TC02818

Appeal number: TC/2011/03595

VALUE ADDED TAX – S35VATA94 – DIY Builders Scheme - whether the particular planning condition prohibited the separate use and disposal of the dwelling – no – conditions satisfied – Appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

ROY SHIELDS **Appellant**

- and -

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

TRIBUNAL: JUDGE IAN HUDDLESTON

Sitting in public in Belfast on 12 March 2012

Ian Huddleston, Tribunal Judge

Celine Corrigan, Member

DECISION

Appeal

1. The issue under appeal is HMRC's decision to refuse the Appellant's claim for a refund of value added tax ("VAT") in the sum of £6,189.56.

2. The claim was brought under the DIY Builders Refund Scheme ("the Scheme") pursuant to Section 35 of the Value Added Tax Act 1994 ("the Act").

3. The decision to refuse the claim was communicated in a letter dated 28 January 2011.

Facts and Context of Appeal

4. Mr. Roy Shields ("the Appellant") lives and operates two businesses from premises at 274 Bangor Road, Newtownards, County Down, BT23 7PH.

5. One business is an equestrian business, which is not registered for VAT.

6. The second is a landscape business which is registered for VAT.

7. Mr. Shields originally lived in a converted building on the small holding which he owned at the subject address. That building did not initially have the benefit of planning permission, and indeed he had previously been refused planning consent for a replacement dwelling on the site.

8. Mr. Shields then obtained a planning consent for a new equestrian manager's house on the holding in March 2003 (planning reference X/2001/1360/0).

9. That planning consent contained the following condition ("Condition 3"):

> *"3 The occupation of the dwelling should be limited to a person solely employed by the equestrian business at 274 Bangor Road, Newtownards, and any resident dependents.*
>
> *Reason: the site is located within a green belt where it is the policy of the Department to restrict development and the consent hereby permitted, is granted solely because of the Applicant's special circumstances."*

10. Much more recently, and then in accordance with current planning policy under PPS 21, the Applicant made a further application to Planning Service, and the occupancy condition referred to above has now been removed (Planning Reference X/2011/0368 dated 13 February 2012 ("the 2012 Permission")).

11. Prior to the removal of Condition 3, the Appellant had proceeded to construct his new dwelling and, upon completion, had lodged his claim under the DIY Building

Scheme for recovery of the VAT he had incurred in the total sum of £6,189.56 on 28 January 2011. The claim was made under reference VAT 431NB.

12. HMRC, having considered the claim, were of the view that the planning permission incorporating Condition 3 limited the occupation of the dwelling to such an extent that only a person employed as a manager of the equestrian business could occupy the property and, as a result of that restriction, declared the claim was ineligible and refused it by way of letter dated the 28 January 2011.

13. The Appellant's Representative, Mr. Donaldson, wrote to HMRC seeking a review of that decision and followed that up with a copy of the 2012 Permission, ie. the planning consent, by which Condition 3 was removed.

14. HMRC, however, in their letter of the 12 April 2011, confirmed this rejection of the claim on the basis that:

"Unfortunately, due to the existence of an occupancy prohibition in place by the Planning Authorities in respect of the DIY Application submitted by Mr. Shields, the application is still ineligible under the Scheme, as it fails under Note 2(c) in the relevant VAT Act and the application cannot be approved."

15. The Appellant appealed to this Tribunal citing in his Notice of Appeal that:

"The occupancy condition imposed by Planning Service does not prevent the separate use or disposal of the dwelling. Although the occupancy is restricted to someone involved in the adjacent equestrian business, the condition does not prohibit a change or ownership or disposal of the property"

and cited as authority for that proposition the case of *Margaret Elizabeth Wendels v HMRC [2010] UK FTT476.*

16. It is probably appropriate to comment on that case at this point. In Wendels the property in question was subject to the following planning condition:

"The occupation of the dwelling hereby permitted shall be limited to a person solely or mainly employed or last employed in the cattery business occupying the plot edged blue on drawing number C27-05-01-1 dated 14 December 2005 and submitted with the Appeal or a widow or widower of such a person or any resident dependent."

17. The Tribunal *Wendells* found that the:

> *"… terms of the planning consent …. did not prohibit its separate use or disposal as a dwelling …..[and the] condition imposed constituted an occupancy condition, not a prohibition on its use or disposal as a dwelling."*

18. On that basis the appeal was allowed. Mr. Donaldson, therefore, argues that Condition 3 is an occupancy condition and does not create a prohibition on "use or disposal" of the dwelling now occupied by Mr. Shields.

The Legislation

19. In general terms, the provisions of Section 35(1) and 1(A) VATA provide the legislative context for claims made under the DIY Builders Referral Scheme; effectively allowing zero rating for certain developments in certain circumstances:

> *"35(1) Where –*
>
> *(a) a person carries out works to which this section applies,*
>
> *(b) his carrying out of the works is lawful and otherwise than in the course of any business, and*
>
> *(c) VAT is chargeable on the supply, acquisition or importation of any goods used by him for the purposes of the works*
>
> *the Commissioners shall, on a claim made in that behalf refund to that person the amount of VAT so chargeable."*
>
> *"35(1A) The works to which this section applies are,*
>
> *(a) the construction of a building designed as a dwelling or a number of dwellings;*
>
> *(b) the construction of a building for use solely for a relevant residential purpose, or relevant charitable purpose; and*
>
> *(c) a residential conversion."*

20. For the purposes of this appeal the first question, therefore, is whether the works were carried out in the ordinary course of business. If they were, the appeal must clearly fail.

21. What is germane to that question are the notes to Group 5 Schedule 8 which are made applicable by virtue of Section 35(4) of the Act.

22. The relevant notes provide as follows:

> *"Notes*
>
> *(2) A building is designed as a dwelling or a number of dwellings where in relation to each dwelling the following conditions are satisfied:*
>
> *(a) the dwelling consists of self-contained living accommodation;*
>
> *(b) there is no provision for direct internal access from the dwelling to any other dwelling or part of a dwelling;*
>
> ***(c) the separate use, or disposal of the dwelling, is not prohibited by the terms of any covenant, statutory planning consent or similar provision; and***

(d) statutory planning consent has been granted in respect of that dwelling and its construction or conversion has been carried out in accordance with that consent."

23. Essentially Notes (2)(a) and (b) are a question of physical application, and are relevant to cases such as the construction of granny annexes etc. which may in the context of the actual construction be physically attached to existing dwellings.

24. Note (2)(c), however, is one of legal interpretation based on the actual terms of any planning consent which has been granted, and it is Note 2(c) which is engaged in the present appeal.

HMRC's Case

25. HMRC's view is that as the Scheme allows a specific exception to DIY builders scheme, and that as it is an exception to the general rule that VAT should be charged and not be recoverable that it should be narrowly construed.

26. For the purposes of the present appeal, HMRC take the view that there is a relationship between the commercial activity (ie. the equestrian business) which is co-located upon the same land as the house based on the terms of Condition 3 and that, therefore, applying Note 2(c) recovery should not be permitted.

27. On the specifics around Condition 3, HMRC take the view that occupancy conditions of this type vary in strength and application, depending upon the particular planning agency and the circumstances of each case. They do accept that a clause in a planning permission relating to the occupancy of a house will not of itself infer a prohibition upon the use or disposal of it.

28. Where, however, the occupancy condition extends beyond the class of person / class of activity into specified persons or a specified activity, HMRC's view, as expressed to the Tribunal, is that the condition should properly be considered to be a prohibition preventing use separate to the commercial activity that is carried on, and that, therefore, Note 2(c) is engaged.

29. In support of that proposition, they cite the case of *Paul Cussins v HMRC [2007](VTD20541)*.

30. In that case, the planning condition was in the following terms:

"8 The residential accommodation hereby permitted shall only be occupied in conjunction with the commercial use hereby approved.

Reason: The site lies in an area where new residential development is restricted."

31. The Tribunal Judge in that case in rejecting the Tax Payer's appeal stated that:

"The wording of condition 8 to our mind establishes a close nexus between the residential and commercial premises and taken in the context of the published

planning policies of Rydale District Council and the reason for the decision as clearly stated, this defines the domestic enjoyment as conjoined with the commercial."

32. On the basis of that authority HMRC argue that if **either** separate use **or** separate disposal of the property is found to be prohibited then Note 2(c) is engaged and the claim denied.

33. HMRC also rely upon the authority of *HMRC v Lunn [2010STC486]*. The relevant planning condition in that case was in the following terms:

"*The development hereby permitted shall only be used for purposes either incidental or ancillary to the residential use of the property known as Radbrook Manor and shall not be used for commercial purposes."*

34. In the particular case the Tribunal found that the phrase "separate use" as used in Note 2(c) had the meaning "separate from" (in that case) the predominant residential use. As to the question of "use", the Tribunal also found that on a practical interpretation the term "use" meant that a dwelling was used by simply being occupied.

35. On that basis, therefore, HMRC contend that where a building is subject to a planning condition tying a property to a specified business, then there is a prohibition on separate use arising from the nature of the occupation as the dwelling cannot be used for a use which is separate from the business.

36. On the facts of the present case, therefore, HMRC contend that whilst they accept that separate disposal has not expressly been prohibited they do take the view, based on *Cussins* and in *Lunn*, that if a separate use has been prohibited by the terms of the planning permission then Note 2(c) is engaged and the claim must fail.

37. On that basis they seek to distinguish the Appellant's reliance upon *Wendels* on the basis that the present condition is more restrictive than in *Wendels* in that it does not provide for occupation by a person or a successor who is no longer or not engaged in the business.

38. HMRC are also of the view that *Wendels* has been wrongly decided.

39. As to the removal of Condition 3 (ie. by the later permission granted in February 2012) HMRC say that the correct time for the application of Note 2(c) is at the date of construction, and for this proposition they rely on the authorities of *A E and J M Harris v HMRC [2004] VTD18822* and *Michael J Watson v HMRC [2010] UK FTT00780*.

The Appellant's Case

40. The Appellant was represented by his planning consultant, Mr. David Donaldson.

41. Mr. Donaldson gave the planning history of the construction of the dwelling and, indeed, the claim.

42. As to the question arising under Section 35(1)(b), ie. if the dwelling was erected *"in the course of furtherance of a business"* Mr. Donaldson put the position that the dwelling was purely constructed to provide living accommodation for Mr. Shields and his family, and that no trade or business was conducted from it.

43. Evidence was also given that since 2009 there had been another lawful dwelling on the holding which could have been used for the purposes of the equestrian building – namely the property in which Mr. Shields initially resided even though that did not, at the beginning, have planning permission.

44. Other than being proximate to the equestrian business, the proposition put by the Appellant is that there was no other nexus between the business and the residential use to which the dwelling is put – save for Condition 3 which appears in the planning consent.

45. As to the requirements of Note 2, the Appellant's position is that the dwelling clearly meets Note 2(a), (b) and (d) – a point which HMRC does not dispute.

46. As regards the issues raised by HMRC in respect of Note 2(c), Mr. Donaldson makes the following points:

(1) as regards "use", in planning terms, he makes the point that the building falls firmly within Class C1 – residential use and that, therefore, clearly is not constructed "in the furtherance of a business" in the sense used in S35;

(2) on the point of the occupancy restriction, Mr. Donaldson referred to VAT Notice 719 and paragraph 4.2.2 in particular which (when it was enforce) stated that:

"*Occupancy restrictions are not prohibitions in separate use or disposal, and do not affect whether a building is "designed as a dwelling"*.

(3) Mr. Donaldson acknowledges that VAT Notice 719 has been replaced by VAT Notice 731(NB) which does not mention occupancy conditions, but in its place, at question 13, states that:

"*If the building is an annex, extension or any form of ancillary structure or building which cannot be used separately from another property, then it does not have independent status and cannot qualify for a refund under this Scheme"*

As an allied point, therefore, Mr. Donaldson puts the argument that the whole purpose of Note 2 is to deny refunds where buildings are physically and functionally dependent upon one and other – and denies that that applies in the present case.

(4) His final point is that Condition 3, is in substance an occupancy condition and, therefore, does not constitute a prohibition on either the "separate use or the disposal of the [subject] property", and that it relates only to the category of persons who may occupy it. In short he invites the Tribunal to conclude that there is no requirement for the building to be

used in association with the equestrian business and that, to the extent that there is the limitation under Condition 3, that it relates only to, at most, one of the occupants – in this case the Appellant but not by extension his family.

47. As suggested above, in support of that proposition Mr. Donaldson relies on *Wendels* but also on the most recent case of *Ian Phillips [2011] UK FTT 372*. In that case, a couple, who operated a number of holiday chalets, applied for planning permission to build an additional house on the site for their son and his wife. The planning permission, as granted, included a requirement that the house should be occupied *"only by persons engaged in the management or operation of the existing holiday chalet letting business, together with their family members."*

48. On an appeal under the DIY Builders Scheme, HMRC rejected the claim which was then allowed on appeal.

49. The Tribunal, having reviewed the earlier cases concluded that *"the essential element in each case is that there is a positive obligation on one or more of the occupants of the house to be engaged to a greater or lesser extent [in the business] .... …… [but] there is no obligation which requires the "house" to be used in the management of same"* and that, therefore, the restriction was an occupational restriction which did not affect the use of the property that Note 2(c) was not engaged and that the claim should be allowed.

Decision

50. Logically it makes sense for the Tribunal to deal with the issue arising under Section 35(1) of the Act first.

51. If the Tribunal were to find that the works in this case were done (to use the language of that section) *"in furtherance of the business"* then the claim must necessarily fail.

52. In the present case, however, the Tribunal finds that the dwelling was not built in furtherance of the business – construing that phrase in its ordinary meaning.

53. We say this for the following reasons:

(1) in the first place, the Appellant had already been living on the property for some time – indeed since circa 1993. Initially he had lived in a property which did not have the benefit of planning permission, but in respect of which he subsequently achieved a Certificate of Lawful Use;

(2) on the evidence of the Appellant, we find that the house was not actually "required" for the purpose of the equestrian business. There is no doubt it made the operation of that business easier, but it was not, we have concluded, a functional necessity;

(3) again, on the evidence before the Tribunal, the construction cost was privately financed by the Appellant and was not financed, nor did the final

dwelling, form any part of the assets of either the equestrian business or indeed the landscape business;

(4) the evidence to the Tribunal was that the landscape business did assist, by the provision of collateral security, for the private loan which Mr. Shields needed to construct the dwelling, but there was a clear distinction between the two.

54. In essence what the Tribunal finds is that because of the siting of the dwelling in the green belt, the Appellant found it easier to get planning permission by referring the businesses with which he was involved, but we do not find that the construction of the dwelling was, of itself, in furtherance of the equestrian or, indeed, the landscaping business.

55. Indeed, on the evidence to the Tribunal, it appeared that Mr. Shields had undertaken an investigation as to whether to or not it might be more tax efficient to construct the dwelling "through the business" (ie. the VAT registered landscaping business), but had been advised by his accountant that given the actual lack of usage that there would be no compelling case to argue for recovery of VAT on that basis.

56. As to the issue of the engagement (or not) of Note (2)(c) it clearly falls to the Tribunal to decide on which line of the fence this case actually falls.

57. Is it the case that there is such a "close nexus" (to cite the Tribunal Judge in *Cussins*) established by the language of Condition 3 such as to engage Note 2(c) and deny the claim or, is it the case, that (applying *Wendels* and *Philips)* the condition is in truth an occupancy condition such as the requirement is imposed upon occupiers rather than upon the development of the property or dwelling itself.

58. In *Cussins* the language of the planning condition in contention (see paragraph 30 above) was that *"the house [could]* ***only*** *be occupied in conjunction with the commercial use hereby approved."*

59. That obviously spoke in respect of the nature of the actual development (ie. the dwelling) itself. The linkage or "nexus" was clear and unambiguous.

60. In a similar vein, the planning condition in *Lunn* (see paragraph 33 above) spoke of the *"development … only [being] used for purposes either incidental or ancillary to the residential use of Radbrooke Manor."*

61. Again, as a matter of interpretation, the planning condition related to the nature of the particular development and then to create co-dependency between that and the business – the latter would not have existed "but for" the former.

62. As against that line of cases, the point adopted by the Tribunal Judge in *Wendels* was that on a true interpretation the condition in play was an **occupancy** condition insofar as it spoke of "***occupation*** *of the dwelling [being] limited to a person solely or mainly employed in the cattery business and that therefore it was, in truth, an occupancy condition of the type which HMRC in public notice 719 had already indicated not to be construed as something which engaged Note 2(c)."*

63. It was that same approach which was adopted in the *Phillips* case where, again, the language is in terms of "*[occupation] only by persons engaged in the management or operations of [the letting business]"*.

64. The contrary line of cases therefore attempts to distinguish "occupation" from a "prohibition", and in doing so looks at the possibility of others who may occupy.

65. In both *Wendels* and *Phillips* there was reference to other family members and/or dependents.

66. Indeed, Ms. Tilling for HMRC invited us to distinguish *Wendels* (and presumably *Phillips*) on that basis, ie. that Condition 3 in this case referred not only to such a "person" involved in the business, but also to "and any resident dependents".

67. The one thing that it is possible to distil from a review of the cases is that each planning condition must be considered on its own terms. In written submissions from the parties dated 4th and 12th October 2012, we were referred to the case of *HMRC v Holden* [TC02043] where the planning condition was in the following terms:

> "The flat hereby permitted shall be occupied only in conjunction with the quotation of the photographic study from 240a Highbridge Road.

the appeal in that case being based on note 2(c) was dismissed.

Since then there has been the case of *HMRC v Bull* [TC 02510] released on 1st February 2013. That case also involved an equestrian business with the planning consent in point allowing for "the erection of a single storey dwelling….to release the existing static mobile home…" subject to a planning condition that

> "occupation of the dwelling be limited to a person or persons employed in the operation of the adjoining equestrian centre."

The Tribunal in that case found that the condition "constituted an occupancy restriction and did not prohibit the separate use or disposal of the dwelling..." and consequently allowed the appeal.

68. It is clear therefore that there are a category of cases which are closer to the occupancy conditions of the type to which reference was originally made in Public Notice 712 where indisputably there is a connection with an allied business, but not one which satisfies the "but for" test which arises under *Lunn*.

69. Having reviewed the cases, on our interpretation of Condition 3 we find it to be just such a condition.

70. In short, therefore, we are of the view that whilst it contains a limitation as to occupancy it does not, by its terms, reach the level of being a prohibition on disposal or use such as to engage Note 2(c).

71. Indeed, in our view, insofar as the condition countenances the occupancy extending to any "resident dependents", it cannot be said to amount to a prohibition on use.

72. In context, what clearly happened, was that the Appellant sought to rely on the existing business to justify the grant of planning permission in a "green belt" area.

73. It follows that any such planning permission, as is granted in those circumstances, will by its necessity create a linkage between the underlying business and the dwelling.

74. The terms of the condition, however, in this case, we find is in the nature of an occupancy condition.

75. As such we conclude that Note 2(c) is not engaged insofar as the condition does not go far enough to satisfy the "but for" test referred to in *Lunn*.

76. We conclude, therefore, that the appeal should be allowed.

77. We should point out that HMRC have not actually investigated the merit of the claim itself.

78. The effect of allowing the appeal is, therefore, subject to HMRC's own review of the actual claim in terms of quantum.

79. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

IAN HUDDLESTON
TRIBUNAL JUDGE

RELEASE DATE: 7 August 2013