

[2017] UKUT 0410 (TCC)



Appeal No: UT/2016/0162

VAT - interpretation of Paragraph 36(2) of Schedule 10 to the Value Added Tax Act 1994

**UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER**

**THE COMMISSIONERS FOR HER MAJESTY'S
REVENUE & CUSTOMS**

Appellant and Respondent

- and -

BALHOUSIE HOLDINGS LIMITED

Respondent and Appellant

**TRIBUNAL: THE HONOURABLE LADY WOLFFE
(Sitting as a Judge of the Upper Tribunal)**

Sitting in public in Edinburgh on 24 April 2017

Elisabeth Roxburgh, instructed by Office of the Advocate General, for the Appellant

Philip Simpson QC, instructed by Grant Thornton, for the Respondent

DETERMINATION AND REASONS

Introduction

The Tribunal Decision Appealed Against

1. This is an appeal by the Commissioners for Her Majesty's Revenue and Customs ("HMRC") against a decision of the First-tier Tribunal, sitting in Edinburgh, released on 31 May 2016, [2016] UKFTT 377 TC (the "Tribunal Decision"), in which Judge Gemmell and Judge Shearer allowed an appeal by the Appellant Balhousie Holdings Limited ("Balhousie") in respect of:
 - (i) a decision of HMRC, by letter dated 24 June 2014, that Balhousie was liable to a VAT self-supply charge arising from the disposition of the Huntly residential care home ("the Huntly care home") to Target Healthcare REIT ("Target") in March 2013 (the "Review Decision"); and
 - (ii) a decision of HMRC, by letter dated 9 February 2015, to issue a notice of penalty assessment to Balhousie in respect of the Review Decision (the "Penalty Decision").

Balhousie is the respondent to this appeal; it was the appellant before the First-tier Tribunal. HMRC is the appellant in these proceedings before the Upper Tribunal. It was the respondent in Balhousie's appeal to the First-tier Tribunal. For ease of reference, I shall refer to them by name, "Balhousie" and "HMRC".

Procedural History

2. While the First-tier Tribunal refused to grant HMRC permission to appeal to the Upper Tribunal ("the UT"), by a decision released on 26 September 2016, the UT allowed HMRC's application for permission to appeal, made under rule 21 of the Tribunal Procedure (Upper Tribunal) Rules 2008.

The Issue

3. Balhousie operates 25 care homes. It also operates a VAT group with Balhousie Care ("BC") and three other subsidiaries. The issue in this appeal is whether Balhousie was liable to account for VAT on a self-supply that arose as a consequence of BC's sale of the Huntly care home, which had been zero-rated when supplied to BC, to a third party (Target) in March 2013, and the immediate lease back of the Huntly care home from Target to BC. The answer to this issue turns on the interpretation of Paragraph 36(2) of Schedule 10 to the Value Added Tax Act 1994 ("the Act") and the determination of whether or not, by virtue of those arrangements, BC had "disposed of its entire interest" in the Huntly residential care home, within the meaning of that provision.

Summary of Parties' Positions

4. Balhousie argues that BC did not dispose of its "entire interest" in the Huntly care home because the arrangements with the third party were a sale and lease back, and that one had to look at the substance of those arrangements as a whole, and which had been governed by missives between the parties. HMRC argues that the proper focus is on the individual transactions, particularly the disposal. On that approach, BC disposed of its entire interest in

the property on sale, notwithstanding the existence of an agreement immediately thereafter to lease the Huntly care home back to BC.

Summary of the Tribunal Decision and Grant of Permission to Appeal to the UT

5. The First-tier Tribunal considered that the sale and lease back transaction was a composite transaction forming a commercial unity. The First-tier Tribunal held that, although BC had disposed of its entire interest in the care home for a *scintilla temporis*, the sale and lease back was not a disposal of BC's entire interest in the Huntly care home for the purpose of paragraph 36(2) of Schedule 10 to the Act. Accordingly, the First-tier Tribunal allowed Balhousie's appeal. The UT granted HMRC's application for permission to appeal on the basis that "the question of whether a sale and leaseback should be regarded as involving a disposal of the seller/lessee's entire interest in the property for the purposes of Paragraph 36(2) of Schedule 10" was arguable.

The Relevant Statutory Provisions

6. It may assist to summarise the relevant statutory provisions before setting out their terms. Item 1 of Group 5 of Schedule 8 of the Act applies zero-rating (which may be beneficial to the tax payer) to the first grant by a person constructing a building "intended for use solely for a relevant residential ...purpose" of a "major interest" in the building. It is common ground between the parties that the supply by Faskally Care Home Limited ("FC") of the Huntly care home to BC was correctly zero-rated. However, provision is also made in paragraphs 36 and 37 of Schedule 10 to the Act for the removal of zero-rating, in certain circumstances. These circumstances include *inter alia* where the recipient of the supply of the building, which had attracted zero-rating on the basis that it was intended to be used solely for a relevant purpose, "has...disposed of [its] entire interest" in the building within a period specified by the legislation. The recipient of the supply (here, BC) is treated as having sold the building to itself immediately prior to that disposal. The practical effect is that the favourable zero-rating is withdrawn from the date of that subsequent disposal.

7. I set out the relevant provisions, as follows.

8. Section 30(2) of the Act provides:

“(2) A supply of goods or services is zero-rated by virtue of this subsection if the goods or services are of a description for the time being specified in Schedule 8 or the supply is of a description for the time being so specified.”

9. Paragraph 1 of Group 5 in Schedule 8 to the Act provides:

“The first grant by a person—

(a) constructing a building—

(i) designed as a dwelling or number of dwellings; or

(ii) intended for use solely for a relevant residential or a relevant charitable purpose; or

(b) *converting a non-residential building or a non-residential part of a building into a building designed as a dwelling or number of dwellings or a building intended for use solely for a relevant residential purpose,*

of a major interest in, or in any part of, the building, dwelling or its site.”

The Definition of “major interest”

10. Section 96 of the Act provides, *inter alia*:

“(1) In this Act –

...

“major interest”, in relation to land, means the fee simple or a tenancy for a term certain exceeding 21 years, and in relation to Scotland means the interest of the owner, or the lessee's interest under a lease for a period of not less than 20 years...”

The Provision for Zero-rating on Certain Supplies Relating to Buildings

11. Paragraph 35 of Schedule 10 provides:

“35 Introductory

(1) This Part of this Schedule applies where one or more relevant zero-rated supplies relating to a building (or part of a building) have been made to a person (“P”).

(2) In this Part of this Schedule—

“relevant zero-rated supply” means a grant or other supply which relates to a building (or part of a building) intended for use solely for—

(a) a relevant residential purpose, or

(b) a relevant charitable purpose,

and which, as a result of Group 5 of Schedule 8, is zero-rated (in whole or in part);

“relevant premises” means the building (or part of a building) in relation to which a relevant zero-rated supply has been made to P;

“relevant period”, in relation to relevant premises, means 10 years beginning with the day on which the relevant premises are completed.

(3) Where P is a body corporate treated as a member of a group under sections 43A to 43D, any reference in this Part of this Schedule to P includes a reference to any member of that group.”

Circumstances in which Zero-rating of the Supply Will Cease

12. So far as material, paragraph 36 of Schedule 10 provides:

“36. Disposal of interest or change of use following relevant zero-rated supply

(1) Paragraph 37 applies on each occasion during the relevant period when—

- (a) there is an increase in the proportion of the relevant premises falling within subparagraph (2) or (3), and
 - (b) as a result, the proportion of the relevant premises so falling (“R2”) exceeds the maximum proportion of those premises so falling at any earlier time in the relevant period (“R1”).
- (2) The relevant premises fall (or part of the relevant premises falls) within this subparagraph if P has, since the beginning of the relevant period, disposed of P's entire interest in the relevant premises (or part).
- (3) The relevant premises fall (or a part of the relevant premises falls) within this subparagraph if—
- (a) those premises do not (or that part does not) fall within sub-paragraph (2), and
 - (b) those premises are (or that part is) being used for a purpose that is neither a relevant residential purpose nor a relevant charitable purpose.
-”

The Charge to VAT

13. Paragraph 37 of Schedule 10 provides, *inter alia*:

“37. Charge to VAT

- (1) Where this paragraph applies, P's interest, right or licence in the relevant premises held immediately prior to the time when the increase referred to in paragraph 36(1) occurs is treated for the purposes of this Part of this Schedule as—
- (a) supplied to P for the purposes of a business which P carries on, and
 - (b) supplied by P in the course or furtherance of that business
- immediately prior to the time of that increase.
- (2) The supply is taken to be a taxable supply which is not zero-rated as a result of Group 5 of Schedule 8.
- (3) The value of the supply is taken to be—
- (a) in the case of the first deemed supply under this paragraph, the amount obtained by the formula—
- $$R2 \times Y \times (120-Z)/120, \text{ and}$$
- (b) in the case of any subsequent deemed supply under this paragraph, the amount obtained by the formula—
- $$(R2-R1) \times Y \times (120-Z)/120$$
- (4) For the purpose of sub-paragraph (3)—
- (a) R1 and R2 have the meaning given by paragraph 36(1)(b),

- (b) Y is the amount that yields an amount of VAT chargeable on it equal to—
 - (i) the VAT which would have been chargeable on the relevant zero-rated supply, or
 - (ii) if there was more than one supply, the aggregate amount of the VAT which would have been chargeable on the supplies, had the relevant premises not been intended for use solely for a relevant residential purpose or a relevant charitable purpose, and
- (c) Z is the number of whole months since the day on which the relevant premises were completed.”

Factual Background

14. Like the First-tier Tribunal, I was provided with a joint bundle of productions comprising documentation relative to the transaction concerned as well as a number of witness statements. No examination or cross examination was made in respect of these witness statements, which was also the position before the First-tier Tribunal. There is no suggestion that the First-tier Tribunal erred in any finding of fact it made; the contention is that it erred in law in its application of the relevant statutory provisions to those facts.
15. Accordingly, it is not necessary to set out the background in any detail. This is fully set out at paragraphs 6 to 29 of the Tribunal Decision.
16. For present purposes it suffices to summarise the arrangements which have led to the present appeal. In or around 2010, Balhousie decided to construct three new care homes. One of these was the Huntly care home. The land and subsequently the new care home at Huntly belonged to a subsidiary of Balhousie, namely FC, which was not part of the VAT Group. Following completion of the build, BC acquired the Huntly care home. This first sale to BC was zero-rated for VAT purposes.
17. Balhousie funded this project by entering into a sale and lease-back agreement with Target. HMRC understand that this arrangement was adopted by reason of the difficulties in obtaining bank financing at that time. This arrangement was entered into in March 2013. Missives were concluded by means of an offer on behalf of Target, dated 8 March 2013, and accepted on an unqualified basis by BC on the same day. The missives provided that, at the date of entry, BC should give Target entry to and actual vacant possession of the Huntly care home.
18. The missives included an obligation by Target to grant a lease of the Huntly care home in favour of BC with effect from the date of settlement. The lease provided that the property had to be used for an “Approved Use” which was specified as use as a residential care home and/or nursing home.
19. Balhousie’s position is that these arrangements are part of a composite transaction, whose discrete elements are interdependent. On that approach, the arrangements are looked at as a unity and judged by their substantive effect, not by an analysis of their discrete parts. Accordingly, while Balhousie accepts that BC granted a disposition of the Huntly care home and that BC accepted a lease back of those subjects, it stresses that those arrangements were governed by the missives. The disposition and lease, together with the missives, constitute composite arrangements entailing reciprocal obligations. The date of conclusion of the missives, the date of entry under the disposition and the date of the term of the lease were all the same date.

20. By contrast, HMRC contend that VAT is a transactional tax. It is therefore appropriate, it contends, to look at each transaction individually, regardless of what other transaction takes place as a consequence or as part of a larger series of transactions.

HMRC Change of Position

21. Miss Roxburgh, appearing on behalf of HMRC in this appeal to the UT, began by advising of a change of position on the part of HMRC. In particular, she explained that as HMRC now analysed matters, there were a number of supplies. When considering a disposal of an entire interest, this related back to the major interest that was the subject of zero-rating. When this was sold or assigned, a party had disposed of its entire interest. One looked at the major interest and asked whether, at the end of the transaction, the party had its major interest. On this approach, the *scintilla temporis* was irrelevant. In other words, as soon as a party divested itself of ownership, it did not matter if it retained a right or regained a separate right. That constitutes disposal of an entire interest and it mattered not what other interests might have been retained or granted separately. HMRC, therefore, did not rely on the *scintilla temporis* argument which it had advanced before the Tribunal. As a consequence, HMRC now argued that it was irrelevant that a separate interest was retained or gained.

Submissions on behalf of HMRC

The Proper Approach to Composite Arrangements

22. Before turning to the argument in detail, Miss Roxburgh made a number of general observations about the analysis of a composite transaction for the purposes of the Act. Under reference to the observations at paragraph 37 of Customs and Excise Commissioners v Southern Primary Housing Associations Ltd [2003] EWCA Civ 1662; [2004] STC 2009 (“Southern Primary”), she argued that for the purpose of VAT one looked at “transactions individually, component transaction by component transaction.” Even if linked, for VAT purposes they remain distinct transactions. Only if one transaction was merely ancillary to a main transaction, would one disregard the distinct nature of each transaction (*per* Card Protection Plan Ltd v Customs and Excise Commissioners (Case C-349/96) [1999] STC 270, [1999] 2 AC 601, at paragraph 29). In this respect, VAT was different for other forms of taxation.
23. She next turned to Customs and Excise Commissioners v Robert Gordon’s College [1995] STC 1093, a case not included in the Joint Bundle of Authorities, nor cited to the First-tier Tribunal. In Robert Gordon’s there was a similar argument albeit in relation to a different form of self-supply. In that case, an independent school charged fees, which constituted an exempt supply for the purpose of VAT. The College developed disused farmland and buildings it owned for use as playing fields and ancillary facilities. In order to secure the advantage of being able to deduct input tax, the College waived exemption from VAT in respect of the grant of an interest in land. The College granted a lease of the fields and facilities to a company, set up for this purpose, in return for a premium and annual rent payable by the company. The company granted a non-exclusive licence to the College for use of the fields and facilities.
24. HMRC (or, more accurately, the Commissioners for Customs and Excise as they then were) treated this as a self-supply. The College appealed to the Tribunal, which allowed the appeal

and held that the College occupied the subjects under a licence and, hence, was outside the self-supply charge. HMRC appealed. The Court of Session allowed the appeal, taking into account the fact that the College had originally developed the land and granted the lease. The House of Lords allowed the College's appeal against this decision. In doing so, Lord Hoffmann (giving the principal Opinion) emphasised (at p 1100 A-C) that for the purposes of VAT "it is not permissible to take a global view of a series of transactions in a chain of supply". From this, Miss Roxburgh argued that it was therefore not a question of a single supply. One had to determine whether there was a supply by a third party. The prior dealing of the taxpayer was irrelevant. One simply looked at each supply. This approach, she said, permeated the whole of the statutory framework.

25. Finally, she noted that, as zero-rating was a derogation from VAT, it had to be interpreted strictly (see Lord Hoffman at page 1096 B-E of Robert Gordon's).

Summary of Errors HMRC contends First-tier Tribunal made in the Tribunal Decision

26. In its skeleton argument HMRC argued that the First-tier Tribunal erred in law in its interpretation of paragraph 36(2) of Schedule 10 to the VAT Act 1994. (I did not understand this to be affected by HMRC's change of position, noted above). In particular, HMRC argued that the First-tier Tribunal ought to have concluded that:

- (i) the reference to an "entire interest" in paragraph 36(2) of Schedule 10 is to the particular interest in land which was the subject of the initial zero-rated supply;
- (ii) a sale of land is a transfer of a party's entire interest in land irrespective of whether a separate interest in that land is obtained as the result of a connected transaction;
- (iii) BC therefore disposed of its entire interest in the Huntly care home when it sold the same to Target on 8 March 2013; and
- (iv) the disposal by BC gave rise to a charge to VAT in terms of paragraph 37 of Schedule 10.

27. HMRC's motion was for the Upper Tribunal to uphold the appeal, and to reinstate the Review Decision and the Penalty Decision.

Proper Approach to the Interpretation of the VAT Act 1994

28. In its written skeleton, HMRC made a submission as to the proper approach to the interpretation of the Act. Under reference to UBS AG v Revenue and Customs Commissioners [2016] UKSC 13, [2016] 1 WLR 1005, it argued that, in interpreting a statutory provision, it is necessary to have regard to the purpose of the particular provision and, so far as possible, to interpret its language in a way which gives effect to that purpose (paragraphs 61 to 63 of UBS). It was also necessary to consider whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically. Where the relevant fact is the overall economic outcome of a series of transactions then that is the fact upon which it is relevant to focus. However, where the legislation required consideration to be given to a specific transaction, then other transactions, although related, are unlikely to have any bearing on its application (UBS at paragraphs 66 to

- 68). Miss Roxburgh also founded on these passages in her oral submissions. She drew a distinction between an indirect tax, which invited a consideration of the economic reality or outcome of a series of linked transactions, and VAT. The latter was a tax on supply and necessarily the focus was on each supply, viewed separately.
29. Each provision of an enactment has its own purpose which was to be understood in the context of the larger purpose of the enactment in which it is contained. Generally, the purpose will be found from a consideration of the particular Act itself. It may be possible to determine the purpose of a provision by reference to a line of government policy which Parliament clearly had in mind when framing the enactment. This can include reference to advice issued in respect of the legislation (Greenwich London Borough Council v Powell [1989] AC 995 at page 1011). In determining legislative purpose, the court can have regard to any reports in Hansard which disclose the manner in which the promoter of the provision intended it to be interpreted (Pepper (Inspector of Taxes) v Hart [1993] AC 593). Miss Roxburgh noted that, while Balhousie referred to a passage in Hansard dating from 31 January 2011 (see paragraph 38 of the Tribunal Decision), this was at such a high level of generality that one could not be clear as to what, specifically, the passages Balhousie founded on related to in the Act. The position prior to the 2011 change, was that there was a self-supply charge if there was a disposal and also a change of use within 10 years. All that could be gleaned from Hansard, and the amendments to the Act in 2011, was an intention to alter the position, and that a disposal itself would suffice to trigger the charge.
 30. If it is not possible to identify the purpose of a particular enactment, or the purpose is doubtful, the court is unlikely to depart from the literal meaning. The court must not infer a purpose without a proper foundation for doing so (Astall v Revenue and Customs Commissioners [2010] STC 137 at paragraph 44). Here, Miss Roxburgh argued, the only purpose that could be gleaned from the very general language of the passages in Hansard, were the need to provide for fairness and certainty, and to minimise avoidance risks arising on disposal of a whole interest on sale. In Astall, Arden LJ had eschewed reference to the Explanatory Note because it was in very general terms. That, she argued, was the position here.
 31. The correct meaning of a statutory provision is that which the legislature can be taken to have intended by using the statutory words in their context. That context includes the whole statute and the setting in which the statutory provision was enacted. The court is looking to identify the ordinary meaning of language in the general context of the statute (R v Secretary of State for the Environment, Transport and the Regions, ex p Spath Homes Ltd [2001] 2 AC 349 at pages 396 G-H, 397 A-D and 398B-C). This was no different than interpretation of any other statute.
 32. Miss Roxburgh identified a number of subsidiary points of interpretation:
 - (i) The interpretation of a statutory provision is not a process for its improvement or for removing anomalies (Stock v Frank Jones (Tipton) Ltd [1978] 1 WLR 231 at pages 234 and 238).
 - (ii) The heading of a section, sidenotes, or marginal notes are part of the Act. They provide an approximation of what is covered by the section. Nonetheless, it is permissible to consider them when considering the purpose of a section (Stephens v Cuckfield RDC [1960] 2 QB 373 at 383). As augmented in oral submissions, Miss Roxburgh noted that

permissible external aids to interpretation (such as an Explanatory Note to a statute) might also be relied on.

- (iii) Where the same word is used throughout a statute there is a presumption that it has the same meaning unless the context requires otherwise (Madras Electric Supply Corporation Ltd v Boarland (Inspector of Taxes) 1955 AC 667 at page 685).

Miss Roxburgh next turned to consider the relevant provisions of the Act in the light of this approach to statutory interpretation, and in particular the purpose of the key provisions.

Meaning of Disposal of Entire Interest

- 33. The critical words to be construed were the disposal of BC's "entire interest" in the Huntly care home. Those words appeared in the following context: Paragraphs 35 to 37 of Schedule 10 to the Act provide for the circumstances in which a taxpayer who has been the recipient of a zero-rated supply of specified interests in property (as it is accepted that BC was in respect of the Huntly care home) will incur a charge to VAT in respect of that supply (the "Self-Supply Charge").
- 34. Paragraph 36 of Schedule 10 sets out the circumstances in which the Self-Supply Charge will be payable. It provides for two situations in which this will occur. The first, contained in paragraph 36(2) of Schedule 10 is where the tax payer has disposed of his entire interest in the property (or part of it). The second, contained in paragraph 36(3) of Schedule 10, is where the premises are no longer used for a relevant residential purpose or a relevant charitable purpose. These were, Miss Roxburgh argued, mutually exclusive provisions. Further, there was nothing in paragraph 36(2) of Schedule 10 to suggest that it was concerned with the continuation of the relevant purpose, which was the subject matter of paragraph 36(3).
- 35. HMRC note that while the phrase "major interest" is defined in section 96 of the Act, the Act does not contain a definition of the phrase "entire interest". It was against this background, that the First-tier Tribunal concluded that BC had not disposed of its "entire interest" in the Huntly care home when it entered into the sale and leaseback agreement with Target. The First-tier Tribunal considered that the real right of ownership and the real right of lease were both interests. Following the transaction, BC still had an interest in the Huntly care home as a tenant under a lease. In coming to this conclusion, the First-tier Tribunal found that it did not matter that there was a short period of time when BC had no interest in the Huntly care home. Nor did it matter that the interest it held after the transaction was a different interest to that which had been the subject of the initial zero-rated supply.
- 36. HMRC contends that, when the phrase "entire interest" is considered in context, it is clear that Parliament intended it to be a reference to the whole of the interest which was the subject of the zero-rated supply. On that basis, where a party disposes of the interest in property that was the subject of the zero-rated supply, paragraph 36(2) will be invoked. HMRC argue that this is the case, regardless of whether the party obtained a separate interest in the property as a result of a connected transaction.

Purpose of Paragraph 36 of Schedule 10

37. HMRC argued that the First-tier Tribunal had erred in concluding, at paragraph 81 of the Tribunal Decision, that the purpose of paragraph 36(2) of Schedule 10 is “ensuring that use continues for relevant residential purposes and how that test may be policed”. There is nothing in VAT Act 1994 to support that purpose. Nor is there anything in Hansard or the other guidance issued by Parliament which would allow that purpose to be inferred.
38. Moreover, it was contended that it was clear from a reading of paragraph 36 that it provides for two circumstances in which a Self-Supply Charge will arise under paragraph 37. The purpose of paragraph 36(3) was, it was argued, to provide a charge to tax where there is a change in use. That cannot be the purpose of paragraph 36(2), which makes no reference to change of use. Had Parliament intended to restrict the Self-Supply Charge to circumstances where there was a change in use, then one would expect the provision to be in similar terms to paragraph 36(3).
39. This analysis is supported by consideration of the title to paragraph 36, which refers to “Disposal of interest or change of use” (emphasis added). It was submitted that this also suggests that the issue of change of use is separate to, and distinct from, a disposal of an interest. The guidance issued by HMRC in VAT Notice 708 provided further support, where it is stated that a Self-Supply Charge will arise when ownership of a property is transferred irrespective of whether or not the transferee intends to use the building for a qualified use (VAT Notice 708 at paragraph 19.3.1 and cf discussion of previous provisions at 19.2.1). This reflected the nature of the amendment made in 2011.
40. In these circumstances, it was argued that all that can be said of the purpose of paragraph 36 is that it sets out the circumstances in which the recipient of a zero-rated supply must account for the VAT on the original supply as output tax. The suggested purpose of ensuring that use continues for a relevant purpose cannot be ascribed to the provision where it covers situations where there is no change in use.

Proper Interpretation of Paragraph 36(2) of Schedule 10

41. HMRC argued that the First-tier Tribunal erred by failing to give proper consideration to the statutory context in which paragraph 36(2) of Schedule 10 has been enacted. When considered in its context, paragraph 36(2) is engaged whenever the interest in property which was the subject of the zero-rated supply is disposed of.
42. In terms of item 1(a)(ii) of Group 5 in Schedule 8 to the VAT Act 1994, zero-rating is granted in relation to the first grant of a major interest in, or in any part of, the building, dwelling or its site. “Major interest” is defined in section 96 of the Act. In Scotland, a major interest is either the interest of the owner of property or the interest of the lessee under a lease in excess of 20 years. Two points arose from this. First, only two specifically defined interests will result in zero-rating in terms of the provision. Secondly, those interests are separate and distinct interests. It would be both consistent and logical, HMRC argued, to view the reference to “entire interest” in paragraph 36(2) in the same way. Miss Roxburgh developed this argument in submissions, as follows: The reference to an “entire interest” was, in fact, a reference to the qualifying major interest (ie ownership or interest under a long lease). The references in paragraph 35(1) to the relevant zero-rated supply was a reference to the entire supply referred to. Paragraph 37 directed one back to look at the transfer of the original interest. This was illuminated by the *pro rata* calculation that took place under paragraph 36(1), eg if there had been the development of a whole site and then the disposal of 20% of it. Accordingly, in

paragraph 37(2), it was the interest the tax payer had immediately before the chargeable event that was “the major interest” to which one had regard. Putting it another way, one could not have a deemed supply (under paragraph 37(2)) other than a deemed supply of the “major interest” originally received.

43. Paragraph 37(1) also makes reference to the taxpayer’s interest for the purposes of calculating the Self-Supply Charge. It is stated that the interest held prior to the chargeable transaction is deemed to have been supplied to the taxpayer at that time. It was clear from the wording that the interest is assumed to be the same interest as was the subject of the original zero-rated supply. This can be seen from the terms of paragraph 37(4), which specifically refers to the relevant zero-rated supply in calculating the charge to tax. This, it was said, was a further indicator that the reference to “entire interest” in paragraph 36(2) was a reference to the specific interest which was the subject of the zero-rated supply. This also accorded with Scots property law. Real rights of ownership and under a lease were distinct.
44. This interpretation is also in keeping with the ordinary meaning of the words used. Where a party sells a property he disposes of his entire interest in the property. It does not matter whether the party thereafter obtains a separate interest in the property, for example a tenant’s interest under a lease. The real right of ownership and the real right of lease are separate categories of real right (Reid, The Law of Property in Scotland, 1996, at paragraph 5). It is clear from the legislation that the interest of ownership and the tenant’s interest under a lease are also viewed as separate categories of interest.
45. In these circumstances, viewing the provision in the context of the statute, the Parliamentary intention was that a Self-Supply Charge would occur under paragraph 36(2) whenever the taxpayer disposed of the specific interest which had been the subject of the zero-rated supply.
46. HMRC next turned to consider the interpretation proposed by Balhousie and which the First-tier Tribunal had accepted.

Interpretation Proposed by Balhousie and Accepted by the Tribunal

47. Before the First-tier Tribunal Balhousie had contended, and the First-tier Tribunal had accepted, that a sale and lease-back transaction did not constitute the disposal of a party’s entire interest in a building for the purposes of paragraph 36(2) of Schedule 10. This was because BC had retained an interest in the building by way of the lease. This argument was supported by reference to the approach of the Court in Sargaison (Inspector of Taxes) v Roberts [1969] 1 WLR 951. However, HMRC argued that there were a number of difficulties with this approach, as follows:
 - (i) *Incorrect purpose identified:* the First-tier Tribunal’s approach proceeded on an erroneous interpretation of the purpose of the provision in question. If it is recognised that change of use is not relevant to paragraph 36(2) of Schedule 10, then it can be seen that the fact BC continues to operate the Huntly care home for a relevant purpose is irrelevant.
 - (ii) *Failure to consider words in their statutory context:* Balhousie’s interpretation ignored the context in which the words are used throughout the Act. In determining the intention of Parliament, the context in which the words are used is relevant.

- (iii) *Approach in Sargaison*: The interpretation proposed by Balhousie follows the approach taken by the court in Sargaison. However, the provision under consideration here is not the same as that in Sargaison. Miss Roxburgh drew two points from this. The first related to context. The question for the court in Sargaison was when the right to claim capital expenditure would be lost in the context of income tax. When considering provisions relative to income tax, Miss Roxburgh accepted it will often be relevant to consider the overall economic outcome of a series of commercially linked transactions. However, VAT operates differently to income tax. In particular, in the context of VAT, transactions must be looked at separately even if they are linked, in the sense that one would not have happened without the other (The Commissioners of Customs & Excise v Southern Primary Housing Association Limited [2004] STC 209, at paragraph 37). In Sargaison, the court was addressing a different question under different legislation. Secondly, the wording used in the two provisions, while similar, is not identical. Sargaison is a well known decision. Had Parliament intended this provision to operate in the same manner to the provision in Sargaison, then one would have expected the same words to be used.
- (iv) Furthermore, there was nothing to indicate that the purposes of the statutes under consideration here and in Sargaison were the same. Mr Megarry’s observations about the use of “broader language” had no application. Here, Parliament had precisely defined what a “major interest” was.
- (v) *Increase in avoidance risks*: When the provisions were revised in 2011, the revisions were intended to provide fairness, certainty and consistency. They were intended to minimise avoidance risks and to be more straightforward to apply. Reference was made to Hansard, 31 March 2011, Delegated Legislation Committee. It would increase avoidance risks if the provision could be avoided wherever the transferee obtained a lesser interest in the property on or following transfer of the original interest held. This is to be contrasted with the certainty that arises where any transfer of the interest which was the subject of zero-rated supply will result in the Self-Supply Charge being incurred.
48. Looking at the transaction realistically, it was of a type intended to be covered by paragraphs 35 and 36 of Schedule 10 to the Act. Property law recognises distinct interests or rights in land. The definition of “major interests” in section 96 of the Act supports this. Construing the words in paragraph 36, in the context of the Act and its purpose, the different elements of the transactions attracted their own VAT treatment. By its disposal, BC incurred the Self-Supply Charge.
49. For these reasons, it was submitted, HMRC’s appeal should be allowed.

Submissions on behalf of the Respondent

50. Mr Simpson QC, who appeared for Balhousie, stressed the composite character of the overall arrangements by which BC disposed of, and leased back, the Huntly care home. He emphasised, too, that the individual transactions (of the disposal and the lease) were governed by the missives between BC and Target.

51. The first chapter of Balhousie’s submissions was regarding the proper approach to the interpretation of tax legislation. This was “to have regard to the purpose of a particular provision and interpret its language, so far as possible, in the way which best gives effect to that purpose”: UBS AG v HMRC [2016] 1 WLR 1005, at paragraph 61, *per* Lord Reed. In that same case it was observed that, as regards the facts, “[i]f, as in Ramsay, the relevant fact is the overall economic outcome of a series of commercially linked transactions, then that is the fact upon which it is necessary to focus. If, on the other hand, the legislation requires the court to focus on a specific transaction, as in MacNiven and Barclays Mercantile, then other transactions, although related, are unlikely to have any bearing on its application.”: *per* Lord Reed, at paragraph 68. The idea underlying this is that, “[T]he ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically.”: The Collector of Stamp Revenue v Arrowtown Assets Limited [2003] HKCFA 52, *per* Ribeiro, PJ, at paragraph 35. Reference was also made to The Pollen Estate Trustee Company Limited v Revenue and Customs Commissioners [2013] 1 WLR 3785, *per* Lewison, LJ, at 3792. In particular, Pollen Estate shows that this approach to interpretation (i) applies in cases where no issue of tax avoidance arises, and (ii) can apply in a manner favourable to the taxpayer, in that case by extending the availability of a relief from stamp duty land tax beyond the limit of its literal meaning.
52. In the context of European law, and in particular in the context of VAT, the proper approach to analysing facts against the legislative wording is even less tied to the literal meaning of the words in the legislation than the approach just described, which is based on direct tax cases. Reference was made to Litster v Forth Dry Dock & Engineering Company Limited [1990] 1 AC 546. Accordingly, to the extent that interpretation of provisions concerning zero-rating is informed by the approach of European law, the present facts are more strongly in favour of Balhousie than simply on an application of the approach set out in UBS.

The Policy behind Paragraphs 35 and 36(2) Schedule 10 of the Act

53. It can be seen that the policy behind paragraphs 36 and 37 of Schedule 10 to the Act is that zero-rating should be available only to the extent that the building is used for a relevant charitable or residential purpose for ten years. In support of this submission, reference was made to four documents or statements (presumably as external aids to interpretation), namely:
- (i) The statement by the Exchequer Secretary to the Treasury (Mr Gauke) to the Third Delegated Legislation Committee at a hearing on the proposed order to enact the provision, on 31 January 2011 (Hansard, 31 January 2011, Delegated Legislation Committee, col 5). The purpose was to clawback zero-rating where it no longer applied. The emphasis was on the change of use;
 - (ii) Revenue and Customs Brief 49/10 (7 December 2010, “the RCB”), which explained the reasons for introducing the provisions;
 - (iii) The Explanatory Note to the Value Added Tax (Buildings and Land) Order 2011 (SI 2011 No 86) (“the Explanatory Note”), which enacted these provisions. There was no reference to a supply or grant or major interest. There was simply a reference to disposal of an entire interest. The focus was still on use or change of use. While Ms Roxburgh had cited Astall as an example where the court found the explanatory note of no assistance, that did not apply in this case. The change of language in paragraph 36(2)

was, Mr Simpson argued, intentional. It was not focusing just on whether there was a supply; it focused on the broader issue such as disposal of an entire interest. There was no supply referred to in paragraph 37(1)(a)(b). The taxpayer was treated as making a supply to itself; and

- (iv) The list of scenarios in which zero-rating is said to be lost in VAT Notice 708, Buildings and Construction, paragraph 19.3 (the wording of the first item suggests that it anticipated an outright sale to a third party, and not a sale and leaseback entered into for financing purposes). In oral argument, Mr Simpson accepted that not much could be taken from this Notice.

In Balhousie's skeleton argument it was noted parenthetically that before the First-tier Tribunal, HMRC had suggested that in the course of the legislative procedure, there had been some change in the purpose pursued material to the present case. However, what the change was, was not identified. It was noted that no such change – or indeed any purpose at all – has been identified in the grounds of appeal or in HMRC's skeleton argument.

- 54. Mr Simpson noted that in none of the legislative materials referred to is there any reference to a policy directed at requiring not only that the building continue to be used for a relevant residential purpose, but also that it continue to be so used by the person who first acquired it. Balhousie argued that there is no obvious reason why such a policy would have been intended. If it were the policy behind the provisions, then there were anomalies, as follows: where the original acquirer leased the building to a new operator, zero-rating would be withdrawn; but it is clearly not withdrawn in that scenario. A policy requiring the original acquirer to continue to use the building for a relevant residential purpose may arise out of concerns about policing withdrawal when the property is no longer used by the first acquirer. But, it was submitted, that any such concerns do not in any event arise in the present case.
- 55. Against that background, it is clear that the policy proposition is met. Applying the legislation, purposively construed, to the facts, realistically viewed, BC has not disposed of its entire interest in the subjects: the building continues to be used for a relevant residential purpose. Moreover the person using the building for that purpose is the person who first acquired it, and who thereby benefited from the zero-rating.

Consideration of Other Scenarios under Paragraph 36 of Schedule 10 to the Act

- 56. To reinforce its argument about the correct statutory purpose, being that zero-rating should only be available to the extent that a building is used for a relevant charitable or residential purpose for the prescribed 10 years, reference was made to other scenarios.
 - (i) Merely leasing the building to another entity who uses it for a relevant residential purpose does not lose zero-rating: see paragraph 36 of Schedule 10, and the RCB, Annex A. Thus, if, in a single transaction, the first acquirer disposes of only the right to use the premises for a limited period, zero-rating is not withdrawn.
 - (ii) Furthermore, it was also suggested that, considering matters the other way around, if the first acquirer disposed of merely a fee in the building while retaining a liferent (or other right of occupation), for example limited to a specified period, that would not be enough to mean the withdrawal of zero-rating (it is of course competent for a liferent, or some other right of occupation, to be specified as enduring for a particular period of time, or

until a particular event other than the death of some individual: reference was made to Campbell v Wardlaw (1883) 10 R (HL) 65; Chaplin's Trustees v Hoile (1890) 18 R 27; Naismith v Boyes (1899) 1 F (HL) 79; McDonald's Trustees v McDonald's Executrix 1940 SC 433; Dobie, Manual of Liferent and Fee (1941), pp 1 f; and Gordon and Wortley, Scottish Land Law (3rd edn, 2009), vol 1, 17-26). Thus, if the effect of the present transaction had been achieved in that way, no charge to VAT would have arisen. The same result would follow if an owner settled property into a trust, in terms of which the owner had a right of liferent (or occupancy) and the fee were vested in a third party.

- (iii) If a residential care home were in England, it was argued that it was clear that a taxpayer could grant a leasehold interest to a nominee on its behalf, and then sell the freehold to a third party, by two separate transactions. (See Ingram v Inland Revenue Commissioners [2000] 1 AC 293.) In that scenario, it could not be said that the taxpayer disposed of its entire interest by either transaction. Under Scots law, however, it is not possible to structure a transaction in this way: see Kildrummy (Jersey) Limited v Inland Revenue Commissioners 1991 SC 1. Accordingly, it was argued that it would be inappropriate for a different tax result to follow simply depending on whether the property in question were located in Scotland or in England.

57. From these scenarios Balhousie argued that, given that HMRC appeared to accept that at least the first of these would not engage paragraph 36(2) of Schedule 10 of the Act; and as there does not appear to be any material difference between that and the second and third structures (liferent retained, and trust and liferent retained) set out in (ii) above; there does not appear to be any reason why the purpose of the legislation should require the structure in the present case to lead to the opposite result.

The case of Sargaison v Roberts

58. Indeed, Mr Simpson noted that the only case to consider similar wording to that of paragraph 36 of Schedule 10 of the Act, albeit in relation to a different tax, was the case of Sargaison, and it relied on the point just made about the undesirability of different tax outcomes in the different jurisdictions. That case concerned income tax. A farmer owned the land he farmed. He incurred capital expenditure on various items. The expenditure qualified for capital allowances. In 1964, the farmer created a trust for his family, and conveyed the land into the trust. The land was then immediately leased back to the farmer. The farmer continued to claim capital allowances in respect of the previous expenditure. However, the claim was refused on the ground that the right to claim capital allowances was lost if, “the whole of [the person’s] interest in the land in question ... is transferred ... to some other person”: Income Tax Act 1952, section 314. It is submitted that there is no material difference between these words and the terms used in paragraph 36(2) of Schedule 10 of the Act. (It was noted that HMRC had asserted that there is some material difference, but that neither before the First-tier Tribunal nor in any of the documents before the Tribunal have HMRC explained what that difference is).
59. In Sargaison, the farmer appealed. The General Commissioners allowed his appeal, and the inspector appealed to the High Court. In the High Court, Megarry, J, held that the farmer had not lost his right to capital allowances. Megarry, J, identified (at p 955) the issue as being whether these words applied, “where an owner conveys away the whole of his interest but receives back some lesser interest, as in the now familiar transaction of sale and lease-back”. He described (at 956) the statute as being, “drafted not in terms of English property law, with

references to estate owners and the like, but in broader more popular language which invites a broader and less technical construction”. He gave the reason for this as being that the statute had to be workable in three different legal systems. Megarry J, then held that the appropriate approach was to look at “the substance of [the] transaction’ and not at ‘the machinery used to carry it through”. He concluded:

“The taxpayer’s interest has, uno ictu, been merely reduced from ownership of the freehold to ownership of a lease; the whole of his interest in the land has therefore not been transferred to another; and that is the end of the case. I respectfully agree with the common sense approach of the general commissioners...” (at 958).

60. Balhousie argued that there was no material difference between the wording in section 314 Income Tax Act 1952, as referred to in Sargaison, and that in paragraph 36(2) of Schedule 10 to the Act. There is no reason of policy or principle to take a different approach to the latter than the approach taken by Megarry, J, to the former.

Proper Interpretation of Paragraph 36(2) of Schedule 10 to the VAT Act 1994

61. Mr Simpson argued that HMRC’s approach was too narrow. While Ms Roxburgh had argued that because VAT was a transaction tax and one had to consider the withdrawal of zero-rating, that it must concern a supply. But, Mr Simpson argued, this did not necessarily follow. Those arguments would apply equally to paragraph 36(3) but that paragraph was not concerned with supply. It was argued that, as a generality, it is possible in UK tax law for a sale and leaseback transaction to be treated as a single, composite transaction instead of two separate transactions: see for example Samarkand Film Partnership No 3 v HMRC [2012] SFTD 1 (the decisions in the Upper Tribunal and the Court of Appeal did not call this into question as a matter of principle).
62. Paragraph 35 of Schedule 10 to the Act referred to a grant or supply in the same way as this was done in Group 5 of Schedule 8: to identify a particular supply of a major interest in land. Looking at paragraph 35(3) that after 10 years, the zero-rating will remain. The entitlement to zero-rating depended on the intention to use the building for a relevant purpose: see paragraph 35(2) and Group 5.
63. Turning to paragraph 36, Mr Simpson noted the heading (“Disposal of interest or change of use following relevant zero-rated supply”). One looked at the factual issue relating to a building as opposed to any legal construct. More VAT will be charged as the non-zero-rated use increases. On each occasion, the question was to look at the building overall and to ask how much of it was not used for a relevant purpose.
64. The word “disposal” in paragraph 36(2) was not a reference to a supply or to a grant. Was the legislative intention to catch the transaction or to look at the reality of what was going on (as Balhousie contended)? If the intention had been to withdraw zero-rating upon the supply of an interest, being a supply that had attracted zero-rating, what would the drafter of the legislation say? It would be a supply or grant of the interest that had originally attracted zero-rating.
65. In response to a question from the court, Mr Simpson accepted that if the word “supply” had been used in paragraph 36(2), he could not make this argument. However, he noted that while supply could concern a transaction involving the grant of land or a building, that language had not been used in paragraph 36(2). If the drafter had wanted zero-rating to be withdrawn on

any transaction involving conveyances of the major interest whose supply had been zero-rated, it would have said so. It would have used the phrase “major interest”; but it did not. The language used was of “entire interest”. What was intended is what the wording said. An interest in land was composed of a bundle of rights. “Entire” meant looking at the rights which the taxpayer has and which together comprise his interest. One asked, if he retained any of these any more. The grant of a sub-lease, for example, would not wholly divest the taxpayer. Here the transaction had been the other way around: BC had disposed of its ownership but, at the end of the composite transaction, it had an interest under the lease. Paragraph 36(3) concentrated on use.

66. While, therefore, it was correct that VAT was a transactional tax, the overall purpose of these provisions had nothing to do with transactions that were liable to VAT or concerned a supply. In the case of a change of use, to a non-relevant use, zero-rating could be withdrawn, even in the absence of any transaction or supply at all. Accordingly, it was, he argued, misconceived to focus on supply. The initial attribution of zero-rating depended upon there being a supply but the potential for withdrawal of zero-rating did not. Withdrawal of zero-rating was not dependent upon there having been any supply. Therefore, Mr Simpson argued, there was no necessary link between the withdrawal of zero-rating and to VAT as a transactional tax.
67. Putting it another way, he argued that while it was correct that the arrangements comprised two transactions or supplies (a disposal and a lease), that was irrelevant to the present question. The correct question was to ask, had there been a disposal by BC of its entire interest as a result of the arrangement. If yes, then there is a deemed prior transaction as *per* paragraph 37(1) of Schedule 10 to the VAT Act 1994. If not, then there is no deemed transaction. After the arrangements, BC retained or had acquired an interest under a lease. It had not disposed of its entire interest. Paragraph 36(2) did not invite the question, has there been a supply; it poses a different question: has there been a disposal. Mr Simpson said that that question should be answered ‘no’.
68. In Southern Primary, the deduction sought by the taxpayer necessarily required there to be a transaction. That was not the case here. There was no need to look at the transaction. A “disposal” was not the same as a “supply”: “disposal” was a broader concept. It was not correct to limit oneself to looking at the individual supply to see if the terms for zero-rating were met, as HMRC seek to do. There were two supplies encompassed within the composite transaction. In ascertaining whether there was a disposal, one looked at the commercial reality and the legislative purpose, which was to clawback zero-rating if there were a change of use. One looked at the commercial reality, and this meant looking at both supplies together.
69. Looking at the other paragraphs, nothing in sub-paragraphs 36(4) or (5) assisted. Paragraph 37 applied only if there were a grant of a major interest. Mr Simpson accepted that the circumstances in sub-paragraphs 36(2) and (3) were mutually exclusive. Immediately prior to paragraph 36(2) the taxpayer must hold a major interest. The taxpayer either had this or it didn’t. If the taxpayer continued to hold a major interest after the transaction, then paragraph 36(2) had no application.
70. He also argued that the reference to “P’s interest, right on licence in the relevant premises held immediately prior to [the changeable event]” showed that P must be able to have an interest other than a major interest in the relevant premises. This made it clear, Mr Simpson contended, that paragraph 36(2) would not apply where, even following disposal of the major interest in respect of which zero-rating was granted, a taxpayer still had some interest in the relevant premises.

71. Accordingly, it is submitted that on a proper interpretation of paragraph 36(2) of Schedule 10, BC did not “dispose of [its] entire interest” in the subjects in question when carrying out the sale and leaseback transaction. It was noted that, by contrast, HMRC’s position depends on the fact that although the subject of a single contract (the missives), the two grants were the subject of separate conveyances (the disposition and the lease); and, it is assumed, in terms of abstract property law there must have been a *scintilla temporis* at which Target was in right of the full title to Huntly (albeit not a right *in rem*, as Target did not acquire this until the BC’s disposition was subsequently registered), and immediately thereafter granted to BC the real rights conferred by the lease.

Criticism of the Scintilla Temporis Point

72. As noted above, HMRC departed from the argument (advanced before the First-tier Tribunal, see paragraphs 47 and 49 of the Tribunal Decision), that there was a brief point in time - a *scintilla temporis* - when BC had wholly divested itself of its entire interest in the Huntly care home. For completeness, I should record what Balhousie had stated in reply in its skeleton argument, under reference to the case of Ingram v Inland Revenue Commissioners [2000] 1 AC 293. In Ingram, an inheritance tax planning exercise involved the conveyance of the English equivalent of the real right of ownership in certain land by the owner to her solicitor, receiving it as her nominee. Her solicitor then granted her leases of the land, and conveyed title into a trust for the benefit of the former owner’s descendants. The Inland Revenue Commissioners argued that the lease could not come into being until the land had been conveyed into the trust; and that therefore there had been a reservation of benefit engaging section 102 of Finance Act 1986. In the House of Lords, Lord Hoffmann gave the leading speech and stated (at 303):

“But the revenue’s version of reality seems entirely dependent upon the *scintilla temporis* which must elapse between the conveyance of the freehold to the donee and the creation of the leasehold interest in favour of the donor. For my part, I do not think that a theory based upon the notion of a *scintilla temporis* can have a very powerful grasp on reality.”

73. Lord Hoffmann then discussed the nature of the approach taken by section 102 Finance Act 1986 and continued (at 303 f.):

“If one looks at the real nature of the transaction, there seems to me no doubt that Ferris J. was right in saying that the trustees and beneficiaries never at any time acquired the land free of Lady Ingram’s leasehold interest. The need for a conveyance to be followed by a lease back is a mere matter of conveyancing form. As I have said, she could have reserved a life interest by a unilateral disposition. Why should it make a difference that the reservation of a term of years happens to require the participation of another party if the substance of the matter is that the property will pass only subject to the lease?”

74. Thus, Balhousie concluded, even in the context of a direct tax the proper approach is to consider the substance of linked conveyancing transactions rather than their form. HMRC’s position, which ultimately is that the *scintilla temporis* means that BC “dispose[d] of [its] entire interest” in the Huntly care home, is based wholly on the form of the transaction; and their approach leads to different results depending on whether the same effect is achieved by retention of the lesser interest out of a grant of the greater one, or the grant of the greater

interest followed by a grant of the lesser interest in return. This is precisely the approach rejected by Lord Hoffmann. It is an approach that makes no sense in the context of the provision of VAT law in issue in the present case.

Response to specific points made by HMRC

75. Balhousie noted that HMRC rely on the principle of statutory interpretation that where the same word is used throughout a statute there is a presumption that it has the same meaning each time, unless the context otherwise required: paragraph 5.8. “Major interest” and “entire interest” are not the same word. Indeed, it argued that the use of the term “entire interest” implies that if, following the disposal, the taxpayer still has any part of the interest previously acquired, paragraph 36(2) does not apply, whether or not what remains is a ‘major interest’. Conceptually, HMRC’s approach denies the possibility of disposals of part only of an interest: if HMRC are correct, in what circumstances is there a disposal of part only of an interest?
76. Turning to the issue of statutory purpose, HMRC suggest that all that can be said about the purpose of paragraph 36(2) is that the provision, “sets out the circumstances in which the recipient of a zero rated supply must account for the VAT on the original supply as output tax”. That is not its purpose. That, Mr Simpson argued, is what it does. The provision’s purpose is the end it is seeking to achieve by what it does. Ultimately, despite having proposed the legislation HMRC seem to be saying that they do not know what its purpose is. It is submitted that the policy of the provision is to support the primary policy of ensuring that the subjects are used for a relevant residential purpose for the necessary period, by ensuring a continuing link between their use and the taxpayer who benefited from zero-rating. This policy purpose is met by the First-tier Tribunal’s decision.
77. It is of course accepted that the reference to “interest” in paragraph 36(2) is a reference to the interest whose acquisition was zero-rated, and that ownership and the right of a lessee are each rights. However, it does not follow that a sale and leaseback transaction counts as “disposal of [the] entire interest”. Otherwise, the word “entire” would have no purpose or content. HMRC generally do not give any indication of what purpose or content it might have.
78. HMRC assert that Sargaison is irrelevant. In doing so, they do not address any of the reasons given by Megarry, J, for his decision, despite the fact that even if Sargaison did not exist those points would equally apply to the present case. Instead, HMRC refer to Southern Primary. The issue in that case was in a different context rendering it inapplicable. In addition, HMRC submit, in effect, that there is a material difference between the phrases “the whole of [the person’s] interest ... is transferred” and “the disposal of [the person’s] entire interest”, without explaining what that difference is.
79. Finally, HMRC assert that the interpretation taken by the First-tier Tribunal creates opportunities for avoidance, without explaining what they would consider to be avoidance in this context. This is important given HMRC’s case depends on drawing a distinction between (i) a transaction in which part only of an existing interest is transferred away and (ii) a transaction in which the whole of an existing interest is transferred away in circumstances such that part of it is immediately and inevitably transferred back. What opportunities for avoidance arise in (ii) that do not arise in (i)?

Response to the Case of Robert Gordon’s

80. If this case were decisive, Mr Simpson suggested that it was odd that it came so late. In that case, the context was dependent on whether there was a transaction, being a supply by someone else to the college. That case was concerned with input tax. If there was a VAT-able supply, by a third party developer, then the self-supply provisions were excluded. In that context the legislation did require that there was a VAT supply. That was not so, here. The case was distinguishable.

Motion

81. For the foregoing reasons it was submitted the Tribunal should refuse HMRC's appeal.

HMRC's Reply and the Parties' Supplementary Submissions

HMRC's Reply at the Hearing

82. Ms Roxburgh made some further points in her reply, as follows:-

- (1) She accepted that, as Mr Simpson pointed out, the word "disposed" was used in paragraph 36(2), not the word "supply". However, when dealing with supplies in relation to heritable property, in Group 5 of Schedule 8 to the Act, the word "grant" had been used and this was synonymous with "supply". This invited consideration with what each party had done with its entire interest. It was more natural to use the word "dispose" than "grant", as the former did not presuppose a monetary payment and so avoided any loopholes of a disposal by gift rather than sale. "Disposal" was intended to cover all transfers of the relevant interest.
- (2) Under reference to paragraphs 37(1) and 35(2), she argued that the relevant zero-rated supply is not restricted to the grant of a major interest. While item 1 of Group 5 of Schedule 8 to the Act concerned the grant of a major interest, the other items within that group covered other matters. The Self-Supply Charge could therefore arise on a self-supply of these types of supplies (ie the other items in Group 5) as well as that of a major interest (ie item 1 of Group 5).
- (3) She argued that "right" was used in two senses: a "real right" (as that was understood in Scots law) but also as a component part of a real right. "Major interest" was defined in relation to real rights. This was illustrated by the case of Ingram. In that case, the court had looked at the taxpayer's rights arising from her status as tenant, not owner. These were separate rights. The case of Ingram was against BC. Any right (eg of occupation) that BC had at the end of the arrangements arose *qua* tenant, not as owner. Accordingly, it had disposed of its entire interest even if it had acquired a separate interest.

83. There was a degree of confusion toward the end of submissions about some of the examples drawn from the items in Group 5. Having regard to this, to the lateness of the hour, and to the fact that HMRC was responding to what was said to be a new argument, made under reference to paragraph 37(1) (which I have set out at paragraph [70]). I suggested that this be dealt with by way of brief, written supplementary submissions. These are summarised in the following paragraphs.

HMRC's Supplementary Submissions

84. HMRC argued that the phrase in question was in place to recognise the fact that a Self-Supply Charge may arise not only in respect of the grant of a major interest in land but also in respect of any other supply which has been the subject of zero-rating in terms of Group 5 of Schedule 8 of VATA.
85. Under reference to paragraph 35(1), Ms Roxburgh argued that a Self-Supply Charge may arise in respect of (i) “a grant” and (ii) “any other supply which relates to a building” intended for a relevant purpose, and which has been zero-rated as a result of Group 5 in Schedule 8 to the Act. The reference to “a grant” is to the first grant of a major interest in accordance with item 1 of Group 5. The reference to “other supplies” is to the supplies outlined in items 2 to 4 of Group 5. An example would be the services of a building contractor to construct the relevant premises in accordance with item 2 of Group 5. Furthermore, she argued that item 2 of Group 5 was of particular importance. It provided that:

“The supply in the course of construction of –

- (a) A building designed as a dwelling or number of dwellings or intended for use solely for a relevant residential purpose or a relevant charitable purpose; or
- (b) Any civil engineering work necessary for the development of a permanent park for residential caravans,

of any services related to the construction other than the services of an architect, surveyor or any person acting as a consultant or in a supervisory capacity.”

Accordingly, item 2 allowed a party that constructs a building to receive zero-rated supplies. This is the case whether that party is the owner of the premises or not. Where the party constructing the building is not the owner, that party’s interest in the premises may be a lease, a licence or some other contractual right. An example is where a university constructs student accommodation on land owned by a local authority. In those circumstances, the university will often have a licence to occupy the site for a specified period of time.

86. Returning to the terms of paragraph 36(1), it was contended that the combined effect of paragraphs 35 and 36(1) was that, where the conditions in paragraphs 36(2) or (3) are met, paragraph 37 will apply in respect of each relevant zero rated supply. It can therefore be seen that paragraph 37 is intended to apply not only to circumstances where a first grant of a major interest has been zero-rated. It is also intended to apply whether other zero-rated supplies have been made.
87. The terms of paragraph 37(1) were then considered. This was a deeming provision, and, where the requirements of paragraph 36 were met, the person who received the zero-rated supply is treated as making that zero-rated supply to himself immediately prior to the chargeable transaction. Viewed in context, it was clear that the reference to “P’s interest” is a reference to any major interest the grant of which was the subject of zero-rating. This is consistent with the definition in section 96 of Act, which she had addressed in her principal submissions. By contrast, the reference to “right or licence” is intended to describe the right of a person who constructed a building on land it did not own. As just argued, that person may have received zero-rated supplies in terms of items 2 to 4 in Group 5. The width of the language was, she argued, indicative of the fact that the legislature was looking to cover all the grounds for occupation which could arise.

88. In either scenario the legislature was looking to provide that, on the requirements of paragraph 35 and 36 being met, the original zero-rated supply is to be treated as being supplied by the person with the interest in the relevant premises to himself. Where the supply in question is the grant of a major interest in terms of item 1 of Group 5, the supply will be of P's interest itself. However, where the supply comes within any of the other items, the deemed supply is the supply that was made in relation to P under that item.
89. While the provision might have been better expressed, to interpret the wording in the manner proposed by Balhousie, would mean that a Self-Supply Charge could only ever apply to the supply of an interest in property. As such, it would be confined to supplies made under item 1 of Group 5. This was clearly not the intention of the legislature.
90. HMRC's interpretation is supported by the wording in paragraph 37(2) which provides that: "The supply is taken to be a taxable supply which is not zero-rated as a result of Group 5 of Schedule 8." Accordingly, it was implicit in this provision that the supply might otherwise have come within the category of supplies for which zero-rating could be claimed. This could only be the case for supplies that were subject to zero-rating under items 2 to 4. Any deemed supply of an interest in property could not be a first grant given that there was a previous grant which was zero-rated. HMRC drew further support from the formula used to calculate the charge to VAT contained in paragraph 37(3) and (4). Y in the equation is defined in paragraph 37(4)(b) as:

"Y is the amount that yields an amount of VAT chargeable on it equal to—

- (i) the VAT which would have been chargeable on the relevant zero-rated supply, or
- (ii) if there was more than one supply, the aggregate amount of the VAT which would have been chargeable on the supplies,

had the relevant premises not been intended for use solely for a relevant residential purpose or a relevant charitable purpose"

91. HMRC made two further points: first, the reference again to the "relevant zero-rated supply" showed that Parliament was looking back to the original zero-rated supply; and secondly, it is clear that paragraph 37 was not to be restricted only to supplies of a major interest in property but to all supplies coming within the definition in paragraph 35(2). For those reasons, the reference to "right or licence" in paragraph 37(1) does not support Balhousie's interpretation of paragraph 36(2).

Balhousie's Supplementary Submissions

92. In the supplementary submission it was recognised that the broad wording of paragraph 37(1) of Schedule 10 to the Act may be intended to ensure that the withdrawal of zero-rating also takes effect in relation to items 2 to 4 in Group 5 of Schedule 8 to the Act. Balhousie offered the following points:
- (1) First, HMRC assert that the term "interest" in paragraph 37(1) means "major interest": paragraph 3.3. This it was argued, is plainly incorrect. For example, Group 1 in Schedule 9 to the Act exempts certain transactions involving land and buildings from VAT. It applies to, "The grant of any interest in or right over land or of any licence to occupy land, or, in relation to land in Scotland, any personal right to call for or be granted any such interest or right, other than [exceptions]." Balhousie argued that it was clear that in this provision, "interest" does not mean "major interest". Therefore, there is

no reason to suppose that “interest” in paragraph 37(1) of Schedule 10 (or indeed in paragraph 36) meant “major interest”.

- (2) Moreover, the wording of paragraph 37(1) clearly, at least, allowed for Balhousie’s interpretation of paragraph 36(2). As HMRC had submitted to the Tribunal (and indeed to the First-tier Tribunal, though it is suggested that in their reply at the hearing on 24 April 2017 HMRC asserted the contrary) paragraph 36(2) operated so as to require a comparison of the rights the taxpayer holds before and after the transaction(s) in question. “Rights” in this context meant the rights that, together, make up whatever “overall” right the taxpayer has in the land or buildings whose supply has been zero-rated; so, for example, a right of possession on the basis of ownership is treated for the purposes of paragraph 36(2) as the same as a right of possession under a lease. If, after the transactions in question, the taxpayer holds any of the rights it had before the transaction, then paragraph 36(2) does not apply, regardless of the form in which this has come about (thus, taxpayers in the same substantive position are treated equally, substance being given precedence over form). Otherwise, the word ‘entire’ has no purpose. But the taxpayer may have something less than a major interest after the transaction; and accordingly, the extended scope of paragraph 37(1) to “[any] interest, right or licence” allows for paragraph 36(2) to be considered each time the taxpayer reduces the (specific) rights it has in relation to the building in question.

93. In any event, regardless of any inference that may be drawn from paragraph 37(1) it is submitted that the interpretation of paragraph 36(2) put forward on behalf of the Respondent is the correct one.

Discussion

The Proper Approach to the Interpretation of a Tax Statute

94. Both parties submitted that the courts have moved from a literal to a purposive approach in the interpretation of taxing statutes. This is undoubtedly, if unremarkably, the case: see, eg *per* Lord Reed in UBS at paragraphs 62 and 68. The former passage confirms (following WT Ramsay Ltd v Inland Revenue Commissioners [1982] AC 300), that the purposive approach to statutory construction is extended to taxing statutes, and that the “analysis of the facts depended on the purposive construction of the statute”. In the second passage Lord Reed observed, as follows:

“68 Secondly, it might be said that transactions must always be viewed realistically, if the alternative is to view them unrealistically. The point is that the facts must be analysed in the light of the statutory provision being applied. If a fact is of no relevance to the application of the statute, then it can be disregarded for that purpose. If, as in *Ramsay*, the relevant fact is the overall economic outcome of a series of commercially linked transactions, then that is the fact upon which it is necessary to focus. If, on the other hand, the legislation requires the court to focus on a specific transaction, as in *MacNiven* and *Barclays Mercantile*, then other transactions, although related, are unlikely to have any bearing on its application.”

95. In UBS Lord Reed traced the significance of Ramsay as heralding a purposive approach to the interpretation of tax statutes, “the essence” of which was “to give the statutory provision a purposive construction in order to determine the nature of the transaction to which it was intended to apply”: Barclays Mercantile, quoted at paragraph 36 of UBS. Lord Reed also

cited the observation that “[t]he paramount question always is one of interpretation of the statutory provision and its application to the facts of the case” (being an observation of Lord Nicholls in MacNiven v Westmoreland Investments Ltd, quoted in Barclays Mercantile.) There is nothing to suggest that these observations were confined to direct tax legislation. The purposive approach is the same regardless of the subject-matter of the legislation concerned, but the statutory purposes of the different statutory regimes are likely to be different. It should be borne in mind that UBS was concerned with direct tax. This distinction is relevant. At paragraphs 64 to 68 of UBS Lord Reed was discussing the post-Ramsay approach in the particular context of avoidance schemes in direct taxation cases, and in which consideration of the overall effect of a composite transaction formed part of the assessment. This was because, as Lord Reed explained at paragraph 64, tax avoidance schemes commonly included elements inserted that had no business or commercial purpose, but which had been intended to have the effect of removing transactions from the scope of the particular tax charge. The observations at the end of paragraph 68, founded upon strongly by Mr Simpson, must be understood in this context. The observation that transactions “are to be viewed realistically” is integral to the kind of assessment under consideration in that case. The implication of Mr Simpson’s focus on this passage, and his argument for a “realistic” analysis of the arrangements between BC and Target (which he equated with their overall effect), was that the approach by HMRC was not consistent with this. However, on a careful reading, the last two sentences of paragraph 68 of UBS describe different types of statutory taxing provisions. Not all taxing statutes require consideration of the “overall outcome of a series of commercially linked transactions”. HMRC argue that VAT is a particular type of tax attracting a specific approach, (ie it was one falling within the last sentence of paragraph 68 of UBS). I did not understand Mr Simpson to demur from that proposition. I turn to consider the proper approach to VAT.

The Proper Approach to VAT

96. Ms Roxburgh emphasizes that VAT is a transaction tax and in support of this proposition she referred to the decision of the Court of Appeal in Southern Primary. In that case, which also concerned VAT in relation to a supply of land, the taxpayer argued that the input tax it incurred in the purchase of land for development was recoverable. The land purchase was one of three linked transactions: the other two being the taxpayer’s subsequent sale of the land to a housing association and the building contract entered into between the taxpayer and that housing association for the development of the land. It was accepted in that case that the three transactions were commercially connected. HMRC rejected the taxpayer’s contention that input tax was recoverable on the purchase of the land. The taxpayer appealed and its argument was accepted by the tribunal and also on the Commissioners’ appeal from the tribunal. The Court of Appeal, however, found in favour of HMRC. Miss Roxburgh founds on the observations at the end of that case (at paragraph 37) but, as there are similarities in that case to the argument presented here (based on the commercial reality and composite character of the transactions concerned), it may assist to see those comments in their wider context.
97. In Southern Primary HMRC argued that the tribunal had fallen into the following (among other) errors. It
- “(a) focused on the taxpayer's overall commercial aim;
 - (b) treated the two separate supplies as if they were one;
 - [...]
 - (d) applied a test of attribution for which there is no authority — namely whether the input *enabled* the taxpayer to make a taxable supply;

- (e) failed to appreciate that the taxpayer's use of the land was exhausted on its sale and the land could not thereafter be attributed to construction works carried out thereafter.”

98. On behalf of the taxpayer it had been argued that there was no “illegitimate focussing on the overall commercial aim” and that “the intention to use the land for the purposes of the building contract was not just a future intention to use the land for taxable purposes, it was essential for those taxable purposes”. (Paragraph 30.) Jacobs LJ agreed (at paragraph 31) that the “case does not turn on the overall commercial aim point”. However, he noted that there was substance in the Commissioners’ points, particularly point (d), above. He found (at paragraph 32) that there was a there was a link of the taxpayer’s acquisition of the land “with the contract but the link was not direct and immediate” and so did not satisfy the “cost component” test. He continued (at paragraph 33) as follows:-

“... There is nothing about the development contract as such which makes the land purchase and sale essential. If the housing association had already owned the land or had bought it from some third party, the inputs of the development contract would have been just the costs of carrying it out. The fact that there were commercially linked land transactions does not mean that those transactions are directly linked to the costs of the development contract. One would not say that the cost of buying the land was a cost of the development contract itself. It follows that the input tax on that cost is not a cost of the contract.”

99. He proceeded to develop that reasoning:

“34. Other guidance from the ECJ supports that conclusion. Thus in *BLP* para. 26 the Court reaffirmed the principle of neutrality — namely that “all economic activities, whatever their purpose or results, are taxed in a wholly neutral way”. That principle would be violated if this development contract were taxed differently from an exactly similar “freestanding” contract.

35. Again if one applies the “fundamental principle” that “VAT applies to **each transaction** by way of production or distribution of deduction of the VAT directly borne by the various cost components” (*Midland* para 29) one is driven to ask whether the land purchase price is a cost component of the development contract — which to my mind it is obviously not. And, if one adapts *Midland* para.30 to the case the test is whether the expenditure on the land purchase was part of the costs of the development contract which used the land acquired. It did not. The carrying out of the development was on the land acquired, but did not utilise the land, whose ownership was irrelevant. [.....]

36. *Midland* para. 31 is also in point — there the Court said that lawyers' fees were not “generally part of the costs of the output transaction” and “therefore” did not have any direct and immediate link with the output transaction.” Again the Court is focussing **on the objective, transaction-by-transaction nature of VAT law**. The price of a land purchase is not “generally” part of the costs of a development contract and therefore does not have any direct and immediate link with it.” (Emphasis added, in bold; underlining in original.)

100. Jacobs LJ applied these principles to the facts of the case before him. “Turning back to the Tribunal”, he said, at paragraph 37

“...it concluded that there was a direct and immediate link between the land purchase and both the land sale and development contract, with both an exempt and a non-exempt transaction. **VAT law does not work in such a generalised way. You have to look at transactions individually, component transaction by component transaction.** They may be linked in the sense that one would not have happened without the other, but **they remain distinct transactions nonetheless.** Only if one transaction is merely ancillary to a main transaction can one disregard the distinct nature of each transaction (see *Card Protection Plan v CCE (Case C-349/96)*[1999] STC 270, para. 29). If that were not so, the principle of neutrality would be violated. Moreover there would be intractable problems as to which input was being attributed to which part of the “overall transaction”. You may find, as here, taxable and exempt transactions all mixed up in the same “overall” transaction — which is illegitimate.” (Emphasis in bold added; underlining is in the original.)

101. There is, in my view, considerable force in these observations, which emphasize that for the purposes of VAT one looks “at transactions individually, component transaction by component transaction”. Further support for this, if needed, is to be found in the observations of Lord Hoffmann in Robert Gordon’s at pages 1099j to 1100e, which observations are themselves predicated upon a decision of the ECJ in BLP Group plc. In Robert Gordon’s, the Inner House of the Court of Session had allowed the taxpayer’s appeal, doing so in part by taking into account “the totality of the transactions” concerned. On HMRC’s appeal, the House of Lords found that approach to be wrong in law. Lord Hoffman referred to BLP, which had been issued after the Inner House’s decision. In BLP the ECJ emphasised that each transaction in a “chain of transactions” (imagery suggested in the Advocate General’s opinion in that case) must be examined separately to ascertain objectively what input tax or output tax was deductible and payable. Commenting on that case, Lord Hoffmann observed:

“that decision makes it clear that for the purposes of European VAT legislation, it is **not permissible to take a global view of a series of transactions in the chain of supply.** In considering whether or not the college used the land as a service supplied by a third party, it is irrelevant that it had developed the land at an earlier stage.” (Emphasis added.)

In the context of VAT, and perhaps in contradistinction to other forms of tax (eg the types of taxes at issue in UBS (income tax) or in Sargaison (capital allowances)), this approach is in my view the correct one. In any event, the conventional transactional approach applied to VAT should not be subsumed into an approach that gives primacy to the “commercial reality” or the “overall effect” of a transaction, if the relevant taxing statute does not enjoin that approach. It is in my view clear from the first paragraph of the Tribunal’s own discussion (at paragraph 66 of the Tribunal Decision) that it was deflected from the correct approach. This error led the Tribunal to treat the overall arrangements as the relevant transaction: see paragraphs 67 to 69 and 71 of the Tribunal Decision. I should note that the Tribunal did not have the benefit of as full a citation of authorities as I have had and, in particular, the case of Robert Gordon’s had not been cited to it. For completeness, I should add that no argument was advanced on the basis of, Card Protection Plan Ltd v Customs and Excise Commissioners [1999] 2 AC 601.

102. While dealing with the parties’ submissions about the proper approach to taxing legislation, I should address Miss Roxburgh’s proposition that zero-rating, as an exception to VAT, should be construed narrowly. As a generality, I accept this is correct and that proposition may

properly inform the scope of what falls within a zero-rated supply. It was less obvious as to how this proposition is to be applied, if at all, in the different context of construing the provisions governing the circumstances in which a particular tax treatment might be lost. I have therefore not applied that proposition in determining the essential question which is: what is the proper interpretation of paragraph 36(2) of Schedule 10 to the Act?

103. Finally, it is here convenient to address parties' submissions based on the documents offered as external aids to construction (Hansard, the Explanatory Notes to the 2011 SI, the HMRC Briefing Note no 49/10 and VAT Notice No 708 (the latter two items I refer as "the HMRC materials")). I found none of these to be of assistance. Paragraphs 35 to 37 in Part 2 of Schedule 10 were substituted by the VAT (Buildings and Land Order, SI 2011/86) ("the 2011 SI"), with effect in relation to buildings completed on or after 1 March 2011. It is generally impermissible to refer to Hansard to construe a statute. I am not persuaded that this case is within one of the exceptions to that general prohibition. In any event, the passages in Hansard dating from 2011 do not address themselves comprehensively to these substituted paragraphs. To the extent there is comment on the specific subject-matter of the paragraphs to be inserted, they focus on a change of use. It is obvious, though, that the circumstances potentially capable of triggering a charge to tax in the new paragraph 36 are not confined to a change of use. This necessarily follows from the fact that there are two sets of circumstances potentially giving rise to the charge to tax (in paragraph 36(2) and (3)); that these are mutually exclusive; and that only one of these concerns a change of use from one of the relevant purposes. The comments in Hansard are therefore not co-extensive with the subject-matter of the proposed paragraphs. They are therefore an unsafe, or incomplete, guide to the purpose of the amendments effected by the 2011 SI. It is for this reason that Balhousie's reliance on Hansard as an external aid to construction, to support the contention that the statutory purpose is confined to use, is unconvincing, for it fails to address the terms of paragraph 36(2).
104. Mr Simpson did not go so far as to argue that the supposed statutory purpose as gleaned from Hansard, and which he said emphasised the issue of use, could be invoked to override or ignore the terms of paragraph 36(2). In my view, such an argument would be impermissibly to disregard the statutory words Parliament used in favour of comments which, when made in the context of introducing an amendment, may not have been –and in terms of the subject-matter of paragraph 36(2) of Part 2 of Schedule 10, clearly were not- comprehensive in their discussion of the purpose of the proposed amendments. It follows that the Tribunal erred in law in the manner in which it identified the statutory purpose, or confined that purpose solely to the issue of change use (see paragraph 71 of the Tribunal Decision).
105. Even were it permissible to take into account the passages in Hansard, to the extent that there was a statutory purpose for Part 2 of Schedule 10 to be gleaned, those purposes are, as Ms Roxburgh contended (at paragraph [30] above), "fairness and certainty", and to "minimise risks arising on disposal" of a whole interest on sale. In respect of those purposes, I accept Ms Roxburgh's submission, based on the case of Astall, that these purposes are expressed at such a level of generality as to afford little guidance on the particular phrase ("entire interest") under consideration.
106. For completeness, I should state that I found the other external aids to interpretation to be uninformative. Further, the HMRC materials simply record HMRC's view of the legislation and are of course not binding.

Paragraph 36(2) in the Context of Part 2 of Schedule 10 to the VAT Act 1994

107. Before turning to consider the proper interpretation of paragraph 36(2) of Schedule 10 to the Act, it is helpful to consider the statutory context in which that provision appears in Part 2 of Schedule 10.
108. A supply comprising the construction and first supply of certain types of buildings (eg for residential use) is generally an exempt supply (see item 1 of Group 5 of Schedule 8 to the Act). Part 1 of Schedule 10, which is headed up “Buildings and Land”, makes provision for the option to tax certain supplies of this character which would otherwise be exempt. Part 2 of Schedule 10, headed up “Residential and Charitable Buildings: Change of Use etc.”, includes paragraphs 35 to 37. Paragraph 36 falls to be considered as part of this small cluster of provisions.
109. Paragraph 35 defines the scope of application of Part 2 of Schedule 10. It concerns “relevant zero-rated supplies” of a building to a person (“P”) (paragraph 35(1)), and which was intended for use solely for a “relevant residential purpose” or a “relevant charitable purpose” (paragraph 35(2)) (hereinafter collectively referred to as the “relevant purposes”). The “relevant premises” are defined as meaning the buildings (or part) “in relation to which a zero-rated supply has been made to P” (paragraph 35(2)). The “relevant zero-rated supply” therefore comprises two parts: (i) the “grant or other supply which relates to a building”, and (ii) which was “intended for use solely for” one of the relevant purposes. Having regard to its terms, it is in my view clear that paragraph 35 is concerned with the original zero-rated supply. I accept Ms Roxburgh’s submission to this effect.
110. Passing over paragraph 36 for the moment, I note that paragraph 37 is headed “Charge to VAT”. Where the charge to tax is triggered, by the occurrence of one or other of the two circumstances set out in paragraph 36(2) or (3), paragraph 37 creates a deemed supply to P (see paragraph 37(1)), which is treated as a non-zero-rated taxable supply (paragraph 37(2)). Paragraph 37 sets out (in paragraph 37(3) and (4)) the formulae, and ancillary matters, for determining the value of that deemed supply. It is envisaged that the charge to tax may be triggered more than once: see paragraph 37(1), which applies “on each occasion during the relevant period...”. The formulae in paragraph 37 is different depending on whether the charge is triggered by the “first deemed supply” under paragraph 37 (in which case it is that set out in paragraph 37(3)(a)) or by “any subsequent deemed supply” (in which case the formula in paragraph 37(3)(b) applies). The purpose of the formula is to ascertain the value of the deemed supply (paragraph 37(3)) by identifying the relevant proportion of the VAT that would have been chargeable on the relevant zero-rated supply (or supplies, if more than one: see paragraph 37(4)(i) and (ii)). From all of this, it is clear that the value is necessarily calculated by reference to the original supply (“the relevant zero-rated supply”). Again, this reinforces Miss Roxburgh’s submission that what Part 2 of Schedule 10 is concerned with is the original zero-rated supply.
111. It can be seen, therefore, that Part 2 of Schedule 10 comprises a short anti-avoidance code. Its scope is defined in paragraph 35, and the charge to tax is set out in paragraph 37. The circumstances giving rise to the charge are those identified in paragraph 36(2) and (3). I turn to consider paragraph 36 in more detail.

The Proper Interpretation of Paragraph 36(2)

112. Parties were agreed that the circumstances in sub-paragraphs 36(2) and (3) are mutually exclusive. In any event, that follows from the words in sub-paragraph 36(3)(a): “those premises do notfall within sub-paragraph (2)”. While this was not formally agreed, both

parties accepted that paragraph 36(3) was concerned with a change of use from the relevant purposes. Logically, sub-paragraph 36(2) must necessarily relate to something other than a change of use of the relevant premises. Given the scope of paragraph 35, and given that the impact of a change from one of the relevant purposes is provided for in paragraph 36(3), then paragraph 36(2) is likely to be concerned with the other circumstance giving rise to a potential charge to tax, namely a subsequent disposal of P's entire interest in the relevant premises which were the subject of the "relevant zero-rated supply".

113. The trigger in paragraph 36(2) to a charge to tax is a "disposal of P's entire interest in the relevant premises (or part)". The reference to "P" points the reader back to the "relevant zero-rated supplies", as defined in sub-paragraphs 35(1) and (2). The starting point therefore is a consideration of the original supply which attracted zero-rating as a consequence of the option to tax. In this case, that is the supply of the Huntly care home by a third party to BC.
114. The question is whether the subsequent arrangements entered into by BC did or did not fall within paragraph 36(2). The fundamental difference in approach between the parties is whether those arrangements are viewed as a composite transaction the net result of which was that BC regained a relevant interest in the Huntly care home under the lease, and on which approach it was not necessary to be concerned with any intermediate steps (as BC contended and the Tribunal accepted), or whether each individual transaction within those arrangements (including *inter alia* the disposition) was subject to a distinct VAT analysis (HMRC's position). While at the outset of the hearing before me Miss Roxburgh abandoned the *scintilla temporis* argument, the argument she presented adhered to the transactional approach which formed part of HMRC's argument to the First-tier Tribunal. For the reasons already stated, *prima facie* HMRC's approach is more consistent with VAT as a transactional tax on taxable supplies.
115. In relation to Mr Simpson's contention (recorded at paragraph [64], above) that paragraph 36(2) does not use the word "supply", I accept as correct Ms Roxburgh's argument (recorded at paragraph [82(1)], above) that "disposal" was intended to cover all transfers of the relevant interest. Such a transfer may, or may not, constitute a supply. That, it seems to me, is consistent with this as an anti-avoidance provision.
116. Turning to the phrase "entire interest", Balhousie argues that this must mean something other than "major interest". I agree, but this does not necessarily lead to the outcome for which Balhousie contends.
117. Mr Simpson argues that "entire interest" means something other than "major interest" and, he says, this invites a wider scope such as to enable consideration of the net effect of a series of transactions. One, in fact, disregards the individual transactions viewed in isolation, but (in the name of a realistic as opposed to an artificial approach) looks at their overall effect or end result. If at the end of these arrangements the taxpayer still holds some interest in the subjects, he has not disposed of his entire interest. In my view, the question toward which paragraph 36(2) is directed is whether the taxpayer has disposed of its entire interest, but that necessarily includes consideration of the character of the interest said to have been disposed in its entirety. For the purpose of a relevant zero-rated supply falling within item 1 of Group 5 to Schedule 8 of the Act, one is concerned with a disposal of what had been a "first grant...of a major interest...in the building". Accordingly, the correct question in respect of a relevant zero-rated supply of that character, is whether P has disposed of its entire interest in the major interest comprised of that relevant zero-rated supply.

118. I accept Ms Roxburgh’s submission that paragraph 36(2) is directed at all types of zero-rated supplies provided for in Group 5 of Schedule 8 of the Act, and not just to item 1. Mr Simpson accepted this. In that context, it is helpful to recall that in terms of section 96, in Scotland, a “major interest” can only be in two forms: the interest in heritable property *qua* owner and the interest of a tenant under a lease of not less than 20 years.
119. Furthermore, it is correct, as Mr Simpson contends, that there may be a bundle of rights or interests encompassed within a major interest. So, for example, the pre-eminent characteristics of ownership are a right to exclusive possession and an unfettered power of disposal. There are, of course, lesser dealings that an owner of heritable subjects which were acquired by a relevant zero-rated supply may engage in, such as a grant of a lease (Mr Simpson’s first scenario), and which would not result in the owner divesting himself of his “entire interest” in those heritable subjects. Balhousie’s argument is, in effect, that because the right BC had as a result of the composite arrangements (ie a right of occupation under the lease) was the same as one of the rights it enjoyed before those arrangements (being occupation as an incidence of ownership), there had been no disposal of BC’s entire interest in the Huntly care home. In my view, the fallacy in this approach is to conflate the similarity of those rights, but to disregard their source. The crucial difference is that, as a result of the arrangements, BC’s right of occupation was derived from the lease. While that right might in practical terms mirror the right of occupation BC had as one of the incidents of ownership, there was a critical disjunction, in that BC no longer derived that right of occupation from the supply that had constituted the relevant supply. Accordingly, if one compares the rights BC held both before and as a consequence of the composite arrangements, as Balhousie suggests, BC no longer enjoys any rights flowing from the original or relevant zero-rated supply. It may have a right of occupation, but this now flows from the lease, not from the original disposition.
120. Applying this construction to the facts, it is in my view undoubtedly the case by the disposition of the Huntly care home to Target, BC “disposed of its entire interest” in the Huntly care home. It matters not, in my view, that by a further linked transaction it acquired under the lease a right of a similar character. That outcome does not result in an unrealistic or artificial approach divorced from reality. It flows from the terms of paragraph 36(2), properly construed. I have already identified (in paragraphs 101 and 104, above) the Tribunal’s errors in law that lead it to the opposite conclusion.
121. It follows that I allow HMRC’s appeal.

LADY WOLFFE

RELEASE DATE: 20 October 2017

