[2019] UKUT 0072 (TCC)

Appeal number: UT/2018/0139

VAT – option to tax under Part 1 Schedule 10 VATA – whether disapplication provisions in paragraphs 12 to 17 applied on the basis that land was exempt land – circularity of statutory provisions – anti-avoidance – "intention" or "expectation" of "relevant transferee" – appeal dismissed

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

ON APPEAL FROM THE
FIRST-TIER TRIBUNAL (TAX CHAMBER)

DAVID MOULSDALE
t/a MOULSDALE PROPERTIES

Appellant

v

THE COMMISSIONERS FOR HER MAJESTY'S
REVENUE AND CUSTOMS

Respondents

TRIBUNAL: LORD ERICHT
JUDGE DEAN

Sitting in public at George House, 126 George Street, Edinburgh on 30 October 2019

Philip Simpson QC, for the Appellant (David Moulsdale t/a Moulsdale Properties)

Mr David Thomson QC and Ms Elisabeth Roxburgh, Advocate, instructed by the Office of the Advocate General for Scotland, for the Respondent (HMRC)

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DECISION

The issue in the present appeal

1. The appeal before the F-tT concerned the Respondents' decision dated 16 March 2017 that the sale of the property at 5 Deerdykes Road, Cumbernauld ("the property") was a taxable supply for the purpose of VAT as the requirements of paragraph 12 of Schedule 10 to VATA 1994 were not met with the result that the option to tax made by the Appellant in respect of the property was not disapplied and the property was not exempt from VAT.

2. The Appellant appealed against the decision to the F-tT, which dismissed the appeal. The F-tT considered that, in applying the terms of Regulation 113(1) of the VAT Regulations, the Appellant could not have intended or expected that the property would become a capital item in the hands of the purchaser and the disapplication provisions were not engaged. The Appellant now appeals to the Upper Tribunal against the F-tT's decision.

3. The issue in the present appeal is whether an option to tax made by the Appellant in respect of a property is disapplied by the provisions in Schedule 10 VATA 1994 so that the supply of the property by the Appellant is exempt from VAT.

Background and F-tT Decision

4. The appeal proceeded on the following Statement of Agreed Facts:

> 1. On or about 3 May 2001 the Appellant purchased a property at 5 Deerdykes Road, Westfield, Cumbernauld (the "Property"). The vendor had opted to tax the Property. The Appellant did not opt to tax the Property prior to the purchase. The purchase price of the Property excluding VAT was £1,140,000. VAT was £199,500. The VAT Return that included the purchase is that for period (06/01). The Appellant received a VAT repayment of £195,455.22 pursuant to the completed VAT 20 Return.
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> 2. The Appellant subsequently opted to tax the Property on or about 9 May 2001.
>
> 3. On or about 11 September 2001 the Appellant leased the Property to Optical Express (Westfield) Limited ('OEWL'). At all material times, OEWL's occupation of the property has not been wholly, or substantially wholly, for eligible purposes.
>
> 4. OEWL was a person connected with the Appellant for the purposes of Schedule 10 of VATA 1994 at all material times.
>
> 5. Throughout the period to 2007, the Appellant continued to account for output tax on the lease of the Property to OEWL. In 2007 following a VAT visit the Appellant became aware that the grant of the lease and subsequent supplies under it should be treated as exempt supplies by virtue of Schedule 10 of VATA. The Respondent advised the Appellant that the Appellant was entitled to revisit the last three years and the Appellant sought repayment of output tax charged to OEWL for the period which was not time barred under the three year capping restrictions. On or around 2 September 2014 the Appellant sold the Property to Cumbernauld SPV Limited ('CSPV'). The Property was sold subject to the lease in favour of OEWL. The price was £1,149,374. 35

6. CSPV is not a person connected with the Appellant for the purposes of Schedule 10 of VATA. CSPV did not advise HMRC of an election to waive exemption on the Property prior to purchasing the Property. CSPV was not VAT registered at that time nor has it subsequently become VAT registered."

5. Grants of land generally give rise to exempt supplies for VAT purposes, under Group 1 of Schedule 9 VATA. Part 1 of Schedule 10 VATA provides for a person to "opt to tax" any land. Where an option is exercised effectively, grants made in relation to the land at a time when the option has effect do not fall within Group 1 of Schedule 9 VATA and therefore give rise to taxable supplies.

6. Although there are no authorities addressing the specific issue in this appeal, the parties cited a number of cases of relevance. *PGPH Ltd v Revenue & Customs Commissioners* [2017] UKFTT 782 (TC) (at [6] – [9]) provides a clear explanation of the relevant provisions as follows:

"The option to tax provisions reflect Article 137 of Directive 2006/112/EC (the "Principal VAT Directive"), which permits Member States to allow a right of option for taxation in respect of certain supplies, including supplies of land and buildings. Article 137(2) provides that Member States may restrict the scope of this right. The UK has chosen not only to allow an option to tax but also to restrict it pursuant to Article 137(2). The domestic law provisions which give effect to this restriction are those in paragraphs 12 to 17 of Schedule 10, entitled "Anti-avoidance". Their effect is to prevent an option to tax rendering supplies taxable where certain conditions are met. Despite the title, the conditions set out do not include any tax avoidance purpose.

Paragraph 12(1) is the main operative provision. It provides:

"A supply is not, as a result of an option to tax, a taxable supply if-

(a) the grant giving rise to the supply was made by a person ("the grantor") who was a developer of the land, and

(b) the exempt land test is met."

Both conditions (a) and (b) are in dispute in this case, that is whether PGPH was a "developer" and whether the "exempt land" test was met.

Paragraph 13 effectively defines developer by describing when a grant is made by a developer for the purposes of paragraph 12. Under paragraph 13(2) this test is met if the land "is, or was intended or expected to be, a relevant capital item" and the grant is made at an "eligible time as respects that capital item". The remainder of paragraph 13 expands on these concepts…The effect of paragraph 13(4) is that the relevant intention or expectation must be that of the grantor or a development financier... Although not explicit in paragraph 13 HMRC accepted, and the Appellant did not dispute, that the time at which the intention or expectation must exist is the date of the grant.

Regulation 113 of the VAT Regulations lists the items which are to be treated as capital items. The list includes a building or part of a building on which capital expenditure with a value of not less than £250,000 is incurred on acquisition, construction, refurbishment, fitting out, alteration or extension. It was accepted by both parties that "value" in this context means the VAT exclusive cost."

7. The parties agreed that the legislative provisions are circular. On the issue of circularity, the F-tT explained at [4]:

> "In summary, the circularity can arise where a taxpayer wishes to sell an opted building, or land, but at the point of sale the building or land is not a capital item in the Capital Goods Scheme ("CGS") for the seller. However, if the sale price exceeds £250,000 and is subject to VAT because of the option to tax, it has the potential to become a capital item in the hands of the purchaser and that is relevant in terms of the legislation. In circumstances such as where the "exempt land test"… is met the seller's option to tax is potentially disapplied rendering the supply exempt. However, that can result in circularity since, if the supply is no longer taxable, for the reasons set out below, a capital item in the CGS would not be created and therefore the supply then becomes taxable."

8. As noted by the F-tT at [44]:

> "The unfortunate drafting of these legislative provisions can achieve the opposite result rendering a normal commercial transaction, where there is an option to tax, exempt. The circularity is to be deplored."

9. The difficulty recorded by the F-tT was that both parties invited it to construe the legislation purposively, however the purpose of the provisions was not clear. Having considered the statutory provisions and the material before it, the F-tT concluded at [37], [38] and [43]:

> "The appellant correctly, and conscious of its obligations in terms of VATA, considered the relevant taxing provisions. The starting point is that having opted to tax, the supply should bear tax. However, it can only do so if the option to tax is not disapplied. That is the relevance of the provisions of Schedule 10. Looking back at paragraph 12(1)(b), the supply will not be taxable if the "exempt land test" is met.
>
> The appellant then quite properly looked at paragraph 15. The property was occupied by a relevant person, which was OEWL which was connected with the appellant, but not the purchaser. As can be seen from paragraph 3 of the Statement of Agreed Facts, OEWL's occupation of the building fell, and falls, squarely within paragraph 15(2) and therefore the land is exempt land.
>
> …
>
> As a matter of fact, we find that at the date of the grant the appellant knew that the supply would not be, and could not be, taxable. Accordingly, given the terms of Regulation 113(1) of the VAT Regulations,…and knowing that no other relevant expenditure was likely, the appellant could not have intended or expected that the property would become a capital item in the hands of the purchaser."

Statutory provisions

10. It was agreed before the F-tT that the correct approach to the relevant statutory provisions was as set out in *UBS AG v HMRC* [2016] UKSC 13 at [66] – [68]:

"…'The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically'…

References to 'reality' should not, however, be misunderstood … tax avoidance is the spur to executing genuine documents and entering into genuine arrangements.

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. …"

11. Given the complexity of the provisions, it is worth setting them out in some detail at this point. In so far as relevant, paragraphs 12 to 17 of Schedule 10 VATA 1994 together with paragraph 113 of the Value Added Tax Regulations 1995 provide as follows:

Anti-avoidance

Developers of exempt land

12 (1) A supply is not, as a result of an option to tax, a taxable supply if-
(a) the grant giving rise to the supply was made by a person ("the grantor") who was a developer of the land, and
(b) the exempt land test is met.

(2) The exempt land test is met if, at the time when the grant was made (or treated for the purposes of this paragraph as made), the relevant person intended or expected that the land-
(a) would become exempt land (whether immediately or eventually and whether or not as a result of the grant), or
(b) would continue, for a period at least, to be exempt land.

(3) "The relevant person" means-
(a) the grantor, or
(b) a development financier.

(4) For the meaning of a development financier, see paragraph 14.

(5) For the meaning of "exempt land", see paragraphs 15 and 16.
…

Meaning of grants made by a developer

13 (1) This paragraph applies for the purposes of paragraph 12.

(2) A grant made by any person ("the grantor") in relation to any land is made by a developer of the land if-
(a) the land is, or was intended or expected to be, a relevant capital item (see sub-paragraphs (3) to (5)), and
(b) the grant is made at an eligible time as respects that capital item (see sub-paragraph (6)).

(3) The land is a relevant capital item if-
(a) the land, or
(b) the building or part of a building on the land,

is a capital item in relation to the grantor.

(4) The land was intended or expected to be a relevant capital item if the grantor, or a development financier, intended or expected that-
(a) the land, or
(b) a building or part of a building on, or to be constructed on, the land,
would become a capital item in relation to the grantor or any relevant transferee.

(5) A person is a relevant transferee if the person is someone to whom the land, building or part of a building was to be transferred—
(a) in the course of a supply, or
(b) in the course of a transfer of a business or part of a business as a going concern.

(6) A grant is made at an eligible time as respects a capital item if it is made before the end of the period provided in the relevant regulations for the making of adjustments relating to the deduction of input tax as respects the capital item.

…

(8) In this paragraph a "capital item", in relation to any person, means an asset falling, in relation to the person, to be treated as a capital item for the purposes of the relevant regulations.

(9) In this paragraph "the relevant regulations", as respects any item, means regulations under section 26(3) and (4) providing for adjustments relating to the deduction of input tax to be made as respects that item.

Meaning of "exempt land": basic definition

15 (1) This paragraph explains for the purposes of paragraphs 12 to 17 what is meant by exempt land.

(2) Land is exempt land if, at any time before the end of the relevant adjustment period as respects that land-
(a) a relevant person is in occupation of the land, and
(b) that occupation is not wholly, or substantially wholly, for eligible purposes.

(3) Each of the following is a relevant person-
(a) the grantor,
(b) a person connected with the grantor,
(c) a development financier, and
(d) a person connected with a development financier.
…
(4) The relevant adjustment period as respects any land is the period provided in the relevant regulations (within the meaning of paragraph 13) for the making of adjustments relating to the deduction of input tax as respects the land.
…

Meaning of "exempt land": eligible purposes

16 (1) This paragraph explains what is meant for the purposes of paragraph by a person occupying land for eligible purposes.

(2) A person cannot occupy land at any time for eligible purposes unless the person is a taxable person at that time (but this rule is qualified by sub-paragraphs (5) and (6)).

(3) A taxable person occupies land for eligible purposes so far as the occupation is for the purpose of making creditable supplies (but this rule is qualified by sub-paragraphs (5) to (7)).

(4) "Creditable supplies" means supplies which--
(a) are or are to be made in the course or furtherance of a business carried on by the person, and
(b) are supplies of such a description that the person would be entitled to a credit for any input tax wholly attributable to those supplies.
…

Extract from the Value Added Tax Regulations SI 1995/2518

113 Capital items to which this Part applies

(1) The capital items to which this Part applies are any of the items specified in paragraph (2) on or in relation to which the owner incurs VAT bearing capital expenditure of a type specified in paragraph (3), the value of which is not less than that specified in paragraph (4).

(2) The items are-
(a) land;
(b) a building or part of a building;
(c) a civil engineering work or part of a civil engineering work;
(d) a computer or an item of computer equipment;

(e) an aircraft;
(f) a ship, boat or other vessel.

(3) The expenditure--
(a) in the case of an item falling within paragraph (2)(a) or (d), is the expenditure relating to its acquisition;
(b) in the case of an item falling within paragraph (2)(b), (c), (e) or (f), is the expenditure relating to its-
(i) acquisition,
(ii) construction (including where appropriate manufacture),
(iii) refurbishment,
(iv) fitting out,
(v) alteration, or
(vi) extension (including the construction of an annex).

(4) The value for the purposes of paragraph (3) is-
(a) not less than £250,000 where the item falls within paragraph (2)(a), (b) or (c);
(b) not less than £50,000 where the item falls within paragraph (2)(d), (e) or (f).

Argument for the Appellant

12. On behalf of the Appellant it was submitted that it was not certain that the decision of the F-tT breaks the circularity in the legislation or, even if it does, whether the F-tT had taken the correct approach. Furthermore, it was submitted, the F-tT had erred in its finding of

fact as to what the Appellant knew by basing the finding on an application of the law and what the Appellant must have known about the effects of that law.

13. In relation to circularity, Mr Simpson explained that it was common ground that if the property was to be subject to value added tax at the standard rate, it would become a capital item in relation to CSPV, and that CSPV is a 'relevant transferee'. However, if the Appellant intended or expected that that would be the case, this part of the 'grant by a developer' test is satisfied and the option to tax is switched off. The effect of that is that the property does not become a capital item in relation to CSPV and the option to tax is switched back on. But if the option to tax is switched on and the Appellant intended or expected the property to become a capital item in relation to CSPV, then the option to tax is switched back off and so on.

14. The solution proposed on behalf of the Appellant to break the circularity is that the grantor's intention or expectation should only be considered once when considering whether the test is met. By adopting this approach circularity is not created.

15. Mr Simpson submitted that the F-tT erred in believing that the approach urged on behalf of the Appellant would mean that the Schedule 10 provisions would be limited in their application. It was also submitted on behalf of the Appellant that the F-tT's conclusion demonstrates the circularity as if, as a matter of fact, the Appellant is found to have known that the supply would not be taxable because the option to tax had been switched off, then the Appellant cannot have intended or expected that the property would become a capital item in relation to CSPV and so the 'grant by a developer' test is not met, and the option is not switched off.

16. Mr Simpson cited *PGPH Limited* v. *HMRC* [2018] S.T.F.D. 546 in support of the submission that the facts at the time of supply must be considered and any intention on the Appellant's part inferred from the objective surrounding circumstances; the focus should be on the expenditure and not the legal issues.

17. Although Mr Simpson agreed that no evidence was called before the F-tT, there was evidence within the joint bundle of documents, in particular a letter from Mr Graeme Murdoch (the Appellant's financial controller) on behalf of David Mousdale Properties to HMRC dated 22 December 2016 in which it was stated as part of the "Facts of transaction" that the property was expected to be a Capital Goods Scheme item for the purchaser, and to which the F-tT only referred in general terms. Mr Simpson submitted that the F-tT had erred in rejecting the evidence of Mr Murdoch that it was intended or expected that, because of the supply to CSPV, the property would become a capital goods item for CSPV. The Appellant submitted that, contrary to *PGPH Limited,* the Appellant's intention or expectation was negated by the application of the principle that ignorance of the law is no defence. The F-tT erred in failing to apply a subjective test as to the Appellant's intention. Moreover, if knowledge of the law is sufficient to overcome a taxpayer's actual intention, the effect is that the Appellant's intention or expectation was that the property would not be a capital goods item, and the option to tax is switched back on.

18. Mr Simpson submitted that the F-tT erred in making a finding of fact based on the proposition that as a matter of law the option to tax was not switched off and the Appellant was deemed to know that.

Argument for HMRC

19. On behalf of HMRC it was submitted that the F-tT was correct to conclude that the current transaction does not meet the requirements of paragraph 13(4) of Schedule 10 to VATA. As the property became a capital item for the Appellant in 2001 it was no longer a capital item for the Appellant by the time that the transaction in question took place due to the expiry of time, the 10 year interval adjustment period having expired (see Regulations 113(2) and 114 of the VAT Regulations).

20. The issue for the F-tT was, therefore, whether it was intended or expected that the property would become a capital item in respect of CSPV. The test to be applied is subjective by reference to the intention or expectation of the Appellant at the time when the transaction occurred.

21. HMRC agreed that when the provision is applied by reference to the capital item created by the grant itself, it results in circularity. HMRC submitted that the approach to adopt to avoid circularity is that the reference to the creation of a capital item must be a reference to a capital item other than the one which would arise on the grant. Mr Thomson submitted that adopting this interpretation is in keeping with the purpose of the legislation because the capital item arising from the grant itself causes no avoidance risk.

22. Mr Thomson submitted that the F-tT identified, by its reference to *UBS v HMRC* (see [10] above), the correct approach to paragraph 12(3) which is to look at whether the grant is one to which the provision was realistically intended to apply. In considering the purpose of paragraph 12, Mr Thomson relied on *Principal and Fellows of Newnham College in the University of Cambridge v Revenue and Customs Commissioners* (*"Newnham College")* [2006] EWCA Civ 285 in support of HMRC's submission that the disapplication of the option to tax provisions is intended to prevent the inappropriate recovery of input tax. The context of the provisions must be borne in mind and in doing so, on the facts of this case, there is no sensible reason why the opted property should not be a taxable supply when a grant is made. Mr Thomson also submitted that the F-tT correctly acknowledged that although the legislation is framed as anti-avoidance, the focus is not on any intent to avoid.

23. In response to the Appellant's submissions concerning the evidence, Mr Thomson highlighted the fact that the Appellant did not lead any evidence before the F-tT that subjectively he intended or expected that the property would become a capital item in respect of CSPV.

24. Mr Thomson submitted that it is unusual for the Upper Tribunal to be invited to look at correspondence written by someone who did not give evidence before the F-tT and the contents of which were not the subject of any findings in fact by the F-tT. Mr Thomson submitted that the F-tT proceeded correctly on the basis of the relevant facts which were set out in an Agreed Statement of Facts; as the F-tT identified, at [2] of the F-tT decision, there was "no dispute in relation to the **relevant** facts (emphasis added)". The Appellant now seeks to rely on facts in respect of which the F-tT made no findings and which the Appellant appears to invite the Upper Tribunal to accept as proven. Mr Thomson submitted that the fact of documents being contained within a bundle does not give such documents a self-proving status nor was it agreed between the parties that any correspondence could be taken as evidence of its contents without being spoken to by a witness. The findings of fact made by the F-tT are those which fall to be considered by

the Upper Tribunal. Furthermore, the grounds of appeal relied on by the Appellant did not aver that the F-tT failed to take into account relevant facts.

Decision

25. The question in this case has been correctly identified by the F-tT (para 29) as whether the land was intended or expected to be a relevant capital item in terms of para 13(2) of the Value Added Tax Regulations 1995.

26. Before turning to that issue, we note that the function of this Tribunal is to deal with issues of law. Mr Simpson sought to rely on a letter (referred to in para 17 above) which was neither in the Statement of Agreed Facts before the First Tier Tribunal nor introduced before the First Tier Tribunal by oral evidence, and which accordingly had not been the subject of a finding in fact by the F-tT. We did not understand Mr Simpson to seek to argue that the F-tT's decision was wrong in law on the principles laid down in *Edwards v. Bairstow* [1956] AC 14. However, for the avoidance of any doubt, we note that there is a high threshold for a successful *Edwards v Bairstow* appeal. In our view, for the reasons we set out below, the findings of the F-tT were supported by the Agreed Facts upon which they were based and we were satisfied that the conclusion was not one which could not properly be reached. We therefore conclude that the F-tT's decision was not wrong in law on the principles laid down in *Edwards v. Bairstow*. In any event, had the letter been properly before us as a matter of fact which had been agreed between parties or had been the subject of a finding in fact by the F-tT then we would have given it little weight. It was not a letter by Mr Moulsdale contemporaneous with the event but was an assertion by a member of Mr Moulsdale's staff made in the course of a letter, written more than two years after the sale, seeking to challenge HMRC's decision

27. Turning now to the question before us, on the facts before the F-tT, a grant was made at a time when the option to tax had effect. By virtue of paragraph 10(2) if a grant is made when an option to tax is in force the supply is taxable unless certain conditions are met. Paragraph 12 of Schedule 10 sets out the test for the disapplication of the option to tax.

28. Although headed "anti- avoidance provisions" there was no dispute between the parties that in fact the provisions are not limited to situations involving avoidance.

29. As stated in *PGPH*, the references to intention or expectation in paragraphs 13(2) and (4) of Schedule 10 impose a subjective test; the intention to be ascertained is that of the Appellant at the date of the grant. There is also no requirement that the capital item must exist at the date of the grant (paragraphs 13(2) and (4)). The issue before the F-tT was, therefore, whether at the time of the grant the Appellant intended or expected that the property was or would be a capital item in the hands of the purchaser.

30. We agree with the comments in *PGPH* at [116] - [118] that:

> "The question is exactly what that intention or expectation must be. In my view it must be an intention or expectation to incur expenditure on something which, if it is incurred, will result in there being a capital item within paragraph 113 of the VAT Regulations.
>
> Mr Lall submits that this imports a requirement for some knowledge of the Capital Goods Scheme. Whilst I can see that that is a conceivable literal interpretation of the words, I do not think that it is the correct interpretation on any form of purposive

construction, or indeed that it is necessary to strain the language of the words to conclude that the interpretation Mr Lall suggests is wrong. A perfectly legitimate literal interpretation is that the words "falling … to be treated as a capital item" simply describe a set of facts that would fall within the relevant regulations. The reference to "would become" relates to the nature of the intention or expectation: did the grantor in fact intend or expect that works would be undertaken of a type which would in fact fall within the regulations.

There is no indication from the text of the legislation that Parliament only intended the rules to apply if the land did become a capital item. The draftsman could readily have addressed the point, for example by inserting "and became" after the reference to "intended or expected to be" in paragraph 13(2). It might also be expected that it would be specified that the land needed to become a capital item within a stated period. No such provision was included..."

31. In *Newnham College* Chadwick LJ in the Court of Appeal observed at [28] – [30]:

"I have set out the legislative history in deference to the careful arguments that were addressed to the Court by counsel for the Commissioners. But I am not persuaded that an understanding of that history is of any real assistance in the determination of the issues which are now before the Court. It is plain that the Sixth Directive permits an election to waive the exemption which would otherwise be afforded to the letting and leasing of immoveable property. It is equally plain that the Sixth Directive permits a Member State to restrict the circumstances in which that election can be exercised. Paragraph 2(1) of schedule 10 VATA 1994 confers the right to elect: paragraph 2(3AA) seeks to restrict that right.

It is clear that the object of the restriction is to preserve the basic principle that an exempt business should bear input tax on supplies made to it by being denied the opportunity to treat that tax as allowable tax giving rise to a VAT credit. The restriction in paragraph 2(3AA) seeks to achieve that object by denying to an exempt business the option to treat the letting of a building which it will continue to occupy (for the purpose of that business) as a taxable supply. But that appears from a reading of paragraph 2(3AA) in the context of the other provisions in paragraphs 2 and 3A of schedule 10. The legislative history illustrates the difficulties encountered by the United Kingdom government in promoting legislation which achieves that object without giving rise to unintended consequences. But it does not, I think, throw light on the question which the Court has to determine on the present appeal.

The task of the Court is to interpret the legislation which has been enacted; having in mind the object for which it has been enacted, but recognising that the extent to which that object has been achieved in the particular case must depend on the legislation itself. The Court cannot go outside the legislation. It must accept that, if the legislation fails to achieve that object in the particular case, that must be assumed to reflect Parliament's intention that it was not necessary or appropriate to do so."

32. In the appeal to the House of Lords, Hoffman LJ explained:

"Making exempt supplies is all very well for the recipients, because they pay no VAT. It is less attractive if you are the supplier, because you are not credited with the input tax on the goods and services on which you have been charged VAT."

33. Turning to the decision under appeal, the Ft-T identified the sole issue as the interpretation of the relevant provisions of Schedule 10 VATA. The F-tT noted that there is no requirement for an intention to avoid tax for the provisions to be engaged and it recorded that there was no suggestion in this case that the arrangements were not genuine.

34. As the Appellant had opted to tax the property, any grant in respect of that property would be taxable unless it fell within an exemption.

35. The F-tT proceeded on the basis of the Agreed Facts, recording at [38] that (as per paragraph 3 of the Agreed facts) "OEWL's occupation of the building fell, and falls, squarely within paragraph 15(2) and therefore the land is exempt land."

36. As the property was no longer a capital item for the Appellant the F-tT recognised at [26]:

> "…the only possibility of qualification would be if it were to be a capital item in the hands of the purchaser."

37. This required consideration of the only remaining test under the relevant provisions, namely paragraph 13(4) which looks to the intention of the Appellant. At [34] to [36] of its Decision, the F-tT said:

> "Mr Simpson advanced the argument that the intention should be considered prior to the supply on the basis that it is the grant that triggers the exempt land test. With respect that does not advance matters since the wording of paragraph 12(1) sits well with that since it refers to the "grant giving rise to the supply". We reiterate that what matters is the intention or expectation at the time of the grant.
>
> Capital item is defined in Regulation 113 of the VAT Regulations. There is no dispute between the parties that the property qualified under Regulation 113(2), (3), (4) and 8. The problem is Regulation 113(1) which reads:
>
> "The capital items to which this Part applies are any of the items … on or in relation to which the owner incurs VAT bearing capital expenditure …".
>
> The phrase "VAT bearing capital expenditure" is defined at Regulation 115(3) as being capital expenditure at the standard or reduced rate. The purchaser would only incur VAT if VAT was charged on the supply of the property. Therein lies the problem."

38. No oral evidence was led on the issue and the F-tT concluded on the material before it, namely the fact that the purchaser was not VAT registered (nor subsequently became so) together with the Appellant's knowledge "that the supply would not be, and could not be, taxable" as no VAT was charged on the acquisition and that "no other relevant expenditure was likely" that the Appellant could not have intended or expected that the property would become a capital item in the hands of the purchaser.

39. The requirements of the legislation must be satisfied at the date of the grant; if there is no intention or expectation of expenditure or that works would be carried out resulting in a capital item under Regulation 113(1) then the rules are not engaged. On the facts of this appeal, the only expenditure that could make the property a capital item is on the acquisition but no VAT was charged and there was no evidence before the F-tT that the Appellant had any intention or expectation that the property would become a capital item

in the hands of the purchaser. It is clear that the provision is only intended to apply where, at the point of entering into the transaction, the transferor intends or expects that a capital item will be created in the purchaser. That requirement cannot be met when the grantor knows that the invoice issued will treat the grant as exempt.

40. We reject the Appellant's submission that the F-tT made findings of fact as to the Appellant's knowledge of the relevant provisions. It is clear that the F-tT's approach applied the test by reference to the Appellant's knowledge as to the facts of the transaction and not by reference to his knowledge of the statutory provisions. In doing so, the F-tT clearly had in mind the observations in *PGPH* (see [30] above) and was entitled to reach the conclusion, on the basis of the agreed evidence, as to the Appellant's intention or expectation by reference to the facts of the supply. The F-tT was entitled to reject the Appellant's submission that it is the intention before the supply is made that is relevant (at [21] of the Decision) having concluded that it is the intention at the time of the grant which is relevant (see [33], [34] and [41] of the F-tT's Decision).

41. Our conclusion is fortified by a consideration of the potential for tax avoidance were we to decide otherwise. We agree with the F-tT at [42]:

> "We have some difficulty with [the Appellant's] proposition that the process comes to a halt once it is established that the transaction is exempt in that that would mean that in cases where the sale price of the land and buildings was over £250,000 and the relevant person occupying it met the "exempt land test" there would be no charge to tax. Although the purpose of the legislation is to limit the circumstances in which the option to tax can be deployed it is also aimed at anti-avoidance and to implement that approach would be to encourage the avoidance of tax."

42. It seems to us that in reaching its Decision, the F-tT applied the correct interpretation in its application of the law to the facts and bore in mind the object for which the provisions were enacted. In our view the F-tT correctly identified the test and applied it to the evidence; the submissions on behalf of the Appellant did not persuade us to the contrary.

Disposal

43. We have concluded that the Tribunal properly applied the relevant provisions and that its conclusion was properly reached on the evidence before it.

44. For these reasons the appeal is refused.

LORD ERICHT
JUDGE DEAN

Issued 12 March 2020