are treated as zero-rated. Normally the period of time between the grant of the lease and the final stage payment for building will be 12-18 months.
>
> (g) Where construction of a holiday home had started (Category Two) before the lease was signed, an invoice is issued by LME to the customer for the total value of all stage payments. LME treats the payment as VAT inclusive and issues a VAT invoice to the customer."

21. The appeal primarily concerned Category One sales where there was no existing building when the plot was leased. Where works had been carried out by the time of the grant of the lease, VAT was charged on those works as part of the land.

The single or separate supply issue

22. Although the appeal is by LME against the decision that there was an abusive practice within the *Halifax* principle, it is convenient to consider first the single supply issue raised by HMRC since that comes first logically.

23. The Tribunal dealt with the Main Decision that there were single supplies by LME at paragraphs 59 to 75 of the decision and dealt with the amended Alternative Decision that there were joint supplies by LME and CBL at paragraphs 76 to 81.

24. In relation to the single supply issue, the Tribunal referred to a number of decisions of the Court of Justice including *Card Protection Plan Ltd v Customs and Excise Commissioners* (Case C-349/96) [1990] STC 270 and to further proceedings in that case in the House of Lords (see [2001] STC 174) (together "*CPP*").

25. They then turned to consider the decision of the Court of Appeal in *Telewest Communications plc v Customs and Excise Commissioners* [2005] STC 481 ("*Telewest*").

26. *Telewest* was a case where there were two supplies and two suppliers. Cable television was supplied by one of the regional companies in the Telewest group; and, following arrangements implemented with the specific object of achieving supplies which were not ancillary to the provision of cable television services, a subsidiary of Telewest Communications Ltd (the parent company of the group) was formed to provide copies of the Cable Guide magazine (the listings guide for programmes available on cable tv). Viewed as a separate supply, the latter provision was zero-rated as a publication.

27. One of the arguments in *Telewest* was referred to as "the package argument". Another was referred to as "the *CPP* argument". They were explained by Arden LJ at [39]:

> "Telewest's case on this appeal is (in summary) that the VAT analysis should in this case follow the contract analysis. Telewest submits that the judge was in error in treating as relevant the fact that a customer

could not subscribe for the television services without taking the magazine as well (this was called 'the package argument'). It is not appropriate to ask whether the supply was ancillary to the principal supply of services by Telewest because the doctrine of ancillary supply in VAT law applies only where there is only one supplier ('the *CPP* argument'). In addition the jurisprudence does not support the argument that the VAT position should look to the economic reality of the situation and treat Publications and Telewest as a single supplier ('the artificiality argument').

28. Although there can, in principle, be a single supply by a single supplier where one supply is ancillary to another, Arden LJ rejected, at [67], HMRC's submission, based on the decision in the *French Tips* case (*Commission v France*, Case C-404/99, [2001] ECR 1–2667) that linked transactions will be treated as a single supply. She also identified, at [69], further objections to treating the two supplies in that case as a single supply "merely because the customer could not enter into one transaction without the other". In the present case, that element is absent, making HMRC's case weaker than in *Telewest*. In the present case, customers were not required to use CBL as their contractor; and it is nothing to the point on the package argument that in practice customers universally did so. As Arden LJ noted, at [70], at a certain point the package argument merges into the *CPP* argument and the so-called artificiality argument (to the effect that the VAT position should look to the economic reality of the situation and, in *Telewest*, so as to treat Publications and Telewest as a single supplier). She concluded that there were limits on the extent to which transactions could be recharacterised in VAT law, or, to put it another way, limits on the extent to which taxpayers could be denied the exemptions on which they seek to rely. Accordingly, she accepted the

submissions of Mr Milne QC (for Telewest) that the expectation of the customer was relevant to the question whether two contracts constitute, for VAT purposes, principal and ancillary contracts, but not to the question of whether there is more than one supplier.

29. As to the *CPP* argument, Mr Vajda (for HMRC) submitted that the principles established in *CPP* extended to a situation where there are two suppliers who ought to be treated as one. Arden LJ rejected that submission. She agreed with the judge (Sir Francis Ferris) who had concluded that there was nothing in *CPP* "to justify the proposition that where [there are two separate contracts] the supply made by one supplier, Publications, takes the tax treatment applicable to the supply made by the other".

30. Arden LJ, at [80], also expressly agreed with the judge that two cases referred to by her and by the judge had not been superseded by the *French Laboratories* case (*Commission v France* (Case C76/99) [2001] All ER (D) 33) which Mr Vajda had relied on for the proposition that supplies by two suppliers are capable of receiving the same tax treatment. It is worth setting out what the judge had said:

> **"[103]** On behalf of the appellants I was referred to two English cases as showing that the proposition advanced on behalf of the commissioners is fallacious. The first was *Customs and Excise Comrs v Wellington Private Hospital Ltd* [1997] STC 445 one of the issues in which was whether the supply of drugs to patients admitted to a private hospital was to be treated as part of the same supply as the provision of accommodation and nursing care or a separate supply. Millett LJ, with whom Hutchinson LJ agreed, said (at 462):

> 'In determining whether what would otherwise be two supplies should be regarded as a single supply the court has to ask itself whether one element is an "integral part" of the other, or is "ancillary" or "incidental" to the other; or (in the decisions of the Court of Justice) whether the two elements are "physically and economically dissociable". This, however, merely replaces one question with another. In order to answer this further question, the court must consider "what is the true and substantial nature of the consideration given for the payment" … There are, however, limits to this process. Where supplies are made by different suppliers, they cannot be fused together to make a single supply, and it is probably only in relatively simple transactions that the reduction of multiple to single supplies is appropriate.'

Later on (at 464) he said:

> 'It is to be observed that in all the cases which have previously come before the court, the question has been whether a single transaction for a single price should be properly apportioned into two or more supplies. What the contracting parties have joined together, the commissioners may put asunder, but what the contracting parties have themselves separated; … I do not think that the commissioners can join together.'

[104] The second case was *Nell Gwynn House Maintenance Fund Trustees v Customs and Excise Comrs* [1999] STC 79, [1999] 1 WLR 174 which concerned the liability to VAT of the trustees of a maintenance fund in respect of maintenance payments made by lessees. In relation to one issue it was accepted that if the maintenance had been undertaken by the lessor the supply of the relevant services would be exempt from VAT by virtue of the exemption applicable to the leasing or letting of immovable property. But it was contended that the position was different where, as in the *Nell Gwynn* case, the maintenance was undertaken by trustees who were separate from the lessor. Lord Slynn, with whom the rest of their lordships agreed, rejected an argument based upon *Henriksen* Case 178/88 [1990] STC 768. He said ([1999] SRC 79 at 92, [1999] 1 WLR 174 at 185):

> 'In *Henriksen* one of the lettings was exempt as a letting of immovable property and the other letting was excluded from the exemption as "premises and sites for parking vehicles". The question was how one interpreted the exemption read with the exclusion in a situation where there was a close relationship between the two lettings. In the present case we are dealing with immovable property in Art 13B(b) which is

> exempt but not with any of the exclusions from the exemption. The supply of services is quite separate from any of the exclusions and is by a different taxpayer. Accordingly, it does not seem to me that the linking of two services so as to treat them as one arises.'

Lord Slynn then cited the first of the two passages from the judgment of Millett LJ which I have set out above and said he agreed with him as to the conclusion in the final sentence where he said:

> 'Where supplies are made by different suppliers, they cannot be fused together to make a single supply; and it is probably only in relatively simple transactions that the reduction of multiple to single supplies is appropriate.'

[105] These passages from the *Wellington Hospital* and *Nell Gwynn* cases are directly contrary to the argument advanced on behalf of the commissioners. I think Mr Vajda found himself constrained to admit this. But he said that these cases were decided before the *French Laboratories* case (which, of course, is true) and he contended that if Millett LJ and Lord Slynn had had the benefit of knowing what the Court of Justice decided in that case they would have expressed themselves differently. I do not accept this. For the reasons which I have endeavoured to explain I consider that the *French Laboratories* case was concerned with a quite different issue. It is, in my view, distinguishable on much the same grounds as those on which Lord Slynn distinguished *Henriksen*."

31. Arden LJ dealt with the artificiality argument (under the heading "The artificiality issue") at [81] to [88]. Her rejection of HMRC's case on artificiality in *Telewest* was uncompromising. We cite some of what she had to say:

> "[83] In my judgment, there is an objection in principle in this field of law to taxing transactions according to their economic reality. The economic reality of a transaction is antithetical to legal certainty. If VAT is payable according to economic reality, the seller will not know what VAT to account for, and the purchaser will not know what to VAT to pay. The system for the collection of VAT would no longer be straightforward. Accordingly, there seem to me strong policy reasons against the course which Mr Vajda invites us to take. The principle of legal certainty is one recognised and applied by the Court of Justice in

this field (see, for example, the *Cantor Fitzgerald* case Case C-108/99 [2002] QB 546; [2001] STC 1493 at [33])……..

……

"[87] ……The mere fact that the court seeks to find the commercial reality of a transaction does not mean that it would seek to apply the economic reality of the transaction. The economic reality of the transaction may have nothing to do with either the essential features of what the parties agreed or the legal structure of their transaction. Moreover, as this court said in *Tesco plc v CCE* [2003] STC 1561: 'Economic *purpose* is not the same as economic *effect*' [159] (emphasis added in original).

[88] Economic reality must also be distinguished from economic neutrality, which is a principle of VAT law. This principle, illustrated by the *French Tips* case, precludes *inter alia* persons carrying on the same activities from being treated as regards the levying of VAT in different ways. Thus, in the *French Tips* case, charges made by restaurants had to be treated in the same way for the purpose of VAT whether or not the restaurant could bring itself within the conditions for exemption from VAT on service charges. The Court of Justice has developed a variety of doctrines in VAT law to prevent the distortion of competition in this way. For further examples, see also *First National Bank of Chicago v* CCE Case C-172/96 [1999] QB 570, [33]; the *Muys* case (Case C-28/91 [1997] STC 665, per Advocate General Jacobs at [11] and [12]. However, the authorities do not support the proposition that the doctrine of neutrality entails the proposition that the Court should treat two separate supplies as a single supply because the suppliers are related parties and their supplies are linked….."

32. The Tribunal also referred to *Levob Verzekingen BV and OV Bank NV v Staatssecretaris van Financien ("Levob"*) (Case C-41/04) [2006] STC 766. This case shows that the approach to the issue whether there is one supply shown in *CPP* is not restricted to the narrow question of whether one supply is ancillary to another. It must be remembered that the case concerned supplies by a single supplier. Everything which was said by the Advocate-General and by the Court of Justice was said against that background.

33. We must also mention the case of *Ministero dell'Economia e delle Finanze v Part Service Srl* (Case C-425/06, [2008] STC 3182) ("*Part Service*"). Mr Gammie referred us, as he did the Tribunal, in particular to paragraphs 46 to 54. It is to be noted, as the Tribunal pointed out, that these paragraphs appear in the section of the Judgment dealing with abusive practice.

Submissions for HMRC on the single supply issue

34. Mr Gammie accepted that, having regard solely to the contractual documents, LME agreed to grant a lease of a holiday home plot and CBL agreed to build a holiday home on that plot. However, it was clear, he submitted, from *Customs and Excise Commissioners v Reed Personnel Services Ltd* [1995] STC 588 that contractual arrangements under domestic law are not determinative of the nature of the VAT supply particularly where three parties are involved. That proposition was common ground as it had been in *Telewest*.

35. He said that the Tribunal had, on the evidence, made a finding that there was a supply of a holiday home but, having done so, they erred in law in deciding that based on *Telewest* it was not possible to get over the hurdle of the contractual arrangements. It was necessary to stand back and look at the real nature of the supply. As to the finding in relation to this supply, he referred to the last sentence of paragraph 15(a) of the Decision – the customer "agreed to purchase a holiday home but it is **treated** as two transactions" [our emphasis]. He also referred to paragraph 128, appearing in that part of the Decision dealing with abusive practice, where the Tribunal had concluded that the

supply "being made to the customer is a holiday home. It must be remembered that VAT is a tax on supplies not on contracts."

36. Mr Gammie accepted that the customer was not legally bound to use CBL and that if the contract for the lease of a plot was not signed within 28 days the deposit was forfeit. He also accepted that, in relation to plots sold to customers before any construction work, there was no formal contractual relationship between LME and CBL for construction services.

37. Mr Gammie submitted that the test was whether, looking at all the circumstances objectively, what was supplied was a single indivisible economic supply which it would be artificial to split, see *Levob* at [22]. If all the supplies had been by LME it would be artificial to split them so that there would be a single supply; it made no difference where there was a captive builder, CBL, which customers routinely used to carry out the construction works. He said that all the relevant case law had been cited in *Telewest* but that none precisely answered the point here; *Telewest* was not a single economic supply case in the *Levob* sense. Here the combination of land and building services resulted in the holiday home.

38. Mr Gammie reminded us that *Part Service* had been decided by the Court of Justice since *Telewest*. In *Part Service* the leasing of a car had been split into three elements each of which was supplied by a separate person under a separate contract without an overarching contract; the *Levob* test of whether

objectively there was a single indivisible economic supply and the abuse analysis resulting in a single indivisible supply were, he said, close together. The answers by the Court happened to be framed in the context of abuse because of the way in which the questions by the referring Court were framed. He said that there was no current direct authority on whether there can be a single supply in the absence of abuse where objectively there is a single indivisible economic supply but two contracting suppliers.

39. Mr Gammie said that if there was not a single supply by LME then there was a supply jointly by LME and CBL to the customer. He agreed, however, that there was no joint and several liability under the contracts and that there had been no direction for LME and CBL to be treated as a single taxable person. He agreed that the assessment on CBL had been on the basis of the building services element and was the same as the assessment on LME. There are, he said – and we can agree with that – no clear answers to the issues of apportionment which would arise if the joint supply analysis were correct. This aspect of the case was not argued in submissions to us by either side.

40. There is a separate procedural point concerning CBL which we will come to at the end of this decision.

Submissions for Appellant on the single supply issue

41. Mr Peacock said that LME owned the land and supplied the lease at the outset. CBL provided the building services and was paid in stages over 18

months. There were reciprocal relationships between LME and customers in relation to the land and between CBL and its customers in relation to building services. There had been no suggestion that there was a sham. Although two separate elements could in some cases be treated as one supply where there was a single supplier (see *CPP* and *Levob*), there was no example of those principles applying to treat what would otherwise be two supplies by two suppliers as a single supply. The decision in *Telewest*, which is binding on the Upper Tribunal, is an insuperable hurdle for this element of HMRC's case. The Court of Appeal had even refused to make a reference to the Court of Justice: see Arden LJ at [91].

42. Mr Peacock said that HMRC were seeking to sidestep *Telewest* by contending that CBL supplied LME rather than the customers. There was no authority for recategorising a supply in this way in the absence of abuse. If this was legitimate it did not mean that there was a single indivisible supply to the customer by LME which had already supplied the land. The Tribunal found at paragraph 71 ("It is correct to say, as in the *Telewest* case, there are two suppliers and two supplies. It is not possible, given the legal and commercial relationship, to say that there is a single conflated supply by LME and CBL to the customer") and at paragraph 73 ("The legal relationship between LME, CBL respectively and the customer shows separate reciprocal supplies. The transactions are independent.") that there were separate supplies. Even if LME had contracted for land and building in a single contract, he submitted that there would be separate supplies and separate times of supply.

Conclusions on single supply issue

43. In our judgment, apart from any abuse or sham, it is not possible to combine supplies by two suppliers under two contracts so as to result in one supply for VAT purposes. The issue was considered extensively in the judgment of Arden LJ in *Telewest*. Given that the Court of Appeal itself declined to refer any question for a preliminary ruling, we do not consider that we could properly refer any question ourselves unless the case-law of the Court of Justice since the decision in *Telewest* gives rise to real doubt about the correctness of the decision of the Court of Appeal. In the absence of such doubt, we consider that *Telewest* provides a conclusive answer against HMRC's contentions.

44. We do not consider that subsequent case-law has made the position doubtful. In our judgment the decision of the Court of Justice in *Part Service* provides no basis for reconsideration of the decision in *Telewest*. Although that case did concern separate supplies by separate suppliers, and although reference was appropriately made to *CPP* and *Levob*, we do not read the Judgment as extending in any way the jurisprudence apart from abuse. It is to be noted that at [53] in *Part Service* the Court of Justice referred to a single supply by the taxable person to the customer rather than to a possible single supply by two taxable persons. The ruling of the Court of Justice was directed at abuse. If it had intended its words to be taken as extending the principles discussed in *CPP* and *Levob* so as to enable, in an appropriate case, two supplies by

separate suppliers to be treated as a single supply, we would have expected them to say so, especially in the light of the need for some guidance about how the value of the supply would then be apportioned between the two separate suppliers. The Court of Justice regularly reframes questions referred. If the Court had considered that there was a relevant possibility that there were on general principles single supplies albeit by separate taxable persons under separate contracts, we are confident that the Court would have said so before going on to consider the question of abusive practice.

45. We do not gain any further assistance either from *Don Bosco Onroerend Goed BV v Staatssecretaris van Financiën* Case C-461/08, [2010] STC 4760.

46. In our judgment, the correct treatment for VAT purposes, absent abuse, is that there are separate taxable supplies by LME, of leases of building plots, and by CBL, of building services. We reject HMRC's alternative formulations whichever basis is relied on. These are (i) a straightforward single supply of completed holiday homes by LME to customers, (ii) a supply of building services by CBL to LME with a supply by LME of completed holiday homes to the customers, (iii) a joint supply by LME and CBL of holiday homes to customers and (iv) a supply by LME of completed holiday homes to customers by reference to some economic reality different from the apparent contractual arrangements. We consider that the decision in *Telewest* (with which we would not want to disagree even if it were open to us to do so) leads us inevitably to the conclusion which we have reached.

47. The result is that the cross-appeal by HMRC fails and the appeal turns on the abusive practice issue alone but remembering that this falls to be decided on the basis that the contracts were genuine and not a sham.

The abuse issue

48. In *Halifax*, the Court of Justice re-stated at [55] to [56] some well-known fundamental aspects of the concepts of taxable persons and economic activity and considered also the nature of a supply of goods or services which defined taxable transactions under the Sixth Directive:

> "55. As the Court held in para 26 of its judgment in *EC Commission v Greece* (Case C-260/98) [2000] ECR I-6537, an analysis of the definitions of taxable person and economic activities shows that the scope of the term economic activities is very wide, and that the term is objective in character, in the sense that the activity is considered per se and without regard to its purpose or results (see also *EC Commission v Netherlands* (Case 235/85) [1987] ECR 1471, para 8, and, to that effect, in particular *Rompelman v Minister van Financiën* (Case 268/83) [1985] ECR 655, para 19, and *Zita Modes Sàrl v Administration de l'Enregistrment et des Domaines* (Case C-497/01) [2005] STC 1059, [2003] ECR I-14393, para 38).
>
> 56. That analysis and that of the terms 'supply of goods' and 'supply of services' show that those terms, which define taxable transactions under the Sixth Directive, are all objective in nature and apply without regard to the purpose or results of the transactions concerned (see, to that effect, *Optigen Ltd v Customs and Excise Comrs* (Joined cases C-354/03, C-355/03 and C-484/03) [2006] STC 419, [2006] 2 WLR 456, para 44)."

49. There can be no doubt that, in the present case, both LME and CBL made supplies and carried on economic activities.

50. The Court went on to consider abusive practice at [67] to [86]. Community law cannot be relied on for abusive or fraudulent ends. The application of Community legislation cannot be extended to cover abusive practices by economic operators

> "that is to say transactions carried out not in the context of normal commercial operations, but solely for the purpose of wrongfully obtaining advantages provided for by Community law….." (see at [69])

51. The Court added that this principle applies to VAT. Preventing possible tax evasion, avoidance and abuse is an objective of the Sixth Directive. But Community legislation must be certain and its application foreseeable, a requirement applying all the more strictly in the case of rules liable to entail fiscal consequences. Moreover, a trader is free to choose to structure his business so as to limit his tax liability. His choice between exempt transactions and taxable transactions may be based on factors, including tax considerations relating to the VAT system; the Sixth Directive does not require him to choose the transaction which involves paying the highest amount of VAT.

52. The Court then stated the following principles in relation to abusive practice at paragraphs 74 to 76, 80, 81 and 86:

> "74. In view of the foregoing considerations, it would appear that, in the sphere of VAT, an abusive practice can be found to exist only if, first, the transactions concerned, notwithstanding formal application of the conditions laid down by the relevant provisions of the Sixth Directive and the national legislation transposing it, result in the

accrual of a tax advantage the grant of which would be contrary to the purpose of those provisions.

75. Secondly, 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. As the Advocate General observed in para 89 of his opinion, the prohibition of abuse is not relevant where the economic activity carried out may have some explanation other than the mere attainment of tax advantages.

76. It is for the national court to verify in accordance with the rules of evidence of national law, provided that the effectiveness of Community law is not undermined, whether action constituting such an abusive practice has taken place in the case before it: see *Eichsfelder Schlachtbetrieb GmbH v Hauptzollamt Hamburg-Jonas* (Case C-515/03) [2005] All ER (D) 306, [40].

……..

80. To allow taxable persons to deduct all input VAT even though, in the context of their normal commercial operations, no transactions conforming with the deduction rules of the Sixth Directive or of the national legislation transposing it would have enabled them to deduct such VAT, or would have allowed them to deduct only a part, would be contrary to the principle of fiscal neutrality and, therefore, contrary to the purpose of those rules.

81. As regards the second element, whereby the transactions concerned must essentially seek to obtain a tax advantage, it must be borne in mind that it is the responsibility of the national court to determine the real substance and significance of the transactions concerned. In so doing, it may take account of the purely artificial nature of those transactions and the links of a legal, economic and/or personal nature between the operators involved in the scheme for reduction of the tax burden: see, to that effect, *Emsland Stärke GmbH v Hauptzollamt Hamburg-Jonas* (Case C-110/99) [2000] ECR 1-11569, [58].

……..

86. For it to be found that an abusive practice exists, it is necessary, first, that 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 a 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."

53. To understand the endorsement of what the Advocate General had said, we find it helpful to set out paragraph 89 of his opinion:

> "89. The prohibition of abuse, as a principle of interpretation, is no longer relevant where the economic activity carried out may have some explanation other than the mere attainment of tax advantages against tax authorities. In such circumstances, to interpret a legal provision as not conferring such an advantage on the basis of an unwritten general principle would grant an excessively broad discretion to tax authorities in deciding which of the purposes of a given transaction ought to be considered predominant. It would introduce a high degree of uncertainty regarding legitimate choices made by economic operators and would affect economic activities which clearly deserve protection, provided that they are, at least to some extent, accounted for by ordinary business aims."

54. We need to say a little more about what is meant by "essential aim" in this context. The use of the word "mere" in paragraph 75 of the Judgment in *Halifax* suggests that the test is whether attainment of a tax advantage is the sole aim of the transaction. But the use of the word "essential" in the same paragraph suggests something different; and that is the word used in paragraph 86. Two later authorities have looked at this. The first is *Part Service* which refers back to paragraphs 74 and 75 of *Halifax*. The court concluded that "sole" does not mean sole at all; but instead of repeating the use of the word "essential" it referred to "the principal aim" or "principal purpose" of the transaction.

55. Further, the ECJ has more recently put the test as "sole" purpose: see Case 162/07 *Ampliscientifica srl v Ministero dell'Economia a delle Finanze* [2008] ER I-4109, a decision from a differently constituted chamber of the ECJ on 22

May 2008 a few weeks after *Part Service*: the prohibition is on "wholly artificial arrangements which do not reflect economic reality and are set up with the sole aim of obtaining a tax advantage".

56. Mr Peacock said that we do not need to resolve which of these formulations is to be preferred provided that it is recognised (as we accept it must be) that there is a high threshold.

57. There was some discussion of this point by the Court of Appeal, in which Lord Neuberger gave the only reasoned judgment, in *WHA Ltd v Customs & Excise Commissioners* [2007] EWCA Civ 728, [2007] STC 1694 but Lord Neuberger was prepared to proceed on the basis of the assumption that the "sole purpose" test was correct.

58. The decision in *WHA* is interesting in the way Lord Neuberger deals with a number of general points which arise in the application of *Halifax*.

59. In relation to that decision, we start by pointing out what Lord Neuberger said about the purpose of the VAT provisions with which he was concerned (and with which we are concerned):

> "15 The purposes of the VAT provisions with which we are concerned in the present case is, as in *Halifax* , to be found primarily by reference to the provisions of the Sixth Directive , Directive 77/388 (although the law has subsequently been consolidated into the Council Directive 2006/112 EC ("the Principal Directive"). Those purposes have been

> discussed by the ECJ in a number of earlier decisions including *Elida Gibbs Ltd v Customs and Excise Commissioners* (C-317/94) [1996] E.C.R. I-5339; [1996] STC 1387. In [19] of its judgment in that case, the court said that the 'basic principle of the VAT system is that it is intended to tax only the final consumer'. In the following paragraph, the court confirmed that the system was "based on neutrality", which means that "within each country similar goods should bear the same tax burden whatever the length of the production and distribution chain". In [22], the court stated that "taxable persons [other than the final consumer do not] bear the burden of VAT", but "collect the tax on behalf of the tax authorities and account for it to them". Thus, as explained in [23] of *Elida Gibb*s, VAT is, in general, charged on the consumers in each transaction in the chain, and is recoverable by taxable consumers in the chain, provided they make taxable supplies, so that the tax is ultimately borne by the final consumer."

We shall refer in this decision to the Sixth Directive and the Principal Directive together as "the Directive".

60. Next it can be seen, following *Halifax*, that the purpose of the transaction has to be judged objectively not subjectively. That is to say, it has to be judged by reference to the terms of the scheme and the commercial realities not by reference to what the parties concerned say their intentions were (or what their subjective intention is found to have been). Whether evidence of subjective intention is therefore altogether inadmissible is not, however, entirely clear.

61. It is to be noted that Lord Neuberger envisages a "scheme"; in that context, when considering the purpose of the scheme, the aspects of it which were artificial had to be addressed. A scheme might be abusive whilst having a genuine underlying commercial purpose. After all, as he noted at [29] the Scheme in that case had the purpose of enabling the insurer's liabilities to be performed and reinsured; and thus it could be contended that tax avoidance

cannot be said to be the sole or even the main purposes of the Scheme viewed as a whole. But in answer to that he said this:

> "…..However, as I see it, when considering the purpose of the Scheme for present purposes, one must primarily address the aspects of the Scheme which are artificial. Otherwise, many schemes, however abusive, would succeed: indeed, on the basis of this contention, the decision in *Halifax* might very well have gone the other way. It seems to me that I am supported in this opinion by the reference in [80] of the judgment in Halifax to 'normal commercial operations', and the requirement in the following paragraph that, where abuse is established, the national court must 'determine the real substance and significance of the transactions concerned'. This plainly seems to envisage that a scheme may be abusive while having a genuine underlying commercial purpose."

62. So it can be seen that a genuine need for an end result (a building in *Halifax* or fulfilment of NIG's liabilities in *WHA* and its need for reinsurance) are not enough to avoid the first limb. It is the structure for achieving that end which is important. The focus is on identifying artificial elements which can be said to produce a result contrary to the purposes of the then Sixth Directive.

63. It can also be seen that Lord Neuberger's approach suggests that there is a need to effect a comparison in determining whether the requirement of fiscal neutrality has been breached; the comparison is between the scheme in question, whose artificial elements are to be identified, on the one hand, and normal commercial operations on the other. It seems to us that Lord Neuberger was addressing "normal commercial operations" in the context of the first limb as much as the second limb of *Halifax* and was addressing the operations of a trader carrying out the same sort of business, although it is not

necessary to carry out an examination of the typical business activity of the particular trader concerned. On the facts of *WHA*, it was possible without much difficulty to identify what the consequences of that requirement of fiscal neutrality were (as to which see Lord Neuberger's judgment at [16]). Thus in "the normal commercial operations" of an insurer and claims handler, there would be no question of the input tax concerned being recoverable. In the present case, it seems to us that it is the search for the "normal commercial operations" by which to judge the transactions involved which gives rise to real issues which we have to resolve.

64. However, we need to refer next to the Opinion of Advocate General Mazak in Case C-103/09 *HMRC v Weald Leasing Ltd* delivered on 26 October 2010, after the hearing of this appeal. In that case, the Advocate General considered the references in *Halifax* to "normal commercial operations", discussing its meaning in the section of his Opinion from paragraphs 29 to 33. The second question asked by the referring court in *Weald Leasing* was whether it is an abusive practice for an exempt or partly exempt trader to engage in the leasing of assets even though in the context of its "normal commercial operations" it does not do so.

65. We have no reason to question his conclusion that "normal commercial operations" do not require an examination of the "typical" business activity of a particular trade and that that concept in the context of VAT is unrelated to the operations a particular taxpayer habitually engages in.

66. We do, however, have difficulty with the conclusion that an assessment of whether a transaction is carried out in the context of "normal commercial operations" refers to the second limb of *Halifax* if, in stating that conclusion, the Advocate General is also expressing the view that the concept is not relevant to the first limb. We will return to this aspect briefly at paragraph 87 below.

67. There is one other point which arises out of *WHA* which we need to mention. It is the point that the ECJ in *Halifax* accepted that a taxpayer who has alternative courses open to him is entitled to choose that which minimises his liability to VAT. Lord Neuberger dealt with the point at [38]. We note in passing that although he addressed the argument as one aimed at defeating HMRC's case on abuse once the requirements of the two limbs of *Halifax* had been satisfied, it can be seen also as an argument that the requirements of one or other (or both) of the limbs is not satisfied in the first place. Perhaps nothing turns on that difference of approach. As he recognised, the four questions which he asked do, in any case, overlap.

68. But what is of significance is that this escape from a finding of abuse is circumscribed. No doubt in a case where there are different options which can both be seen as grounded in commercial reality or, to put the point in different words, where "normal commercial operations" can be carried out in different ways to achieve the same result, it is open to a trader to adopt the option which

is the more beneficial to him in terms of VAT. But this is not a licence to adopt any transactions which the trader might choose when they involve artificiality, being contrived to bring a VAT benefit.

69. We have already described in brief general terms the relevant facts in *Part Service* and have looked at the case in the context of the first question referred to the Court of Justice. There was a second question, however, which was directed at the first limb of *Halifax*. It sought a ruling whether there could be an abuse of rights where

> "contracts for leasing arrangements, financing, insurance and intermediation contracts are concluded separately with the effect that only the consideration paid in respect of the grant of the right to use the goods is subject to VAT, whereas a single contract of leasing in accordance with the practice and interpretation of national case-law would include the financing and would therefore make the whole of the consideration subject to VAT".

70. It is relevant to note that this question was asked in the factual circumstances set out in paragraph 8*ff* of the judgment, and in particular paragraphs 11 and 13. These demonstrate the concern about artificiality in the arrangements reflected in the Italian tax office's conclusion, set out at paragraph 17, that there was in fact a single tri-partite contract with an artificial division of the leasing arrangement to reduce the taxable amount. The taxpayer appealed against the liability imposed by the authorities, relying on the fact that the business model had been chosen for a number of specified commercial purposes as set out in paragraph 19. The taxpayer succeeded up the line of

Italian tribunals until the Corte Suprema di Cassazione referred the questions to the Court of Justice. It is to be noted that the Italian court referred the matter to the Court of Justice because it considered that the division of contracts had the effect of reducing the VAT burden to a lesser amount "than that resulting from an ordinary leasing contract": see paragraph 25. It therefore appears that there must have been, in Italy, some objectively identifiable normal commercial operations under which there would be found a single supply of the different supplies which existed on the facts of *Part Service.* Accordingly, the reference was made (see paragraph 31) to raise the question whether "the abuse of rights bar operates where the economic reasons, other than the accrual of a tax advantage, are wholly marginal or insignificant, and not a possible alternative explanation".

71. In answering this question, the Court of Justice (at paragraphs 48 to 53) referred to *Levob* and *CPP* as examples of situations where separate transactions were to be regarded a single supply. This was so, for example, in the case of ancillary services. In that context, a service is to be seen as ancillary if it does not constitute for customers an aim in itself but a means of better enjoying the principal service supplied. The same result obtains (*ie* a single supply) where two or more elements or acts supplied by the taxable person to the customer are so closely linked that they form, objectively, a single indivisible economic supply.

72. That all makes perfectly good sense in the context of a single supplier. But there is more difficulty where there are separate suppliers. Thus if A provides a main service X and an ancillary service Y, it may be that there is a single supply of X and Y together. But if X and Y are supplied by different suppliers which are wholly unconnected, it would be difficult to see how there could be a single supply even applying the *Halifax* principle. Now, that result (no single supply) might be reached by saying that Y is not ancillary to X at all where there are separate suppliers, although we do not see why that should necessarily be so. The more likely reason is that there are separate supplies (in fact and for VAT) and that the abuse principle does not apply; the first limb of *Halifax* simply does not apply at all because there is nothing contrary to the purposes of the Principal Directive in unconnected suppliers making separate supplies, albeit one, Y, cannot be made without the other, X. To complete the review of *Part Service,* we need to quote certain passages from the Judgment:

> "54 It is for the national court to assess if, the contractual structure of the transactions notwithstanding, the evidence put before the court discloses characteristics of a single transaction.
>
> 55. In that context, it may find it necessary to extend its analysis by seeking evidence of indications of the existence of abusive practice, which is the concept with which the question referred is concerned."

73. Then, after identifying a number of characteristics of the transactions, the Court said this in relation to their statement of the first limb of *Halifax*:

> "59. As regards the first criterion, [the national] court can take into account that the anticipated result is the accrual of a tax advantage linked to the exemption, pursuant to Article 13B(a)

and (d) of the Sixth Directive, of the services entrusted to co-contracting company of the leasing company.

60. That result would appear to be contrary to the objective of Article 11A(1) of the Sixth Directive, namely the taxation of everything which constitutes consideration received or to be received from the customer.

61. Since the leasing of vehicles under leasing contracts constitutes a supply of services…….., such a transaction is normally subject to VAT, for which the taxable amount is determined in accordance with Article 11A(1)…."

74. Paragraphs 59 and 60 might be seen as lending support to the view that it is a proper approach to apply national law to establish the "real" nature of the transactions (much as one would in a conventional tax-avoidance scheme in accordance with purely domestic law). But it must be recognised that the Court was answering the question referred in the context of an identified normal commercial arrangement namely "a single contract of leasing [which] in accordance with the practice and interpretation of national case-law would include the financing".

75. There is one other point we make before moving on from our discussion of *Halifax*. The abuse principle is one of European Union law. It is not to be treated as if it had precisely the same impact as domestic rules developed in the field of direct taxation (such as the line of cases starting with *Ramsay v IRC* [1982] AC 300). Nonetheless, the first limb of *Halifax* is concerned with abuse which results in a tax advantage "contrary to the purposes of those provisions", that is to say the relevant provisions of the Sixth Directive (at that time) and the national legislation transposing it. Since "neutrality" is directed at ensuring that within each country similar goods (or services) should bear the

same tax burden, it is appropriate, as *Halifax* states, to look at national legislation as well as the Sixth Directive in order to understand the purpose which is to be respected.

76. The abuse issue was addressed in paragraphs 82 to 139 of the Tribunal's decision. Mr Peacock was heavily critical of the Decision in general and of this part of it in particular. He did not pull any punches in saying that the Decision

a. contains a large number of internally contradictory findings of fact;

b. contains a large number of instances where the Tribunal has simply failed to find facts of the utmost significance;

c. frequently and unlawfully rejects the unchallenged evidence of witnesses;

d. is often simply incoherent; and

e. makes findings despite there being absolutely no evidence in support.

77. Many of his criticisms are not without some foundation. It is not easy to identify the findings of fact. There is no summary of the evidence nor any statement of the findings of fact made. The findings have to be extracted from the discussion and conclusions. Sometimes it is not easy to say whether the Tribunal was reciting evidence or was making a finding of fact. We recognise that the variety and complexity of the issues rendered it a difficult decision to prepare but we have to say that we are left, in some respects, with no clear picture of what the Tribunal actually did decide or of their reasoning in reaching the conclusions which they did.

78. We do not want to set out in the body of this Decision lengthy passages from the Decision. It is, nonetheless, necessary to refer to key paragraphs. We therefore set out, in the Annex to this Decision, some paragraphs from the part of the Decision which deals with abuse to which the reader of this decision might find it helpful to refer without the need go to the Decision itself which can be found on the Tax Chamber website, the link to which is: http://www.financeandtaxtribunals.gov.uk/Aspx/view.aspx?id=4374.

79. The structure of the Decision is, broadly, as follows. In paragraphs 84 to 93, the Tribunal make some general observations about the purpose of the Directive and the nature of abuse. Then the Tribunal consider the first limb of *Halifax* at paragraphs 94 to 105 and consider the second limb starting at paragraph 106.

The abuse issue: the first limb of *Halifax*

80. The question under the first limb of *Halifax* is whether the transactions in question result in a VAT advantage to the trader which is contrary to the purposes of the Directive or the VATA. The Tribunal spent some time identifying at least some of those purposes at paragraphs 89 to 93 of the Decision. We do not disagree with much of what they say. It is perhaps a mere quibble to question whether the primary objective, rather than an objective, is the objective identified in paragraph 90 and whether "The" rather than "A" clear objective is as stated in paragraph 93. But the suggestion that a

taxable person carrying out the same transaction can be expected to be treated equally with a competitor ought to be qualified by a recognition that they must be proper comparators. A similar point arises in relation to the "similar transactions" mentioned in paragraph 91, giving rise to the question of what the proper comparator is for an actual transaction, a matter of some importance to which we will return.

81. One of HMRC's original reasons for asserting that the first limb of *Halifax* was met appears from their letter of assessment. They stated, no doubt correctly, that zero-rating can only be established for clearly defined social reasons, referring to *Talacre Beach Caravan Sales Ltd v Customs and Excise Commissioners* (Case C-251/05) [2006] STC 1671 ("*Talacre Beach*"). They stated that there were no clearly defined social reasons for the supply of a holiday home to be zero-rated so, if LME and CBL were to succeed in making zero-rated supplies of holiday homes, then the purposes of the VAT Directives and domestic legislation intended to implement them would be defeated. It is not now contended (and was not in the end contended before the Tribunal) by HMRC that the homes in the present case cannot fulfil the "clearly defined social reasons" requirement of the Directive.

82. Mr Peacock pointed out that the UK has zero-rated construction services in relation to dwellings (that is to say where a supply is made in the course of construction of a building designed as a dwelling). This applies as much to holiday homes as it does to any other dwelling; and it applies even if the

holiday home is subject to a restriction preventing residence throughout the year.

83. In any case, LME's and CBL's position is that there is no supply by CBL (or anyone else for that matter) of a holiday home; there is a supply of land and a supply of construction services by different suppliers and what is zero rated is the supply of the construction services. The UK has, we note, deliberately chosen to zero-rate supplies of construction services in the course of construction of a dwelling: it did not have to do so and could, had it wished, have excluded such supplies in relation to holiday homes. It is, unsurprisingly, not suggested before us by HMRC that zero rating of such construction services is contrary to the purpose of the Directive.

84. HMRC therefore needs to find another reason apart from social policy for saying that the result for which LME contends in the present case is contrary to the purposes of the Directive and the VATA. The reasons given to the Tribunal and to us are, in essence these:

a. that the zero rating of the construction services provided by CBL would distort competition; and

b. that the zero-rating of part of the total consideration paid for the completed building would result in not all of the "supply" being taxed.

85. Mr Gammie, in a succinct statement of HMRC's position, said that it is self-evident that the arrangements that LME and CBL devised produced a non-

uniform VAT treatment comparing a customer who (as HMRC would have it) bought a holiday home from LME/CBL and a customer who bought a holiday home from a developer who straightforwardly sold a holiday home. Thus he seeks to support the Tribunal when they said that, if part of the consideration paid for the holiday home is VAT free, this would be against the objective of the Directive in guaranteeing uniformity in VAT treatment between similar transactions.

86. It is inherent in that approach that a comparison is to be effected. On the one hand, it is necessary to identify how a trader of the type in question would structure his business and the transactions which would normally take place and to examine the resulting VAT position of that trader. That enables one to identify in context, rather than in abstract, the purposes of the Directive and the VATA transposing it. On the other hand, one looks at the transactions which in fact took place. If those give a more favourable VAT outcome, they can be seen as contrary to those purposes. This is subject to the right of a trader to chose the more favourable option provided that there is no abuse.

87. We do not consider that there is any difference between the transactions, applying this approach, which would normally take place and the "normal commercial operations" referred to in *Halifax*. However, if "normal commercial operations" are identified only for the purposes of the second limb of *Halifax* as Advocate General Mazak appears to be saying in his Opinion in *Weald Leasing Ltd*, we conclude that, on the facts of the present case, it is

necessary to utilise the same or an almost identical concept in order to establish whether the purposes of the Directive and the VATA were being abused. Accordingly, we will continue to use the phrase "normal commercial operations" in relation to the first limb.

88. This need for a comparison is entirely consonant with what Mr Peacock submitted. He is surely right when he says that the application of the principle in *Halifax* will not arise at all unless arrangements are entered into which have the effect that less VAT is payable than might have been the case if other arrangements were entered into. Those different arrangements must, of course, have broadly the same results as each other. The crucial question then is what is the proper comparator for the transactions entered into in the present case. We come to that later.

89. As we understand it, the distortion of competition argument is directed at this comparison and is not intended to go any further. But in case it is intended to go any further, we would suggest that the distortion of competition argument is to that extent something of a bootstraps argument. If the purposes of the Directive and the VATA are being subverted, there is no need to rely on the distortion of competition argument to the extent that it goes further than we have identified. In contrast, if those purposes are not being subverted, it is not easy to see how one can arrive at the conclusions that there is abusive conduct within the *Halifax* principle on the basis of a distortion of competition. To the extent that a distortion of competition is not, of itself, a subversion of the

purposes of the Directive and the VATA, it is outside *Halifax*. Such distortion may give rise to remedies as a matter of competition law, but a change in the VAT consequences of the actual transactions undertaken is not, in our view, one of those remedies.

90. Mr Peacock then seeks to meet Mr Gammie's point by conducting a search for the appropriate comparator. He poses four transactions:

a. LME supplies the land and an unrelated company builds the holiday home.
b. An unrelated company supplies the land and CBL builds the holiday home.
c. LME supplies the land and CBL builds the holiday home ("the self-build model").
d. A company supplies a completed holiday home with its site ("the development model")

91. The VAT consequences of transactions a., b. and d. are, of course, clear. Under transactions a. and b., there are separate supplies: a standard rated supply of land and zero rated supply of construction services. It cannot sensibly be suggested that these results are contrary to some purpose of the Directive or the VATA. It follows that the supply of a holiday home – in the sense of the construction of a building on land already owned – is a zero-rated supply. It might be thought odd that the VATA does not exclude from zero rating construction services provided in relation to those buildings referred to in Note (13) to Group 5. But that is not what the legislation has done. It is

impossible to contend, therefore, that zero rating of the construction services provided by CBL viewed in isolation would be contrary to the purposes of the Directive or the VATA. If the first limb is satisfied, it must therefore be because the transactions in the present case are to be equated with a single supply of a completed holiday home (and thus not zero rated because of Note 13).

92. Returning to transactions a. to d. and apart from application of the principle in *Halifax,* transaction c. would fall to be treated in the same way as transactions a. and b. In order to invoke that principle, HMRC have to rely on the unique relationship between LME and CBL as requiring a departure from that treatment; at least, we can see no other grounds on which HMRC could seek to invoke that principle. The uniqueness is to be found in the ownership structure and the consequent commercial arrangements put in place.

93. Mr Peackock said that there is no relevant distinction between transactions a., b. and c. whereas there is a significant and real distinction between transactions a. and b., on the one hand, and transaction d. on the other. Transaction d. does not present a proper comparison. This is essentially for two reasons.

a. The first is that in transaction d., the supplier takes the building risk, the financial risk and the cash-flow cost with the customer buying the end product without the building risk and typically paying on completion. In

contrast, in the other transactions, the supplier of the land takes no building risk and the customer pays the builder in stages.

b. The second is that a commercial developer selling completed homes is not a relevant comparator. It may be that if a large commercial developer which normally conducted its operations on the basis of sales of completed homes formed a subsidiary to provide construction services in a similar way to CBL an abusive practice would be established. But, so the argument goes, LME and CBL cannot, together, be equated with such a developer. Their entire *modus operandi* is different and their scale of operations is different.

94. Mr Peacock concluded that the proper comparison in the present case is between the transactions which actually took place and transactions under which land is sold to a customer who engages a builder other than the vendor to construct his holiday home.

95. In paragraph 98 of the Decision, the Tribunal identified HMRC's case based on distortion of competition: the zero-rating of the construction services means that not everything which is paid by the customer for the supply is properly taxed and "the Appellant should have to account for VAT on the amount that is paid for the holiday home, which is to say, the land and the construction services". The language used by the Tribunal in this paragraph to identify the argument is in danger, we fear, of leading them to assume that which has

to be decided. Thus reference is made to payment "for the supply"; if this means no more than "for the provision" that is acceptable, for it does not assume that there is only one supply for VAT purposes. But the use of the word "supply" causes concern that the Tribunal are already perceiving the provision of the land and the construction services as a single supply of a completed home. Further the use of the word "Appellant" in the singular is confusing. There were two appellants, LME and CBL, defined in paragraph 1 of the Decision as "the Appellants". Perhaps the Tribunal were intending to refer to LME; if so, it would have been better that they had done so. That would eliminate the danger of treating LME and CBL as if they were one entity so that the "supply" could be seen as single supply by that entity.

96. At paragraph 101 of the Decision, the Tribunal identified the comparable house building market "to see if an unfair advantage would arise to the Appellant when compared to other commercial developers in the holiday home market". There are several things to say about this paragraph.

a. The reference to an unfair advantage is not an accurate reflection of what the first limb of *Halifax* is about. There is, we think nothing "unfair" about a trader adopting a particular business model if it is open to any competitor to adopt precisely the same model although there might be unfairness if that model had adverse consequences for the competitor not suffered by the trader. Rather, the first limb is concerned with transactions

contrary to the statutory purposes in the sense explained in the judgment in *Halifax*.

b. The reasoning by which the Tribunal concluded that LME's business model created distortion of competition was in any case, according to Mr Peacock, unsound. They recognised that LME's model was "self-build", a point emphasised in paragraph 109. They then asserted that most commercial property developers would sell a completely built house; they would not separate the sale of the land from the building of the house. Consequently this was the market which the business model adopted by LME and CBL needed to be compared with. But this, he said, does not establish the proper comparator transactions which are (a) sale by landowner and (b) engagement by purchaser of a builder to construct his holiday home. So there is no distortion of competition at all.

c. As to the Tribunal's conclusion, we note that they gave no reasons for adopting the comparator which they did. There is, in any event, some ambiguity about the comparable market which they identify. Either it is the market where completed houses are sold, whether built by developers who are large or not; or it is the market in which large developers operate. There was no evidence, so far as we are aware, which would have justified a conclusion that developers which were not large normally conducted their business on the basis of sale of completed homes. And the evidence in relation to large developers was rather different from that which the Tribunal recorded (a matter we come to in a moment).

d. Even if they were right in identifying the model which they state was adopted by most commercial developers, they did not explain why it was not possible for LME to take advantage of the entitlement to choose the business model which it did as a way of minimising the VAT liability, an entitlement recognised in *Halifax* as explained in *WHA* at [38].

e. As to that last aspect, there are several points to note:

i. JMP's evidence was that he was commercially unable to pursue the development model because he was insufficiently funded. This is quite an important aspect which we deal with in the next main paragraph of this decision.

ii. JMP says that he decided to pursue the "self-build" model before he had taken any tax advice although HMRC do not accept that. It is not clear to us why they do not accept it. JMP's evidence to that effect was clear; and the fact that the Tribunal found it strange (see paragraph 111) that tax advice was not taken in structuring such a large transaction is not a finding that he did take advice before deciding on the "self-build" model. It is perfectly consistent with what JMP actually said in his witness statement that, had the advice been that the self-build model was a most inadvisable structure from a tax point of view, he would have investigated another model. HMRC say that JMP took tax advice in 1998: that may be so, but he had bought the site in February 1997 and his unchallenged evidence was that he had not taken tax advice at that stage and that he had decided on the "self-build" model. Not

much, if anything, turns on that, since the factors leading to the applicability of the first limb have to be assessed objectively. It does, however, lend support to the submission that the "self-build" model was adopted for commercial reasons.

iii. Mr Johnson is recorded as saying that large property development companies cannot separate the construction and land owning parts of their business. What he actually said in cross-examination was rather different. He gave evidence (which was not challenged) that there were companies (eg Keir for which he had worked) which would have one company owning the land and another carrying out construction. He stated that he was always concerned about risk being introduced into any land-owning company because it was not necessary to do so.

iv. He explained how large developers, such as Waites operate on a speculative basis. They build a sales home, they complete projects. They try to get purchasers during the course of construction, but it is a different and commercially speculative process. We should set out the following passage:

> "Q. [In the context of Waites] So even though you have separated the land and the building there, you do not have a situation where the plot is sold to an individual as a means of avoiding any risk?
> A. No, it is different – it is a different process because you are building predominantly on a speculative basis. So the whole idea at Lower Mill was to have the plots sold to the individual, as I understand, because of liquidity issues, and to keep the business moving, and for that individual to contract with a builder to build the house out. That obviously makes

sense. Unfortunately these PLC companies cannot operate on that basis.

Q. Yes, but there would no reason why Lower Mill Estate could not operate on the basis that it built the house and sold the plot?

A. There is a business case and a cashflow case.

Q. But that would be a perfectly sensible way of doing it, without doing it speculatively, as you put it?

A. Well, not that is ---- transfers risk back into ---- would transfer risk back into Lower Mill Estate. That was the whole idea to keep it totally separate. So I would not think that is a sensible approach."

v. We do not read that exchange as being accurately reflected in what the Tribunal recorded (either in paragraph 101 or anywhere else in the Decision). But that is not the entire point. This passage provides absolutely no support at all for the conclusion that a large property developer is in any way an appropriate comparator for LME and CBL. And yet, so far as we can see, there is nothing else in the Decision which is relied on by the Tribunal as justification for the comparison other than what a large developer, according to the mis-stated evidence of Mr Johnson, does. In any case, Mr Johnson said that developers do sometimes separate out their land-owning and development functions and can provide the land and building services separately. However, he says nothing (either here or elsewhere in his evidence and cross-examination) one way or the other about whether commercial developers build and sell holiday homes as a complete package.

vi. It is curious that the Tribunal said that adopting the "self-build" model would represent an advantage in terms of the cost of

construction. The cost of construction is the same under either model. Probably what the Tribunal meant was that the end cost to the customer would be larger. Certainly, the distortion identified and relied on in the last few lines of paragraph 101 is dependent on the view that in each case the supply is of a completed holiday home, as is shown by the reference to "The splitting of the contract in this way". But that is not the question in relation to the first limb of *Halifax*. The question is whether the transactions result in a tax advantage contrary to the purposes of the Directive and the VATA. The fact that one choice of business model results in less VAT being exigible than another does not of itself establish abuse. We are left with the impression that the Tribunal's conclusion is really no more than an assertion.

vii. We have not overlooked the fact that Lord Neuberger in *WHA* separated the questions (i) whether the Scheme in that case was contrary to the purposes of the Sixth Directive and (ii) whether the abuse argument should nonetheless fail (see [38] in particular). But he himself recognised at [13] that the answers may overlap to some extent. In that case, it was relatively straightforward to identify the normal commercial operations and to perceive what had been artificially introduced, leading to the *prima facie* conclusion that there was abuse: see [16]. It was equally straightforward for Lord Neuberger to reject the argument based on the availability of choice to the taxpayer. But he recognised, in

[28], that there may be cases where it is difficult to decide whether there is abuse or whether the course adopted is one which is properly open to the taxpayer. In a case where there is such difficulty, it is very difficult, as we see it, to separate the two questions: if a taxpayer has a permissible choice, it is not easy to see how making one choice rather than the other could ever be contrary to the purposes of the Directive.

viii. Further, one must be very careful indeed not to adopt a line of reasoning which goes (i) a scheme of transactions is adopted and implemented with a view to minimising tax (ii) that scheme results in less tax than another route to the same end result and (iii) therefore the first limb of *Halifax* is satisfied. Steps (i) and (ii) in the argument may (depending on the facts of the case) show that there is tax avoidance within the second limb of *Halifax*; but they do not of themselves establish satisfaction of the first limb, otherwise whenever a tax avoidance scheme is involved, the first limb would automatically be satisfied, a conclusion which is clearly <u>not</u> the law.

97. We return to JMP's evidence that he was commercially unable to pursue the development model because he was insufficiently funded. His evidence was that such a model is capital intensive (a) because it requires the builder to fund the entire cost of the build and (b) because all consideration from the sale is delayed until the house is sold. A self-build model (a) delivers consideration

for the land element when the land is leased and (b) delivers consideration for the build element in stages as the build progresses. JMP said that he did not have the capital to pursue any model other than a self-build model and nor could he raise it. The reality of the situation was that the self-build model was the only model open to him. HMRC do not accept this. But it was not challenged in cross-examination so far as we are aware and yet the Tribunal made no finding about this reason – a critically important reason according to Mr Peacock – about why JMP pursued the self-build model.

98. What HMRC say about this is that JMP considered various options for raising capital to fund the development of the site. Although the money from Mr. Ganzi (an investor in the project) was used for the land purchase and obtaining of planning permission, there was no legal obligation in the loan agreement to restrict the use of the money. That may be correct, but it does not address JMP's evidence. He decided on the self-build model in the light of the facts mentioned above. There is nothing before us to suggest that he had finance available (whether from Mr Ganzi or anyone else) to fund not only the purchase of the land and infrastructure works but also the construction of houses and the Tribunal made no finding to that effect. We consider that we should proceed on the basis that what JMP has said is correct and forms part of the factual matrix within which we must decide this appeal.

99. Mr Gammie adds this: how the development was being financed does not alter the Tribunal's conclusion that what was being supplied to purchasers were

holiday homes. If by "supplied" he means "provided", that may be so. But if by "supplied" he means "supplied for VAT purposes", JMP's evidence could be important since it will be material to the abuse argument. In that context, it is not easy to see how the normal commercial transactions of a developer such as LME can include transactions which would be commercially impossible, or even difficult, for that developer to effect and not easy to see how a commercial developer which adopts the development model can be seen as an appropriate comparator. Further, even if the development model was not impossible, the commercial position presented by JMP lends support to the argument that the self-build model was a permissible alternative course open to LME/CBL within paragraph 73 of *Halifax* and [37] of *WHA*.

100. Criticisms are made in relation to paragraphs 102 to 104 of the Decision similar to those made in relation to paragraph 101. Confidence is further shaken when the Tribunal refers in the opening of paragraph 105 to a reduction in the taxable amount when what is reduced is the amount of tax, the question being whether part of the taxable amount is zero-rated or not.

101. The conclusion expressed in paragraph 105 is dependent on what has gone before, in paragraphs 101 to 104. But, Mr Peacock rightly said, nowhere have the Tribunal addressed or answered the question why provision of the land by LME and provision of building services by CBL is contrary to the purposes of the Directive and the VATA.

102. Clearly there is nothing contrary to those purposes where a land-owner and an unrelated builder provide land and construction services and where each supply is treated separately for VAT purposes. What must therefore be identified, and what Mr Peacock said the Tribunal had failed to identify, is why the result in the present case (customer pays VAT on land supplied by LME but not on the construction services provided by CBL) is contrary to the purposes of the Directive.

103. Mr Gammie, unsurprisingly, adopts an entirely different analysis from Mr Peacock. He first identified the legal structure adopted by LME (or rather, we would say by JMP) involving the incorporation of CBL. That structure was straightforward and was as follows:

a. Tax and legal advisers acting for LME and CBL created a 'standard' documentation package that customers who wanted to acquire a holiday home would sign up to;
b. That standard package involved LME granting an agreement for lease of a particular plot to a customer and at the same time CBL agreeing to build the holiday home to one of the standard designs for which planning permission had been obtained and which had been chosen by the customer reflecting in part their chosen plot within the development;
c. CBL engaged subcontractors to build the holiday homes, which were paid for in stages by customers;

d. Because the development proceeded in phases around a network of small "villages", construction would sometimes have to begin on particular holiday homes before a purchaser had been found for the relevant plots.

104. That we think gives a description, sufficiently accurate for present purposes, of the process. But we note that there was no contractual obligation on a customer to use CBL in which context Mr Gammie observes in his skeleton argument that

> "the legal form of the contractual documentation was said to be supported by the 'possibility' (however faint) that something different to the standard package might be implemented. This is notwithstanding that in reality nothing different is ever shown to happen, everyone knows that nothing different is really envisaged or is ever likely to happen and no one involved in devising the arrangement intends that anything different will happen. In the present case there was no evidence that any customer used a builder other than CBL (paragraph 123 of the decision)."

105. Mr Gammie also relies on how the Tribunal described the sales process point by point a in paragraph 15(a) of the Decision:

> "The on-site sale operations were run by LME. Customers coming to the on-site sale shop would make enquiries of plots of land and would be informed, at the same time, of the constructions services offered by CBL. The customer therefore agreed to purchase a holiday home but it is treated as two transactions – the sale of land and the purchase of construction services."

106. It is not clear to us why the Tribunal considered that the third sentence follows from the first and second. Even accepting that all purchasers did sign up to

use CBL and did so at the same time as they purchased the plot, the conclusion is inaccurate. We cannot read the third sentence as a finding of fact that customers agreed to buy completed holiday homes although whether that conclusion can be found elsewhere in the Decision is another matter. We can accept the proposition that, as a result of the two contracts entered into, purchasers would end up with a holiday home. But the same could be said if LME had arranged with a wholly independent builder to operate in the same way as CBL, or perhaps had even given a choice of two independent builders or a choice of CBL and one independent builder. In such a case, the purchaser would end up (assuming the contracts were complied with) with a holiday home. But it would be clear that such purchasers had not agreed "to buy completed holiday homes"; they would have agreed to buy plots of land and to have the independent builder erect houses. We read the Tribunal as saying no more than that, as a result of the contracts he entered into, a purchaser would obtain a plot of land with a completed house on it.

107. However, the Tribunal went into the process in more detail in paragraphs 120 to 129 of the Decision. They referred at paragraph 125 to the promotional video which, from the quote from JMP, certainly gives the impression that the customer is buying a completed house ("we sell you a house and a piece of land…").

108. Reliance was also placed by Mr Gammie on paragraph 128. However, this finding, if it is properly to be viewed as a conclusion about the nature of the

VAT supply, is made in the context of the second limb of *Halifax*. By this stage of the Decision, the Tribunal had already decided (in paragraphs 101 to 105) that the first limb of *Halifax* was satisfied. The analysis is thus in the context of whether the essential/principal aim of the arrangements was to obtain a tax advantage. It is, we accept, not seriously open to dispute that the arrangements entered into by LME and CBL with purchasers did achieve a tax advantage as compared with the development model (supply by a single developer of a completed holiday home). But that does not, by itself, provide an answer to the question whether the case is even within the second limb of *Halifax*, let alone within the first limb, since what has to be shown is that the essential or principal aim of the transactions was to achieve a tax advantage.

109. In any case, we do not read the conclusion as a free-standing finding of fact. Rather it is the conclusion which the Tribunal reaches from all of the material which it has considered in paragraphs 106 onwards. To the extent that the analysis contained in those paragraphs is in error, the conclusion in paragraph 128 cannot be relied upon.

110. Mr Gammie himself makes forensically a similar point as part of his general description of the transactions. We do not in any sense criticise him for it since there is great force in what he says. It appears in his skeleton argument:

> "LME and CBL were careful to ensure that their arrangements could not, as a formal or legal matter, be so construed [as a sale of completed holiday homes] and the evidence that they presented to the First-tier

> Tribunal was directed to proving that the formal or legal position that they had adopted reflected the substance or reality of their arrangement. But, having heard LME's and CBL's evidence, the First-tier Tribunal concluded that the substance or reality of the matter was otherwise."

111. Even accepting that the Tribunal did so hold, it must be remembered that such a categorisation does not necessarily lead to the conclusion that there is abuse. First, the substance or reality thus identified is that the purchaser has entered into agreements as the result of which he obtains a completed holiday home. But there are different ways in which that result could be achieved. For instance, a land-owner could build a house and sell it together with the plot; he could contract to sell the house with a yet-to-be-built house on it; he could adopt the self-build route using his captive associated builder; he could adopt the self-build route using an associated builder (as in the present case); or he could make arrangements with a non-associated builder under which they shared an on-site office where the land-owner was able to put the purchaser in contact with the builder but took no interest in the contractual relationships between purchaser and builder. Those are all transactions which it is easy to envisage in the real world. The substance or reality of them all is in this sense the same, namely that the purchase in all cases will end up with a completed holiday home. And yet the VAT consequences at least of the first and last transactions are clear and different.

112. In each of those examples, it is necessary to see what the consequences of the substance and reality are. Is there abuse or is the choice which *Halifax* and *Part Service* recognise one which is available in the particular case?

113. Further, in each of those cases, the substance or reality of the transaction (a real-world provision of a completed holiday home) may not lead to a VAT supply of a completed holiday home for another reason. This is the possibility that although there is a tax advantage gained and intended to be gained, it is not the essential or principal aim of the transaction. The structure of a transaction may be driven by commercial necessities leading to the objective conclusion that the second limb is not satisfied. If one or both limbs is not satisfied, then there is no VAT supply of a completed home. Instead, there are VAT supplies of land and construction services and the assessment of a Tribunal that the substance or reality of the transaction is that there is provision (we avoid the use of the word supply at this point) of a completed holiday home does not lead to the conclusion that there is a supply for VAT purposes of a completed holiday home.

114. It is against all of that background – both what Mr Gammie said was the substance or reality of the transactions and what we have just said about that, substance and reality – that we must view Mr Gammie's submission that the first limb of *Halifax* is, contrary to Mr Peacock's submissions, satisfied.

115. Mr Gammie said that in relation to the first limb of *Halifax*, the Tribunal found that if the consideration paid for the holiday home is VAT free, this would be against the objective of the Directive in guaranteeing uniformity in VAT treatment between similar transactions. Mr Gammie said that it is self-evident that the arrangements that LME and CBL devised produced a non-uniform VAT treatment comparing a customer who bought a holiday home from LME/CBL and a customer who bought from a developer who straightforwardly sold a holiday home.

116. He also refers to paragraph 99 of the Decision where the Tribunal noted that LME and CBL agreed that a distortion of competition would be anti-purposive. But they also noted that a saving of tax is not a distortion unless it is contrary to the intention of the legislation. The agreement of LME and CBL begs the question, of course, about what the relevant distortion was in the present case. And that leads into the next point.

117. Mr Gammie said that the Tribunal concluded on the evidence that the comparable market in respect of which the distortion of competition arose was that of speculative developers, building and selling holiday homes. That is, we agree, what they said at paragraph 101. We have examined this paragraph in some detail already in considering what Mr Peacock had to say about it. But we have to say that we can detect no justification at all for the Tribunal's conclusion on this point. It appears to us to be no more than an assertion of the conclusion. The uninformed reader of the Decision would not have the

first idea, we suggest, why the Tribunal stated that this was the appropriate comparator. We are better informed but we do not understand why they have reached that conclusion either.

118. Mr Gammie said that the Tribunal's conclusion concerning the relevant market chimes with another of their conclusions namely that the substance or reality of what LME and CBL were selling and purchasers were buying was a holiday home. The conclusion in paragraph 102 therefore followed that:

> "… the contractual arrangements between LME and CBL and the customer creates a relationship which allows the customer to receive a finished house and to pay less VAT on the goods and services provided in building that house. The house is sold to the customer for a price that is broken down into a specified amount for land and a specified amount for construction services. The contractual arrangements creates the separation of supplies and consequently the tax saving."

119. This he said, is essentially a conclusion on the facts and one that is consistent with the Tribunal's essential finding on the substance or reality of the arrangements that LME and CBL had devised.

120. We do not accept those submissions. The Tribunal's reasoning does not begin to address why it is appropriate to adopt the development model as the comparator. There is no explanation why the normal commercial operations of a developer of the size of LME – not a Waites or a Wimpey – would be based on the development model rather than the self-build model, a model which, in any case, JMP says he learned was sometimes adopted in other parts of the World. This is not a finding of fact at all: it is a conclusion which

ought, if it is to be made at all, to be made on the basis of findings of fact, themselves based on the evidence, leading to the conclusion that the large developer is the appropriate comparator.

121. Moreover, in reaching their conclusion, the Tribunal relied, in paragraph 101, on the evidence of Mr Johnson. His evidence in was fact more directed at the second limb of *Halifax* and to the question whether there was a genuine and non-tax driven reason for adopting the self-build model. However, the Tribunal did rely on his evidence to identify a distortion in the market. But they so misrepresented his actual unchallenged evidence as to render flawed the comparison which they make.

122. Further, we do not understand why it is said that the tax consequences of a given set of transactions would be contrary to the purposes of the Directive if entered into between purchasers on the one hand and connected persons (in our case, LME and CBL) on the other hand but it would be so contrary if those very self-same transactions, not artificially contrived, were entered into between purchasers and two unconnected persons. We can, of course, see the very different argument in relation to the second limb of *Halifax* where there is a real difference between the two cases, but that is a different argument.

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123. Mr Gammie submitted that the comparator should be identified from the perspective of the customer. We do not see why that should be so. The perspectives of supplier and of customer are, we think, both factors to be taken

into account. In any case, they are only factors in an overall assessment: that is to say, an objective assessment of the purpose of the legislation in a particular context. What would or would not be foreign to its purpose may not be capable of resolution by reference to either of those perspectives.

124. However, let us assume that Mr Gammie is correct in what he says about this. The aim of the customer is undoubtedly to acquire a holiday home. But that could equally be said to be his aim in acquiring a plot and building a house on it himself. There is, we consider, a clear difference between buying the plot and contracting for the building and buying a completed building. Typically, the purchaser of a completed home contracts, *ex hypothesi*, only once the building has been completed. Under different models, a purchaser might acquire an option, or he might pay a deposit or he might even contract to purchase a yet-to-be-built house. But apart from an option fee or a deposit, the development model, as we understand, will only result in significant payment once the house is completed. The discussion of the development model in the Decision appears to us to relate only to the case where a completed house is purchased and that is the comparator market which the Tribunal adopted. The customers in the present case however acquired an interest in the land at the outset for which they paid and they paid for the construction work in stages over a year or 18 months as building work progressed. Customers were able to obtain variations internally and even externally subject to any necessary planning consent. As the Tribunal stated at paragraph 15(d) "many homes were custom built."

125. In our view, the Tribunal's decision on the first limb of *Halifax* is flawed and cannot stand for essentially two reasons, each of which demonstrates an error of law against which LME and CBL have a right of appeal under section 11 Tribunals, Courts and Enforcement Act 2007:

a. First, even if their actual conclusion is one which a properly directed tribunal could have reached, we consider that the Decision does not provide that level of analysis and reasoning, and appropriate fact-finding, which a litigant is entitled to expect. We are entitled, therefore, to set aside the decision and to make our own decision provided that we consider it possible to do so on the basis of the facts found by the Tribunal and other facts which we ourselves feel able to find consistently with section 12(4) Tribunals, Courts and Enforcement Act 2007. If there were a need for further findings of fact which we did not feel able to make, we would have to remit the matter for reconsideration.

b. Secondly, if we are wrong in making that assessment of the Decision, we do not consider that the conclusion reached by the Tribunal, even on their own findings of fact, is one which they could properly have reached.

126. As to the first of those reasons, we have identified the absence of reasoning in relation to identification of the appropriate comparator. Whilst they referred to the right of a trader to adopt, in the absence of abuse, a course which results in less tax than another course, the Tribunal did not address the argument on

the facts or explain why the course adopted by LME and CBL was anti-purposive other than to refer to the fact that less tax is paid under the route adopted than would be paid under the development model. It seems to us that they simply asserted the anti-purposive result by reference to the tax advantage of one course as compared with another, reaching that conclusion because, and only because, they adopted the comparator which they did. They did not explain why it was anti-competitive to adopt a model which resulted in two separate supplies when two supplies would be the inevitable consequence where the vendor of the land and the builder were entirely independent persons. They gave no explanation for the rejection of such transactions as the appropriate comparator.

127. Further, the Tribunal appear to have based themselves on a misunderstanding of Mr Johnson's evidence. Mr Johnson did not say what he is recorded as saying. It is not easy to see what weight the Tribunal attached to their own statement of his evidence, but in the context of paragraph 101 as a whole, displaying as it does, inadequate reasoning, it is unsafe to think that it did not play an important part.

128. Significantly, the Tribunal did not address JMP's evidence about his commercial reasons for adopting the self-build model.

129. Since we consider the Tribunal's decision to be flawed for the first reasons, we can go on to remake the Decision. We have mentioned some aspects of the

evidence in paragraph 94 above. We consider that JMP's evidence should be accepted: it was not effectively challenged in cross-examination and what Mr Gammie had to say about it in submissions does not justify rejection of it. In whatever way one reads that evidence, it provides a clear commercial reason for adopting the course which was adopted rather than the development model which HMRC would have to establish as the normal commercial transaction if it is to succeed.

130. It is to be accepted (indeed it is common ground) that a supply of land by a landowner and a supply of construction services by an independent trader are separate supplies to be taxed as such. There is not a single supply by either of them of a completed holiday home nor a joint single supply. Further, it cannot be contended that the result is anti-purposive: there is no scope for the application of the *Halifax* principle. It is also to be accepted, in our view, that JMP had genuine commercial reasons unconnected with tax for adopting the self-build model. If it is not anti-purposive for a purchaser to acquire a completed holiday home from two unconnected traders as a result of separate supplies, we do not consider that it is anti-purposive either for the purchase to acquire his completed holiday home as a result of separate supplies from LME and CBL in circumstances where there are genuine commercial reasons having nothing to do with tax saving for the supplies to be made available to the purchaser only as separate supplies. We do not need to go so far as to say that it would have been impossible, or even very difficult, for LME to have adopted the development model. It is enough that there are real and genuine

commercial reasons. On the other hand, our conclusion should not be taken as entailing that it would always be open to a developer, including a Waites or a Wimpey which would normally adopt the development model, to adopt the self-build model and to seek to have the supply of land and the supply of construction services recognised as separate supplies to which the *Halifax* principle was not applicable.

131. We have not overlooked what the Tribunal said in paragraph 134:

> "The evidence indicating the obtaining of a tax advantage is strong when compared to the weaker and limited evidence of commerciality (ring-fencing of risk and self-build model)."

132. We are not clear quite what the Tribunal had in mind when they included the words "self-build model" in the parentheses. We cannot read this as a short-hand reference to LME's capital requirement and JMP's evidence about it. That evidence is not referred to anywhere in the Decision and the only reference to capital, or working capital, is in a quotation from a letter dated 3 June 2008 sent by LME's tax advisers to HMRC. If that aspect was intended to be included in the reference to "self-build model" we can only say that we do not consider that it can be regarded as so weak as to justify the conclusion that the essential or principal purpose of the objectionable transactions (*ie* the involvement of CBL) rather than a significant and important (or any lesser epithet) purpose was to obtain a tax advantage. Paragraph 134 is, of course, directed at the second limb of *Halifax*, but we address it lest it be said that it is somehow to be incorporated into the analysis carried out by the Tribunal of

the first limb and thus to show that the commerciality of the arrangements could not be prayed in aid (being too weak) to resist the conclusion that the transactions were anti-purposive.

133. Two consequences follow from the preceding paragraph:

a. Transactions normally taking place under the development model cannot form the normal commercial operations against which the comparison required in the present case as a result of *Halifax* should be judged.

b. Structuring LME's and CBL's businesses in accordance with the self-build model as a matter of genuine commercial choice was an effective choice for VAT purposes as envisaged in *Halifax* and *WHA*.

134. In our view, the correct comparison to make is between transactions taking place under the LME/CBL self-build model and transactions under which LME supplies the land and an unrelated company builds the holiday home. The first limb of *Halifax* is not, therefore, satisfied.

135. But even if it is going too far to say that transactions taking place under the development model are incapable of forming an appropriate comparator, there is nothing, in our view, which would justify the rejection of the self-build model with an unrelated builder as an alternative comparator. At best, from HMRC's point of view, the present case is one where "it is difficult to decide whether a particular arrangement is one which includes a step or steps which amount to an abuse or whether it is a course which is properly open to the

taxpayer as a way of minimising his liability to VAT" within the words of Lord Neuberger in *WHA* at [29].

136. If it is necessary to resolve that difficulty and to conclude that one or other model is the only possible comparator, we would adopt the transactions under which LME supplies the land and an unrelated company supplies the construction services. We see this as being a question of law or of mixed fact and law which can properly be the subject matter of an appeal on an issue of law under section 11 Tribunals, Courts and Enforcement Act 2007.

137. However, we doubt that that is necessary. The onus is on HMRC to establish that there is an abuse and thus that the self-build model is anti-purposive in the present case. Unless we are persuaded, which we are not, that transactions taking place under the self-build model are not normal commercial operations for a developer such as LME, abuse cannot established. In this context, compare *Halifax* at paragraph 75 where the Court said in relation to the second limb that it must be "apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain a tax advantage". This language is not consistent with an obligation on the taxpayer to show the reverse.

138. We add that, even if the development model was not impossible, or even difficult, for either LME or a company similar to LME to adopt, the commercial position presented by JMP lends support to the argument that the

self-build model is a permissible alternative course open to LME/CBL within paragraph 73 of *Halifax* and [37] of *WHA*. In that case, we would nonetheless consider our reasoning in the three preceding paragraphs to apply.

139. Our analysis in [124] to [136] above demonstrates why we also consider that the conclusion reached by the Tribunal cannot stand even on their own findings of fact. Accordingly, if our assessment of the Decision set out in paragraph a. of [125] above is thought to be too harsh and if we are wrong in our conclusion that the Tribunal's decision cannot stand for the reasons set out in that paragraph, we consider, as a matter of law, that the development model was not a valid comparator.

140. LME's appeal therefore succeeds on the ground that the first limb of *Halifax* was not satisfied.

141. We add this. We have focussed very much on the issue of identification of a comparator. We have done so because, on the facts of the present case, we have found that to be the most helpful way in which to deal with the underlying rationale of the abuse doctrine. In other cases, it may be less helpful, or even not helpful at all, to adopt such an approach. But in case it is said that we have placed too much reliance on identification of the comparator, we respond by saying that we have used it simply as a tool to establish whether or not a tax advantage has been gained contrary to the purposes of the Directive and the VATA.

Abuse: the second limb of *Halifax*

142. In those circumstances the second limb of *Halifax* does not strictly need to be separately considered. We should nonetheless, say something about it although we do not propose to address the many criticisms which Mr Peacock makes of paragraph 106*ff* of the Decision.

143. Although the question whether the arrangements put in place by JMP, LME and CBL have, objectively, as their essential or principal purpose the obtaining of a tax advantage, our analysis leading to our conclusions on the first limb point strongly to the conclusion that the second limb is not satisfied either. It does not, of course, necessarily follow from the fact that the transactions are not anti-purposive that they do not have as their essential or principal purpose the obtaining of a tax advantage (or indeed *vice versa*). But given that our rejection of the development model as the appropriate comparator is put primarily on the basis that the normal commercial operations of a developer such as LME would not necessarily be the normal transactions under the development model, it seems to us to follow that the same factors would lead to the conclusion that the second limb of *Halifax* was not satisfied.

144. But if that is wrong, we can see that it would probably be necessary to address in some detail the criticisms of the Decision put forward by Mr Peacock and to

examine carefully what they can be seen as having decided and which of their findings were in fact justified on the evidence. It might then have been necessary to remit the matter to the Tribunal to make further findings. We do not need to take that course.

Conclusion

145. LME's appeal is allowed.

The position of CBL

146. It follows quite clearly from our conclusions that CBL is not itself liable to account for VAT. HMRC take a very technical point that CBL did not appeal; and yet there was an alternative assessment against it if it should turn out that LME was not liable. It is said that the Tribunal did not allow CBL's appeal. Mr Gammie's skeleton argument refers to paragraph 140 where the disposition is "The Appeal is dismissed" and to the summary on the front sheet of the Decision "Appeal dismissed". But those dismissals clearly refer only to LME's appeal. One needs only to look at paragraph 139 to see that the Tribunal saw the case as one where there was a single supply by LME. It is perfectly clear that the Tribunal did not regard CBL as having "supplied" anything other than, perhaps, zero-rated construction services to LME.

147. In any case, our reasoning leads inevitably to the conclusion that CBL is not liable since its supplies were only of zero-rated construction services. If as a matter of formality it is necessary that there be an appeal by CBL, then CBL

can apply to be joined to the appeal and for permission to appeal out of time. We hope that this will not be necessary in order to reflect the rights determined in accordance with our decision.

MR JUSTICE WARREN, President

Judge THEODORE WALLACE
JUDGES OF THE UPPER TRIBUNAL

RELEASE DATE:

ANNEX

THE TRIBUNAL'S DECISION ON ABUSIVE PRACTICE KEY PARAGRAPHS

99. The parties agree that a distortion of competition would be anti-purposive. A saving of tax is not a distortion but a saving that is contrary to the intention of the legislation would be a distortion.

100. The Appellant says there is no distortion. Rather, that the UK has a flawed legislative regime in that sales of a non-holiday home is a zero-rated supply but the sale of a holiday home is a standard rated supply. If a person buys a piece of land and engages a builder to build a holiday home then this would result in less VAT payable than if one buys a completed holiday home. The Appellants argue that this shows a legislative regime which is flawed in the application of VAT charges to holiday and non-holiday homes and the building of holiday homes by those owning land.

101. Where does the distortion, if any, lie? The financial model used by the Appellant to deliver the Site is self build, which involves selling plots of land and building houses separately on the land that has been purchased. Most commercial property developers would sell a completely built house. They would not separate the sale of the land from the building of the house. We heard evidence from Gavin Johnson, a surveyor and adviser to JMP, who said that large property development companies cannot separate the construction and land owning parts of their business. He said that they build and sell holiday homes as a complete package. This is the comparable house building market we need to examine to see if an unfair advantage would arise to the Appellant when compared to other commercial developers in the holiday homes market. Developers would build houses on a speculative basis and try to sell those houses to purchasers during the course of their construction. If a developer is able to build and sell a holiday home using a contractual arrangement which saves VAT then this would be an advantage to that developer. It would be an advantage since the cost of constructing the home would be less than that of the competitor given the tax saving afforded by the contractual arrangements. The purchaser in both cases would be receiving a completely built holiday home. The splitting of the contract in this way creates unequal treatment in the levying of VAT in a similar transaction and so creates a market distortion. A distortion arises where a supply of goods or services provided by competitors are treated unequally or differently for the purposes of VAT.

102. If taken together, LME and CBL, provide a finished house to the customer. The Tribunal, in determining the real substance and significance of the transaction, must consider the "links of a legal, economic and/or personal relationship between the operators involved in the scheme for reduction of the tax burden" (*Halifax,* para 81). This would mean the relationship between LME and CBL operating together and jointly owned. It seems to the Tribunal, that the contractual arrangements between

LME and CBL and the customer creates a relationship which allows the customer to receive a finished house and to pay less VAT on the goods and services provided in building that house. The house is sold to the customer for a price that is broken down into a specified amount for land and a specified amount for construction services. The contractual arrangements creates the separation of supplies and consequently the tax saving.

103. Let us look more closely at the relationship between the parties. The Frequently Asked Questions (FAQ) document states:

> "The land is owned and maintained by Lower Mill Estate Ltd, but a specialist building company, Conservation Builders Ltd, has been engaged to construct the homes on the Estate. One of the advantages to you in this arrangement is that although Lower Mill Estate must charge VAT on the land and the services it provides, Conservation Builders does not charge VAT as it is able to zero-rate the construction of your new home".

104 The FAQ identifies and advertises the tax savings. A holiday home built by LME and CBL, taken together, has a clear advantage over a holiday home built by a commercial property developer who sells the completed home rather than the land and the construction services. A supply of a holiday home structured around the relationship between the Appellant and the customer gives a tax saving where otherwise there will be a tax charge. The contractual arrangement and relationship therefore creates a market distortion.

105. The advantage obtained is a reduction in the payment of output tax by reducing the taxable amount. We know that the Principal VAT Directive seeks to create equality of treatment between taxable persons by guaranteeing a uniformity in the taxable amount for similar transactions. The Directive requires that VAT should be "exactly proportional" to the price paid by the customer. If part of the consideration paid for the holiday home is VAT free then this would be against the objective of the Directive in guaranteeing uniformity of the taxable amount.

106. Let us now look at the second condition to be satisfied for the application of the *Halifax* abuse argument.

107. The second condition required for establishing the *Halifax* abuse argument is that objective evidence must establish that the essential aim of the arrangements is to obtain a tax advantage. The essential aim is taken by the ECJ to mean the sole or main aim. This is a question of degree. If a transaction had a clear commercial purpose, the fact that there was also a tax advantage in undertaking the transaction would not be fatal to the transaction itself. A transaction may have strong or weak commercial reasons for structuring in a particular way. If the commercial reasons are substantial and make commercial sense then the essential aim of the transaction can be considered to be commercial. If, however, the evidence of commerciality is limited or minimal but there is a substantial tax advantage to be obtained, then the

essential aim of the structure would be to obtain a tax advantage. The Tribunal must look objectively at all the evidence to establish whether or not a tax avoidance motive exist. The Appellant may establish their subjective purpose in undertaking and structuring the transaction but it is the objective assessment of the evidence which is the relevant consideration. The evidence which the Tribunal would have to consider is, various company material including marketing documents, board minutes, minutes of meetings with advisers, planning meetings, memoranda and oral evidence among others. In establishing whether tax avoidance was objectively intended, the subjective intention of those undertaking the scheme becomes irrelevant.

…….

128. The Tribunal is not looking to disregard the contracts between the parties. However, the evidence presented creates a doubt as to the true nature of the supply between the parties. This doubt leads the Tribunal to look outside the contract for the true supply. The supply being made to the customer is a holiday home. It must be remembered that VAT is a tax on supplies not on contracts.

…….

134. What we can deduce is that the contractual arrangements and the companies involved are linked. There is joint marketing, standard form documentation, a clear time chronology for agreeing contracts, commission payments inter se, common ownership and common staff. The objective evidence, obtained from the minutes of meetings, notes, correspondence and marketing materials together with the tax advice provided indicates that the essential aim of the transaction was to obtain a tax advantage. The evidence indicating the obtaining of a tax advantage is strong when compared to the weaker and limited evidence of commerciality (ring-fencing of risk and self build model). The companies appeared to be inter-dependent on each other for their trading activity. CBL only constructs homes for customers of LME. The contractual arrangement has been constructed such that there is a VAT advantage to be obtained in the building of holiday homes. Without the splitting of land and construction supplies there would have a greater VAT liability. There may be perfectly legitimate marketing and organisational reasons for splitting the contract between different companies. However, notwithstanding the existence of those particular justifications for splitting the supply, if the principal aim is to secure a tax advantage, then those justifications would not have helped the Appellant to rebut the abusive practice argument. The evidence in this case established that the "minimum threshold" for establishing an abusive practice was met.

MR JUSTICE WARREN

PRESIDENT

MR THEODORE WALLACE

UPPER TRIBUNAL JUDGE

RELEASE DATE: 22 December 2010