[2016] UKUT 0189 (TCC)
Reference: UT/2014/0055
UT/2014/0056

VALUE ADDED TAX – option to tax- whether supply of land taxable at standard rate because option to tax validly exercised – whether prior permission from HMRC required for late election – whether HMRC can validly dispense with this requirement for prior permission – paragraph 3 (9) and paragraph 30 Schedule 10 Value Added Tax Act 1994

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

DARREN HILLS and LYNNE HILLS

Appellants

- and –

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

TRIBUNAL: JUDGE GREG SINFIELD
JUDGE GUY BRANNAN

Sitting in public at the Royal Courts of Justice, London on 8 and 9 February 2016

Rebecca Murray, counsel, instructed by The VAT Consultancy, for the Appellants

Hui Ling McCarthy, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This is an appeal against the decision of the First-tier Tribunal ("FTT") [2014] UKFTT 646 (TC) (Judge Cornwell-Kelly and Mr John Coles) released on 2 July 2014 that the sale to Mr and Mrs Hills ("the Supply") of the freehold interest in Unit 4, Cardiff Gate Business Park ("the Property") by NM Pensions Trustees Limited ("the Trustee") on 22 or 23 December 2011[1] was chargeable to VAT at the standard rate.

2. If the Supply is chargeable to VAT, the obligation to account for and pay VAT falls on the Trustee rather than on Mr and Mrs Hills. They are, however, concerned in the VAT treatment because the sale price of the Property (£650,000) was expressed to be "plus VAT (if applicable)". The amount of VAT involved is £130,000.

3. Mr and Mrs Hills run a dental practice from the Property. The dental practice is exempt from VAT and, therefore, any VAT charged on the Supply will be an irrecoverable cost to Mr and Mrs Hills.

4. In addition, HMRC cross-appeal against the FTT's case management decision refusing HMRC permission to amend its Statement of Case to raise a new point ("the Dispensation Issue"). HMRC also make a protective application to raise the Dispensation Issue before this Tribunal should HMRC's cross-appeal be dismissed.

The facts

5. The FTT set out the facts in [3]-[14]. The FTT's findings of fact are not in dispute and these can be summarised as follows.

6. The Trustee was the trustee of a self-invested pension plan ("the SIPP"). The SIPP was established by a Trust Deed dated 3 January 2002.

7. Dr and Mrs Patel, who were dentists, became members of the SIPP on 30 July 2003 and 5 August 2003 respectively.

8. The Property was purchased by the Trustee on 30 March 2004.

9. The next day, on 31 March 2004, the Trustee granted Dr and Mrs Patel a lease of the Property ("the Lease"). Dr and Mrs Patel used the Property to run their dental practice.

10. On 6 April 2006, the rules of the SIPP were replaced by a new governing Trust Deed ("the 2006 Deed").

[1] The FTT noted that both dates were given in the papers.

11. Over six years later, on 6 August 2010, the Trustee belatedly notified HMRC that it had opted to tax[2] the Property with effect from 14 April 2004. The effective date was amended in correspondence to 30 March 2004. On 16 November 2010, HMRC formally accepted the Trustee's late notification and confirmed that the effective date was 30 March 2004. From 31 March 2004, the Trustee had charged VAT on the rental payments and had accounted for tax on the basis that its supplies to the Patels were taxable.

12. Dr Patel died on 8 September 2010.

13. On 22 or 23 December 2011, the Trustee sold the Property to Mr and Mrs Hills for £650,000, "plus VAT (if applicable)".

14. On 29 April 2014, HMRC wrote a letter to the Trustee stating that if prior permission to opt to tax had, in fact, been required under the legislation then HMRC were exercising their discretion to dispense with the requirement for the Trustee to seek prior permission and to treat the option as valid. The letter stated that HMRC's discretion to dispense with the requirement to seek permission was exercised under paragraph 30 of Schedule 10 to the Value Added Tax Act 1994 ("VATA") 1994. On 7 May 2014 (12 days before the FTT hearing), HMRC disclosed this letter to Mr and Mrs Hills' representatives, having first sought and obtained the permission of the Trustee.

Legislation

15. At the material time, so far as relevant, paragraph 2 Schedule 10 to VATA 1994 sets out the effect of the option to tax as follows:

> *"Election to waive exemption*
>
> 2(1) Subject to sub-paragraphs (2), (3) and (3AA) and paragraph 3 below, where an election under this paragraph has effect in relation to any land, if and to the extent that any grant made in relation to it at a time when the election has effect by the person who made the election … would (apart from this sub-paragraph) fall within Group 1 of Schedule 9 [which exempts the grant of interests in land], the grant shall not fall within that Group."

16. At the material time, Schedule 10 VATA 1994 set out the day on which an election to waive exemption (i.e. an option to tax) takes effect:

> "3(1) An election under paragraph 2 above shall have effect –
>
> (a) subject to the following provisions of this paragraph, from the beginning of the day on which the election is made or of any later date specified in the election; …
>
> …

[2] At the time of the 2004 transaction in this appeal the option to tax was known as the election to waive exemption. Both expressions are well understood as meaning the same thing and we use them interchangeably in this decision.

(2) An election under paragraph 2 above shall have effect in relation to any land specified, or of a description specified, in the election.

…

(6) An election under paragraph 2 above shall have effect after 1 March 1995 only if –

…

(b) In the case of an election made on or after that date –

(i) written notification of the election is given to the Commissioners not later than the end of the period of 30 days beginning with the day on which the election is made, or not later than the end of such longer period beginning with that day as the Commissioners may require; and

(ii) in a case where sub- paragraph (9) below requires the prior written permission of the Commissioners to be obtained, that permission has been given."

17. One of the three main issues before the FTT was whether the Trustee's exercise of the option to tax was invalid because the Trustee was required (but had failed) to seek prior permission from HMRC before the election could be exercised ("the Prior Permission Issue"). For supplies made before 1 June 2008[3], the provision governing prior permission from HMRC was paragraph 3(9) of Schedule 10 VATA which, as far as relevant, provided:

"Where a person who wishes to make an election in relation to any land (the relevant land) to have effect on or after 1st January 1992, has made, makes or intends to make, an exempt grant in relation to the relevant land at any time between 1st August 1989 and before the beginning of the day from which he wishes an election in relation to the relevant land to have effect, he shall not make an election in relation to the relevant land unless the conditions for automatic permission specified in a notice published by the Commissioners are met or he obtains the prior written permission of the Commissioners, who shall only give such permission if they are satisfied having regard to all the circumstances of the case and in particular to –

(a) the total value of exempt grants in relation to the relevant land made or to be made before the day from which the person wishes his election to have effect;

(b) the expected total value of grants relating to the relevant land that would be taxable if the election were to have effect; and

(c) the total amount of input tax which has been incurred on or after 1st August 1989 or is likely to be incurred in relation to the relevant land,

that there would be secured a fair and reasonable attribution of the input tax mentioned in paragraph (c) above to grants in relation to the relevant land which, if the election were to have effect, would be taxable."

[3] It was this provision, rather than the re-written provision in paragraph 28, that was applicable to the supply by the Trustee to the Patels in 2004.

18. As regards supplies made on or after 1 June 2008, the rewritten provision is at paragraph 28 of Schedule 10 which provides as follows:

> "(1) This paragraph applies if –
>
> (a) a person wants to exercise an option to tax any land with effect from a particular day,
>
> (b) at any time ("the relevant time") before that day the person has made, makes or intends to make an exempt supply to which any grant in relation to the land gives rise, and
>
> (c) the relevant time is within the period of 10 years ending with that day.
>
> (2) The person may exercise the option to tax the land only if-
>
> (a) the conditions specified in a public notice are met in relation to the land, or
>
> (b) the person gets the prior permission of the Commissioners (but see also paragraph 30)."

19. Paragraph 30 of Schedule 10[4] allows HMRC to dispense with the requirement for prior permission. If HMRC does so, a purported election is treated as if it had been validly exercised. Paragraph 30 provides as follows:

> "30(1) This paragraph applies if -
>
> (a) an option to tax was purportedly exercised in a case where, before the option could be exercised, the prior permission of the Commissioners was required under paragraph 28, and
>
> (b) notification of the purported option was purportedly given to the Commissioners in accordance with paragraph 20.
>
> (2) The Commissioners may, in the case of any such option, subsequently dispense with the requirement for their prior permission to be given under paragraph 28.
>
> (3) If the Commissioners dispense with that requirement, a purported option—
>
> (a) is treated for the purposes of this Part of this Schedule as if it had instead been validly exercised, and(*b*) has effect in accordance with paragraph 19."

20. The Value Added Tax (Buildings and Land) Order 2008 introduced the present text of Schedule 10 which had effect in relation to supplies made on or after 1st June 2008 subject to transitional provisions and savings in Schedule 2 to the Order.

The FTT's decision

21. There were three main issues argued before the FTT.

[4] Which has effect in relation to supplies from made on or after 1 June 2008.

22. First, Mr and Mrs Hills argued that although the Supply was between the Trustee and themselves, the beneficiary of the SIPP, ie Mrs Patel, was deemed to have made the sale under paragraph 40(2) Schedule 10 VATA 1994. Since Mrs Patel had not opted to tax, the supply to Mr and Mrs Hills was exempt from VAT (the "Grantor Issue"). The greater part of the argument before the FTT concerned this issue.

23. Secondly, in the alternative, Mr and Mrs Hills argued that the Trustee did not in fact exercise the option to tax at all (the "Decision Issue").

24. The third argument put forward by Mr and Mrs Hills was that, even if their first two arguments were rejected, the Trustee's option to tax was invalid because the Trustee was required (and failed) to seek prior permission from HMRC before the election could be exercised (i.e. the Prior Permission Issue).

25. As regards the Grantor Issue, the FTT decided that the Supply was made by the Trustee and paragraph 40 Schedule 10 VATA 1994 did not apply (FTT [58]-[65]).

26. In relation to the Decision Issue, the FTT decided that Mr and Mrs Hills should not be permitted to raise this argument. The issue had not been addressed in their skeleton argument, required issues of fact which could not be established without an adjournment and that HMRC would be prejudiced (FTT [18]). Notwithstanding this conclusion, the FTT appears nonetheless to have decided the Decision Issue against Mr and Mrs Hills (FTT [66]-[69]).

27. The Grantor Issue and the Decision Issue are not under appeal and, therefore, we do not consider them further.

28. As regards the Prior Permission Issue, the FTT, accepting HMRC's arguments, decided that prior permission from HMRC was not required before the election could be exercised (FTT [70]-[73]). The relevant passages of the FTT's decision on the Prior Permission Issue are as follows:

> "70. The second major issue concerns the claim that the exercise of the option to tax in this case required the commissioners' prior permission under paragraph 28 of Schedule 10 –3(9) – and that none was obtained, meaning that the option was not effectively exercised and that the default position remained that supplies of an interest in the property were exempt. This argument is based on the claim that the anti-avoidance provisions of paragraphs 12-17 of Schedule 10 had somehow disapplied the option to tax and that therefore both the lease to Mr and Mrs Patel – and thus the sale the subject of this appeal – were exempt transactions. Although it was common ground that the property was a capital item and that Mrs Patel was connected with the Trustee for the purposes of Schedule 10, it is clear from the facts that the anti-avoidance provisions of paragraphs 12-17 were not applicable.
>
> 71. It has not been established on the balance of probabilities that the conditions at paragraph 12(1)(b) and (2), as subsequently defined, were satisfied. Thus, the appellants have not shown that when the property was acquired it was acquired in circumstances in which Mrs Patel was

> a "development financier" for the purposes of paragraph 14, or that the Trustee at the time the grant of the lease was made intended or expected that the Property would become exempt or would continue for a period to be exempt. Given that 30 March was the date from which the election to tax is deemed to have been effective, and that a lease was granted the following day in what was intended to be a taxable transaction, the conditions for the application of these provisions did not exist.
>
> 72. Paragraph 28, or its predecessor, therefore cannot be in point. We must ask (using the previous wording) whether the Trustee, when it wished to make an election, was a person "who has made, makes or intends to make, an exempt grant in relation to the relevant land … before the beginning of the day from which he wishes an election in relation to the relevant land to have effect"? If so, prior permission would have been needed for the election. While both the invoice issued on 14 April 2004 and the VAT invoice issued on 11 August 2004 give 30 March 2004 as the start date for the rent, the lease itself gave the rent commencement date as 31 March, so it is clear the grant was actually made on 31 March; and the effective date of the option to tax was 30 March.
>
> 73. Thus an exempt grant was not made "before the beginning of the day from which [the Trustee wished] an election in relation to the relevant land to take effect" – the grant was made the day after and was a taxable transaction. The matter can be tested by reference to the wording of Schedule 10 as revised, which leads to the same conclusion: paragraph 28(1) provides that if at any time before the day from which a person wishes an option to tax to take effect the person in question "has made, makes or intends to make an exempt supply to which any grant in relation to the land gives rise" he needs prior permission to elect. The analysis is the same: the option takes effect on 30 March, the grant is on 31 March."

29. As we have said, the FTT refused HMRC permission to amend its Statement of Case in order to argue the Dispensation Issue. The FTT's decision on this point (FTT [19]) was stated as follows:

> "19. In regard to HMRC's application to admit the new issue raised by their letter of 29 April 2014 (purporting to exercise their discretion to dispense with the need for prior permission to exercise the option to tax, if on the facts such permission had been required), our refusal was … based on the lateness of the introduction of this new factor so late in the day and which the appellants had had insufficient opportunity to respond to.
>
> 20. Moreover, we considered that this issue was likely to raise questions outside the tribunal's jurisdiction, both by reason of its being an exercise of the commissioners' discretion and because of the possible argument that it was, in the circumstances, an abuse of a statutory power in altering retrospectively the tax treatment of a transaction which had already occurred; it appeared therefore more suitable to be dealt with on an application for judicial review – as the appellants had indeed argued in their now withdrawn application for

> adjournment – rather than as a matter of normal statutory interpretation by the tribunal. Having regard to the possibility of the Upper Tribunal being in a position to exercise both a statutory interpretation and a judicial review jurisdiction, we explored briefly the option of transferring the appeal entirely to the Upper Tribunal under Rule 28, but HMRC made it clear that they would not consent to that course."

Anti-avoidance provisions: paragraphs 2 (3AA) and 3A Schedule 10 VATA 1994

30. Ms Murray, appearing for Mr and Mrs Hills, argued that the FTT had erred in its interpretation and application of the anti-avoidance rules contained in paragraph 2 (3AA) and 3A Schedule 10 VATA 1994[5] ("the anti-avoidance provisions") in respect of the Trustee's supplies to the Patels.

31. In HMRC's Response to Mr and Mrs Hills' Notice of Appeal to this Tribunal, HMRC stated:

> "HMRC's position is that the anti-avoidance provisions are, in principle, broad enough to cover a situation such as present (and as such, HMRC did not contend otherwise in its Skeleton Argument below)."

32. At the hearing, Ms McCarthy maintained a neutral stance on the application of these anti-avoidance provisions. Even if we accepted that the FTT was wrong in its analysis of the anti-avoidance provisions (at FTT [70] – [71]), the only issue was whether prior permission of HMRC was required under paragraph 3(9) Schedule 10. Even if the FTT had considered that paragraph 2(3AA) was engaged, this would only have had the effect of exempting the Trustee's supplies under the Lease to the Patels. It would have had no effect on the Trustee's supply to Mr and Mrs Hills. Mr and Mrs Hills still needed paragraph 3(9) to be engaged in order to succeed in this appeal.

33. We agree with Ms McCarthy that Mr and Mrs Hills cannot succeed in this appeal unless they can show that the Trustee required the prior permission of HMRC in order to exercise the option to tax in accordance with paragraph 3(9).

34. For this reason and because we received no argument from HMRC on the point, we intend to deal with the anti-avoidance provisions only briefly.

35. In summary, we agree with Ms Murray's submissions.

36. The Trustee was a "developer of the land" for the purposes of paragraph 2 (3AA) Schedule 10 to VATA 1994. Paragraph 3A of Schedule 10 to VATA 1994 provides a definition of a "developer of land" and the FTT correctly found (indeed, it was common ground) that the Property was a capital item in relation to the Trustee.

37. The second limb of paragraph 2 (3AA) Schedule 10 to VATA 1994 was satisfied because the grantor (ie the Trustee) intended the Property to become "exempt

[5] Now paragraphs 12-17 Schedule 10 VATA 1994

land" by virtue of the lease to Mr and Mrs Patel, who would occupy the Property for exempt use. "Exempt land" was defined by paragraph 3A(7). For these purposes, it was common ground that Mr and Mrs Patel were connected with the Trustee (paragraph 3A(7)(c), as the FTT found. Accordingly, the second limb of paragraph 2 (3AA) was satisfied.

38. In our view, the FTT erred in failing: (a) to apply the definition of a developer of land contained in paragraph 3A; and (b) by failing to apply paragraph 3A(7) with the result that the FTT did not appreciate that supplies made by the Trustee to Mr and Mrs Patel were exempt supplies for the purposes of paragraph 2(3AA).

The Dispensation Issue – agreement between the parties

39. As we have explained, the Dispensation Issue formed the centre-piece of HMRC's cross-appeal. In addition, HMRC made an alternative application to raise a new point before this Tribunal, viz the Dispensation Issue on the basis that it concerned a "question of law which no evidence could alter" (*Evans Medical Supplies Ltd v Moriarty (HM Inspector of Taxes)* (1957) 37 TC 540 at 588).

40. In the course of the hearing, Ms McCarthy argued that if we refused permission to hear the Dispensation Issue, Mr and Mrs Hills would be left in a most unsatisfactory position. In that eventuality, the only issue that would have been determined was the Prior Permission Issue. The effect of the dispensation would remain outstanding – there was no dispute that the dispensation letter of 29 April 2014 had been written.

41. After a short adjournment, Ms Murray indicated that Mr and Mrs Hills withdrew their objection to the Dispensation Issue being considered by the Upper Tribunal.

42. Accordingly, we granted HMRC's application to raise the Dispensation Issue as a new point in this Tribunal.

The Prior Permission Issue

Arguments for Mr and Mrs Hills

43. Ms Murray argued that the Trustee had decided to exercise the option to tax on 30 March 2004 and that it was common ground that the Trustee planned to lease the Property to the Patels under the Lease. As a result of the anti-avoidance rules, the Lease was an exempt transaction. Therefore, in a situation where the Trustee never made a taxable supply, the election to waive exemption never took effect.

44. The purpose of paragraph 3(9), as was apparent from the final paragraph, was to ensure a fair attribution between taxable and exempt supplies. In this case, the Trustee had no intention of making taxable supplies because its supplies were caught by the anti-avoidance rules and were therefore exempt. This, therefore, was a situation which fell within the purpose of paragraph 3(9) and would require prior permission of HMRC.

45. Because the Trustee only intended to make an exempt supply (by virtue of the application of the anti-avoidance provisions) the only consequence which an election to waive exemption could have in those circumstances was an abusive one.

46. Therefore, in Ms Murray's submission, the election to waive exemption would not take effect until a non-abusive, taxable supply was intended or made; this could not occur before 23 December 2011. In the meantime, because of the anti-avoidance provisions, exempt supplies were made, therefore, before the election to waive exemption took effect.

47. In accordance with paragraph 3(6), the election did not take effect until after the date of the Supply because the Commissioners had not given permission under paragraph 3(9).

Arguments for HMRC

48. Ms McCarthy submitted that, in accordance with the clear wording of paragraph 3(9), in order for prior permission to be required, the exempt grant had to be an exempt grant *made or intended to be made before* the election took effect. In other words, was an exempt supply made or intended to be made prior to 30 March 2004? In Ms McCarthy's submission the answer to that question was plainly in the negative.

49. The first supply made by the Trustee in relation to the Property was made on 31 March 2004. This was the day *after* the election to waive exemption took effect. The Trustee made no supplies of the Property before 31 March 2004. The Trustee's intention was always to make a supply (the Lease) after the election to waive exemption had taken effect.

50. This interpretation was consistent with the purpose of the legislation. Paragraph 3(9) would serve little purpose if it was (as Ms Murray contended) directed at a situation where exempt supplies were made – or were to be made – *after the election had taken effect* because that situation was dealt with by the normal partial exemption rules, which would apportion any input tax that arose. Paragraph 3(9) was, however, intended to deal with the situation where exempt supplies were made or were to be made *prior to the election taking effect*.

51. Furthermore, HMRC's interpretation was consistent with the statutory context of paragraph 3(9). The phrase in paragraph 3(9) "before the beginning of the day on which he wishes an election in relation to the relevant land to have effect" was a reference to the other provisions in paragraphs 2 and 3 Schedule 10 which refer to the time at which an election "has effect" eg paragraph 2(1) and, particularly, paragraph 3(1)(a). Paragraph 3(1)(a) defined the day on which an election made under paragraph 2(1) took effect.

Discussion of the Prior Permission Issue

52. Even on the assumption that the anti-avoidance provisions applied, we reject Ms Murray's submissions in relation to paragraph 3(9) Schedule 10 VATA 1994.

53. In our judgment, the interpretation which Miss Murray sought to place on the words "before the beginning of the day from which he wishes the election in relation to the relevant land to have effect" in paragraph 3(9) is a strained construction. The day on which an election to waive exemption has effect in paragraph 3(9) is, in context, a reference back to the earlier sub-paragraphs of paragraph 3 and, in particular, to paragraph 3(1)(a) and (6).

54. Moreover, as Ms McCarthy observed, we consider that the purpose of paragraph 3(9) was that it should apply to exempt supplies made or intended to be made *before* the election took effect and that exempt supplies after that time would be dealt with under the usual partial exemption rules.

55. Construing those words in their statutory context, the day on which the election was intended to have effect was 30 March 2004. Therefore, paragraph 3(9) only required prior permission of HMRC in respect of exempt supplies before that date. The grant of the lease to the Patels took place on the following day i.e. 31 March 2004. It follows, therefore, that we decide the Prior Permission Issue in favour of HMRC and have effectively reached the same conclusion as the FTT at [72]-[73].

The Dispensation Issue

56. Having decided the Prior Permission Issue against Mr and Mrs Hills, it is not strictly necessary for us to consider the Dispensation Issue, which only arises if paragraph 3(9) imposed a requirement that prior written permission of the Commissioners should have been obtained in March 2004. Nonetheless, because the point was fully argued before us, we consider the Dispensation Issue below. However, because it is not necessary for our decision we intend to address this point only briefly.

Arguments for Mr and Mrs Hills

57. Ms Murray referred us to Article 13 of the Sixth Directive (77/388/EEC). Article 13B provided for the exemption from VAT of supplies of land and buildings (including the leasing thereof). The election to waive exemption was contemplated by Article 13C and provided:

> "Member States may restrict the scope of this right of option and shall fix the details of its use."

58. Ms Murray submitted that paragraph 3(9) constituted a restriction on the election to waive exemption but paragraph 30 Schedule 10 represented a relaxation of the restriction.

59. Paragraph 30 had to be interpreted, Ms Murray contended, in accordance with ordinary principles of EU law, viz reasonableness, fiscal neutrality, legitimate expectation and legal certainty.

60. HMRC's purported dispensation sought to change the effects of an invalid election to waive exemption. This infringed the principle of legal certainty.

61. Moreover, attempting to grant a dispensation was not an affirmation of HMRC's understanding of the earlier transactions involving the Property. HMRC had understood that the supplies from the Trustee to the Patels were taxable and had not appreciated that they were caught by the anti-avoidance rules and were, consequently, exempt. HMRC's understanding of the transactions in 2004 therefore was, in fact, a misunderstanding.

62. Ms Murray referred to the decision of the European Court of Justice in *Grundsückmemeinscaft Schlossstrasse GbR v Finanzamt Paderborn* Case C-396/98 ("*Paderborn*") in which the Court considered whether a taxable person's right to deduct VAT paid on goods or services supplied to it with a view to certain leasing operations was retained where a legislative amendment post-dating the supply of such goods or services but pre-dating the commencement of the leasing operations deprived the taxable person of the right to waive exemption. The Court held that the right was retained in those circumstances. Ms Murray submitted that the same principle should apply to the retrospective change of the VAT treatment (by means of the dispensation) in this case.

63. Moreover, in Ms Murray's submission, HMRC's letter of 29 April 2014 did not consider the input tax position of the Trustee in 2004. This is the issue that the letter should have considered and the letter was, therefore, unreasonable.

64. As regards the principle of fiscal neutrality, retroactively affirming the VAT treatment of the Trustee's supply to the Patels was simply the affirmation of the mistake. The Trustee should not have been able to recover input tax. Instead of putting right mistake the dispensation letter merely absolved it. HMRC were now out of time to make adjustments to the Trustee's input tax position.

Arguments for HMRC

65. Ms McCarthy submitted that the earliest date on which HMRC could consider exercising its power to give a dispensation under paragraph 30 was on 7 February 2014 when Mr and Mrs Hills's advisers wrote to HMRC advising HMRC that the application of the anti-avoidance provisions required HMRC's prior permission for the option to tax under paragraph 3(9).

66. As regards the *Paderborn* decision, this was not on all fours with the present case. The right to grant a dispensation under paragraph 30 existed when Mr and Mrs Hills bought the Property; it was not as if paragraph 30 had been inserted into the legislative code after the Supply of the Property to Mr and Mrs Hills. In *Paderborn* the legislative change had been made after the purchase of the property in that case.

67. Paragraph 28 (originally, paragraph 3(9)) was a restriction on the right to deduct pursuant to the option to tax. Paragraph 30 was a relaxation of that restriction. There was no obligation under EU law to restrict the option to tax in the manner envisaged by paragraph 28. It was therefore hard to see how it was contrary to EU law to dispense with something which the UK government was not required to enact in any event.

68. In order to show that UK law was disproportionate, Mr and Mrs Hills had to show that the dispensation was outside the UK's wide margin of appreciation. Mr and Mrs Hills had simply failed to do this.

Discussion of the Dispensation Issue

69. We do not consider that the dispensation issued by HMRC in its letter of 29 April 2014 offended against principles of legal certainty or legitimate expectation.

70. We accept Ms McCarthy's submission that there had been no change of law. Paragraph 30 was already in existence when Mr and Mrs Hills bought the Property and, therefore, any argument that they might have based on the Prior Permission issue was always subject to the operation of that provision. In our view, therefore, there was no infringement of the right to legal certainty in the present case. This was, for that reason, very different from the *Paderborn* case where the change in law had come after the acquisition of the property but before the property was leased.

71. Moreover, we did not consider that there was a breach of the principle of legitimate expectation. Again, when Mr and Mrs Hills bought the Property it appears that the Trustees and the Patels thought that the onward sale to Mr and Mrs Hills was liable to VAT. HMRC gave no assurance to Mr and Mrs Hills that the sale of the Property to them would be anything other than a taxable transaction. Therefore, we considered that the principle of legitimate expectation provides no assistance to Mr and Mrs Hills in this case.

72. For these reasons, we reject Mr and Mrs Hills' arguments on the Dispensation Issue.

Disposition

73. For the reasons given above, we dismiss this appeal.

Costs

74. Any application for costs in relation to this appeal must be made within one month after the date of release of this decision. As any order in respect of costs will be for a detailed assessment, the party making an application for such an order need not provide a schedule of costs claimed with the application as required by rule 10(5)(b) of the Tribunal Procedure (Upper Tribunal) Rules 2008.

Judge Greg Sinfield
Judge of the Upper Tribunal

Judge Guy Brannan
Judge of the Upper Tribunal

Release Date: 25 April 2016