TC02839

Appeal numbers: LON/2008/1364, TC/2013/00057, 00063-67, 00237 & 01318

VALUE ADDED TAX – refurbishment of nursing home premises – lease of premises by company to subsidiary – services provided under separate agreement – whether single exempt supply of property together with services or independent supplies of property and services – held, single composite exempt supply of property and services – similar conclusion on basis of manner in which arrangements implemented in practice – deductibility of input tax – held none of input tax on construction costs attributable to taxable supplies – appeal dismissed

Procedure – application for late admission of appeals granted and some appeals consolidated with main appeal

FIRST-TIER TRIBUNAL
TAX CHAMBER

SUNNYSIDE PROPERTY COMPANY LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE JOHN CLARK
JAMES MIDGLEY

Sitting in public at 45 Bedford Square London WC1B 3DN on 3, 4, 5 and 6 June 2013

David Moll, DKS VAT Specialist, for the Appellant

Owain Thomas of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. The Appellant ("SPCL") appeals against a decision by the Respondents ("HMRC") that SPCL was making a single exempt supply arising from a lease and facilities agreement and that VAT incurred on construction services and utilities was directly attributable to such exempt supply. The effect of this decision was to deny relief for input tax incurred by SPCL. SPCL also appeals against a series of assessments made in accordance with that decision.

The background facts

2. The evidence consisted of four large lever-arched files containing documents, as well as witness statements given by Khaled Gamiet and Stephen Aldcroft. Mr Gamiet also gave oral evidence; although it was proposed that Mr Aldcroft should also give oral evidence, it was agreed between the parties at the hearing that his witness statement should stand as evidence without need for additional oral evidence. From the evidence we find the following background facts.

3. SPCL was registered for VAT with effect from 3 April 2006. On its application for registration, SPCL described its business as "rental of property, facilities charges and sale of food".

4. SPCL is part of a group of companies controlled by the Gamiet family. In 1984 Mrs Gamiet started operating a nursing home business with the opening of the Sunnyside Private Nursing Home in Iver, Buckinghamshire. The property was owned and operated as a nursing home by Sunnyside Private Nursing Home Ltd ("SPNH"). SPNH began operating with seven residents but this increased over time to 32 registered places by the time of a valuation made in 2003 (see below). Several of the rooms in the home were shared.

5. In 1992, a second home, Langley Nursing Home was opened. The freehold property was owned by SPNH and the nursing home was operated by a limited company, Langley Nursing Home Ltd ("LNH") registered on 6 May 1992.

6. At the end of 2002, a decision was taken to restructure the existing arrangements. A VAT advice letter written in early 2006, long after the event, suggested that the property companies had been set up "to separate the freehold properties from the operating income to reduce the group's exposure to a large compensation claim that could be funded through the sale of the properties". As we had no specific evidence concerning the reasons for the restructuring, we make no findings in respect of the reasons.

7. A holding company called Trustworth Group Limited ("TGL") was incorporated on 14 April 2003.

8. Three property companies were also formed. Langley Property Company Ltd was incorporated on 15 April 2003. SPCL was incorporated on the same date. Five

Acres Property Company Ltd ("FAPC") was incorporated on 5 June 2003 in preparation for the acquisition of a new nursing home business, Five Acres Nursing Home Ltd ("FANHL") later that year; the shares in FANHL were owned by FAPC. (The shares in FAPC, together with its subsidiary FANHL and its underlying business, were subsequently sold in 2006; neither of these companies is affected by the matters under consideration in these appeals.)

9. In May 2003, a valuation was made for HSBC Bank plc by Atis Real Weatheralls ("Weatheralls"). (Although the title page shows the year as "2002", the date given in the main report is 19 May 2003; in the light of other information within the report, we find the latter to be the correct date.) This was a valuation of Sunnyside Nursing Home, Langley Nursing Home and The Old Rectory Nursing Home in the Milton Keynes area, which (as Mr Gamiet explained in later correspondence with HMRC) subsequently became Five Acres Nursing Home. (The valuation makes no reference to the ownership of the latter home being in the hands of any other entity or group as at that date; the actual date of its acquisition by FAPC and FANHL is therefore uncertain.)

10. The valuation of Sunnyside Nursing Home was £625,000 as an "operational entity", and £700,000 on the "special assumptions" that the business was closed, no accounts were available, the inventory had been removed and registration (by the National Care Standards Commission) had been lost and that the property would be converted or redeveloped for private residential uses.

11. Following the re-structuring, TGL held 100% of the shares in the property companies and each property company held 100% of the shares in its respective nursing home operating company. The respective nursing home properties were transferred to the property companies.

12. Once the new arrangements were in place, the property companies entered into informal (unwritten) lease agreements with the respective operating companies allowing for rents of £35,000 per annum in respect of SPNH and £15,500 in respect of LNH.

13. The offices on the top floor of the Iver property were used by the directors of TGL and the other group companies, and by employees of TGL dealing with the central administration of the group companies.

The refurbishment work

14. Following the introduction of the National Minimum Standards for Care in April 2002, as well as the demands of the nursing home market, it was decided by Mr Gamiet in conjunction with his co-directors that the premises operated by SPNH should be improved. The scale of the proposed development was such that the directors considered completely demolishing the premises and building a new nursing home. Although the cost of doing so would have been similar to that of remodelling the existing premises, it was decided not to demolish and rebuild because this would have meant closing down the nursing home, relocating residents and laying off staff.

15. The directors therefore decided to make the changes by means of alterations, refurbishment and extensions to the existing building, with every room undergoing some form of alteration. Work on the planning of the project began in around 2005, as evidenced by a letter from Mr Aldcroft dated 4 March 2005 and the reference in his witness statement to having carried out a survey in 2005 to develop the design of the services to meet the client's requirements and brief.

16. VAT advice was obtained in early 2006, before the start of the building work but after the plans and specification had been drafted. The advice was that the work could not be zero-rated. Arrangements were discussed with a view to seeking the recovery of a proportion of the VAT incurred on the building project, and the advice set out the way in which these should be implemented. (We consider this in greater detail below.)

17. Following the obtaining of the VAT advice, various steps were taken to formalise the arrangements for payments and charges between SPNH and SPCL. With effect from 1 April 2006, a formal written lease was put in place between SPCL and SPNH in respect of the property in Iver used for the purposes of SPNH's nursing home business. From the same date, a Facilities Agreement was entered into between SPCL and SPNH. (We consider in detail below the facilities provided under this agreement.)

18. The building contract with Thomas Vale Construction PLC commenced on 3 April 2006. The Contract Sum as specified in that contract was £1,212,977 plus VAT. The amount actually spent on the project (under the building contract and otherwise) was approximately £1.6 million plus VAT.

19. While building work was being undertaken at the nursing home, it was decided that payment of rent under the lease should be suspended. (We consider this below.) Office space was made available to TGL for use by the office administrator and a part-time person dealing with the payroll; no payment was made by TGL for the use of that space (initially on the top floor and, once the third phase of the refurbishment work had been completed, on the ground floor).

20. At around the time of formalising the arrangements, a further decision was taken that SPCL should act as a central purchaser for a range of items such as food and provisions, medical supplies and consumables to be supplied to SPNH and LNH at a mark-up of 5 per cent.

21. On 13 April 2006, Mr Gamiet wrote as director of SPCL to apply for its voluntary registration for VAT with effect from 1 April 2006. In his letter he referred to the business of SPCL as comprising exempt rental of property, standard rated facilities charge and supply of food (a mixture of standard and zero rated supplies). Following SPCL's responses to certain enquiries, HMRC issued a Certificate of Registration on 22 August 2006, the effective date being 3 April 2006.

22. The redevelopment of the Iver property began on 3 April 2006, and was carried out in four phases. The work was finished on or shortly before 31 March 2008, with

the property being handed over to SPCL on 1 April 2008, subject to "snagging" items under the building contract.

23. On 1 June 2008 SPCL and SPNH entered into a new Facilities Agreement. On 1 April 2009, SPCL and SPNH entered into a document entitled "Renewal of Lease Agreement", and on 1 June 2010 they entered into a new Facilities Agreement. The details of these documents are considered below.

24. SPCL submitted its first VAT return for the period 09/06. As this was its first return and a large repayment was being claimed, HMRC commenced a routine verification query, and on 17 November 2006 an officer named Mr Pate sent SPCL an email requesting information. Mr Gamiet responded on 24 November with four documents containing financial details; he stated that there were no partial exemption calculations or transactions, and that SPCL did not expect to be involved in any partial exemption until approximately October 2007. After further email exchanges, Mr Pate stated that before repayment could be issued, HMRC had to carry out a visit to look at the company structure and supplies in more depth. A visit was subsequently arranged for 1 February 2007.

25. Following the visit, Ms Powell of HMRC wrote to SPCL on 14 February 2007 enclosing a note of HMRC's understanding of what had been said at the visit. She also requested further information. SPCL provided a response on 23 February 2007. Further requests and responses followed, the final stage being a letter from Mr Gamiet to Ms Powell dated 16 July 2007, which was acknowledged by Ms Powell on 26 July 2007, stating that she had referred the case again to HMRC's Policy Department.

26. On 16 January 2008 Ms Powell responded with her decision on the VAT treatment of the VAT supplies made by SPCL to SPNH and LNH. She set out detailed reasons for her decisions and explained the consequences flowing from them. (With her letter she enclosed a four-page Annex setting out the background.) In the main letter she stated her view on behalf of HMRC:

> "2. My decision is that the supply of the lease of the property Sunnyside Private Nursing Home, the supply of the kitchen equipment and the supply of utilities; Electricity, Gas and Water are a single composite supply.
>
> 3. In addition I put you on notice that I have doubts that you have in fact successfully implemented a change in the contractual position with the suppliers of the utilities and the consumables and that the utilities and consumables therefore continue to be supplied to SPNH and not SPCL. We may investigate the contractual position further."

27. On 15 February 2008, SPCL requested an independent reconsideration of Ms Powell's decisions. SPCL followed this request with a letter dated 23 February 2008 setting out various matters to be taken into account in that reconsideration. Following a letter from Richard Taylor of HMRC's Appeals Unit notifying Mr Gamiet that he would be acting as independent reviewer of the decision, Mr Gamiet wrote to Mr Taylor with further information. After further exchanges of letters, Mr Taylor wrote on 23 May 2008 to Mr Gamiet setting out the result of the internal review. Mr Taylor

upheld Ms Powell's decision, and set out detailed reasons for his views. (As these matters are considered below, we do not think it necessary to set them out at this point.)

28. On 10 June 2008 SPCL gave Notice of Appeal to the VAT and Duties Tribunal against HMRC's decision as confirmed on review.

29. On 2 September 2008 Ms Powell wrote to SPCL setting out adjustments to be made to its September 2006 and December 2006 VAT returns. She stated that she would be making adjustments to the other VAT returns submitted when she had received from Mr Gamiet more details about how the figures declared had been calculated. She set out the normal information concerning SPCL's right to appeal these assessments to the VAT and Duties Tribunal. She enclosed documents formally assessing the tax due.

30. On 12 September 2008, HMRC filed their Statement of Case with the VAT and Duties Tribunal.

31. On 3 October 2008 Ms Powell wrote to Mr Gamiet with queries on VAT summaries which he had provided with his email dated 8 September 2008. He responded on 14 October 2008; he provided information, but explained that in relation to her VAT calculation for periods 09/06 and 12/06, he would await her calculations for the remaining returns before commenting so that he could consider all the VAT returns to May 3008 at the same time.

32. On 12 December 2008 further assessments in respect of the March 2007 and May 2007 VAT returns were notified to SPCL.

33. Further correspondence continued until 2013. During that period, HMRC issued further assessments and made further adjustments to the amounts of VAT to which SPCL was liable. On 16 November 2011, HMRC issued an assessment in respect of the VAT which would be due if HMRC were to lose the appeal notified by SPCL on 10 June 2008. This was for a Capital Goods Scheme adjustment which on such basis should have been declared by SPCL in the November 2009 VAT quarter. On 30 October 2012 a further similar assessment was made in relation to the Capital Goods Scheme adjustments that (on the same assumption) should have been declared by SPCL in the November 2010 and November 2011 VAT quarters.

34. By Directions issued on 7 February 2011, Judge John Walters QC directed that the appeal (LON/2008/1364) be stayed behind the decision of the CJEU in *Field Fisher Waterhouse* (Case 392/11).

35. On 31 January 2013 further assessments were issued as a consequence of HMRC's decision letter dated 16 January 2008 (and a further decision dated 15 August 2011). These related to the returns for periods August 2011 to November 2012, and to a Capital Goods Scheme adjustment in the November 2012 quarter (made on the basis of the assumption referred to above).

36. SPCL made late appeals in respect of a number of the assessments made by HMRC. As these were the subject of an application by SPCL at the beginning of the hearing, they are considered later in this decision.

Arguments for SPCL

37. Mr Moll submitted that in order to resolve the main points at issue, the following points had to be decided:

(1) Was SPCL was making a single composite supply (as HMRC argued), or multiple supplies that were either exempt or taxable?

(2) If SPCL was making a single supply, was part excluded from exemption because the supplies would not normally be associated with leasing of immovable property?

(3) Was the input tax on the building contract directly attributable to the exempt supply of rent [ie the exempt supply under the lease] as HMRC contended, or was it partly attributable to taxable (actual and intended) supplies?

38. There were various supplemental questions relating to the appeal, as the main decision had been extended to additional matters:

(1) Did the supply of freestanding equipment not affixed to the building and maintained by SPCL constitute part of an exempt supply or a separate taxable supply after 1 June 2008?

(2) Did the supply of telephone services using equipment owned and maintained by SPCL constitute part of a single exempt supply or a separate taxable supply after 1 June 2008?

(3) Did the supply of satellite television services using equipment owned and maintained by SPCL constitute part of an exempt supply or a separate taxable supply after 1 June 2008?

39. We consider below Mr Moll's detailed submissions on the facts, and so do not set them out here. In addition to provisions of the Sixth VAT Directive (1977), he referred to Articles 1, 2, 4 and 9 of Council Directive 2006/112/EC ("the Principal Directive"), and on the question of deduction, Articles 167, 168 and 173 of the Principal Directive. Capital goods were covered by Article 189 of the Principal Directive. The relevant domestic UK legislation was principally ss 24, 25 and 26 of the Value Added Tax Act 1994 ("VATA 1994") and in reg 101 of the Value Added Tax Regulations 1995 (SI 1995/2518) ("the VAT Regulations"). He emphasised that the reference in s 24(1) VATA 1994 to "goods or services used or to be used" gave a right of deduction when supplies were made, not necessarily when they were paid for. The language of s 24(1) VATA 1994 was repeated in reg 101(2)(d) of the VAT Regulations. He referred to various other provisions of the VAT Regulations.

40. On the question of single or multiple supply, Mr Moll referred to *Card Protection Plan* (Case 349-96) [1999] STC 270 at [29], *Aktiebolaget NN v*

Statteverket (Case C-111-05), [2008] STC 3203, *Don Bosco Onroerend Goed BV v Staatssecretaris van Financiën* (C-461-08) [2010] STC 476 at [35], and *Everything Everywhere Ltd (formerly T-Mobile (UK) Ltd) v Revenue and Customs Commissioners* (Case C-276-09) [2011] STC 31 at [21].

41. In relation to property transactions, he referred to *Field Fisher Waterhouse* (Case 392-11) [2013] STC 136 and *RLRE Tellmer Property sro* (Case C-572/07) [2009] STC 2006. He referred also to *Antiques Within* [2013] UKFTT 089 (TC) (TC02507), and to *Revenue and Customs Commissioners v Weald Leasing Ltd* (Case C-103/09) [2011] STC 596. He submitted that the case of *Gosling Leisure Ltd* [2012] UKFTT 170 (TC) (TC01866) had similarities to the present case.

42. On the question of deductibility of VAT on the building contract, Mr Moll referred to the "direct and immediate link" test set out by the European Court of Justice ("CJEC") in *BLP Group plc v Customs and Excise Commissioners* (Case C-4-94) [1995 STC 424.

43. Mr Moll submitted an alternative argument. SPCL was making exempt supplies; this was partly the case, but there was also a direct and immediate connection between the VAT on the building contract and future taxable supplies, as well as those within the period of construction.

44. Following his oral submissions, Mr Moll provided final written submissions on the final day of the hearing. As there was no time at the hearing for him to respond orally to Mr Thomas's submissions, Mr Moll provided two further written submissions after the hearing, being SPCL's response to HMRC's submissions and SPCL's response to HMRC's final submissions. As these related to the facts and to the application of the law to the facts, we consider below the matters raised in them, together with Mr Thomas's submissions concerning factual matters.

Arguments for HMRC

45. Mr Thomas referred to the business of SPNH, which was exempt. As SPCL owned the freehold of the Iver property and had let the property to SPNH, this was an exempt supply. As SPCL and SPNH made exempt supplies, on conventional principles neither was in a position to recover its input tax. Mr Thomas submitted that the purpose of splitting the letting of the premises and the provision of facilities at the property was to achieve a taxable income stream for SPCL and so to provide for input tax recovery on the refurbishment costs of the premises. It was common ground that, regardless of the position concerning single or multiple supplies, the costs of the refurbishment project had a direct and immediate link with the exempt supply of the letting of the premises. SPCL would therefore need to establish that there was a direct and immediate link with one or more taxable supplies which it made.

46. SPCL sought to do so by means of a purported contractual separation of the supply of the nursing home premises between a lease and one or more facilities charges; this was argued to bring about separate supplies for VAT purposes. Mr Thomas commented that if those services were separate supplies, it was accepted that

they were taxable supplies. He emphasised that in order for this argument to succeed, it was necessary for SPCL to succeed in establishing that those supplies were separate supplies for VAT purposes, and that the refurbishment costs were a cost component of those separate supplies.

47. SPCL also relied on the making of supplies of food, medical costs and consumables. To achieve success with this argument, SPCL would have to establish that the refurbishment costs were a cost of those separate supplies, which HMRC accepted to be separate taxable supplies.

48. Mr Thomas made detailed submissions on factual issues, which we consider below.

49. On the "single or multiple supply" issue, HMRC's contention was that the supplies made under the lease agreement and the facilities agreements constituted a single supply. The legal principles were clearly set out in the case law of the CJEU and the higher courts in the UK. Mr Thomas referred to the requirement for the courts and tribunals of Member States to have regard to the economic reality of transactions rather than their legal form. Departure from the contractual analysis could affect not only the nature of the supplies but also what the supply was, where it was supplied and when it was supplied; an illustration of this was *MacDonald Resorts* (Case C-270-09). In *Maierhofer* (Case C-315/00) [2003] ECR I-563, the CJEU had referred at [27] to the wording of a provision of Community law, the context in which it occurred and the objectives of the rules of which it formed part. Mr Thomas cited the comments of the CJEU at [39]:

> "In order to determine whether a transaction comprises a letting or construction or repair work, account must be taken of its essential features . . . , irrespective of the way in which it might be artificially presented."

50. He referred to *Loyalty Management and Baxi* (Cases C-53/09 and C-55/09) [2010] STC 2651 at [39]-[42], in which the importance of economic realities had been emphasised.

51. In relation to single or multiple supply, the CJEU had set out in *Card Protection Plan* at [26]-[31] its answers to the first two questions referred to it by the House of Lords. (We consider below the application of those principles.)

52. In *Levob* (Case C-41/04) the CJEU had reiterated and developed the case law set out in *Card Protection Plan*.

53. Mr Thomas referred to *Part Service Srl* (Case 425/06) at [48]-[54]. The reference to the CJEU concerned the correct approach to the application of the principle of abuse of law. However, the CJEU held that it must first be addressed whether the contractual separation which entailed there being two suppliers of services was effective for VAT purposes. This showed that the application of the VAT legislation required a determination to be made as to whether, notwithstanding

the contractual position, supplies which were formally distinct could be considered for VAT purposes not to be separate supplies.

54. Further, the case involved purportedly separate supplies made by two separate entities (although members of the same financial group). Mr Thomas argued that the fact that the CJEU was prepared to contemplate a finding of one transaction even where there were (contractually speaking) two suppliers was an indication of the strength of the requirement to determine the real substance and significance from an economic point of view of the activities of taxable persons.

55. As mentioned above, the present main appeal had been stayed behind *Field Fisher Waterhouse*. HMRC considered that the decision of the CJEU in that case strongly supported their contentions in this appeal concerning the "single or multiple supply" issue. HMRC also argued that the supply of the lease and the supply of facilities by SPCL to SPNH constituted a single exempt supply, either because the supply of the facilities was ancillary to the principal supply of the lease (on the basis of the reasoning in *Card Protection Plan*), or because there was a single indivisible economic supply with the supply of the lease being the predominant element (following the reasoning in *Levob*).

56. In *Part Service Srl* and *Field Fisher Waterhouse*, the CJEU had not indicated any departure from the established *Card Protection Plan* and *Levob* line of authority. Mr Thomas emphasised the factual differences between both those cases and that of SPCL.

57. The principles in these two cases had been repeated in subsequent CJEU cases, including *Aktiebolaget NN*, *Don Bosco*, *Purple Parking* (Case C117/11), and *Finanzamt Frankfurt am Main V-Höchst v Deutsche Bank AG* [2012] STC 1951.

58. Mr Thomas referred to subsequent domestic UK case law, including *Dr Beynon* [2004] UKHL 53, *College of Estate Management* [2005] UKHL 62, *HMRC v Weight Watchers (UK) Ltd* [2008] EWCA Civ 715, and *HMRC v David Baxendale Ltd* [2009] EWCA Civ 831.

59. Although a copy of the case was included in HMRC's bundles of authorities for the hearing, Mr Thomas did not specifically draw our attention to the recent Upper Tribunal decision in *Revenue and Customs Commissioners v Hon. Society of Middle Temple* [2013] UKUT 0250 (TCC); this had been released at about the time when HMRC's skeleton argument had been served on the Tribunal. Mr Thomas therefore made written submissions on that case after the hearing, which we consider in our discussion of the legal principles set out below.

60. On the issue of attribution of input tax, Mr Thomas referred to ss 4, 26(1) and 26(2) VATA 1994 and to reg 101 of the VAT Regulations.

61. On deductibility of input tax in respect of the costs of refurbishment, the purpose of the VAT Directives was to impose a tax on the consumption by the final consumer of any goods and services received by him. Article 1(2) of Council Directive 2006/112/EC ("the Principal Directive") set out this foundation of the tax.

Mr Thomas referred to the basic principles of the VAT system. Article 173 of the Principal Directive dealt with the extent of the right of deduction where goods or services were used for both taxable and exempt purposes; it allowed deduction of "only such proportion of the VAT as is attributable to" taxable supplies.

62. The use of the words "for transactions" in Article 173 showed that to give rise to the right to deduct, the taxed costs must have a direct and immediate link with taxable outputs, and that the ultimate aim pursued by the taxable person was irrelevant in this respect. Mr Thomas cited *BLP Group plc* (C-4/94) at [19]-[23], and *Midland Bank plc v Customs and Excise Commissioners* (Case C-98/98) at [30]. It followed that a person who made exempt supplies was not entitled to deduct VAT in respect of those transactions and was therefore treated as the final consumer of such goods and services; *Ursula Becker v Finanzamt Munster-Innenstadt* (Case 8/81) at [44].

63. The test to determine whether a particular cost or purchase had been used to make a specific taxable supply was whether there was a direct and immediate link between the cost and the supply. UK case law had confirmed the test and also confirmed that it could alternatively be described as the "cost component" test (*Dial-a-Phone Ltd v Commissioners of Customs and Excise* [2004] STC 987 (CA) at [28]).

64. The test was not a "but for" test or a commercial linkage test (*Commissioners of Customs and Excise v Southern Primary Housing Trust* [2004] STC 209 (CA) at [32]-37]). The question had to be determined by reference to the economic reality of the transactions at issue. In other words, the use in question was "economic use" (*St Helen's School Northwood v Revenue and Customs Commissioners* [2006] EWHC 3306 (Ch) at [75]. While that case concerned the question of the fair and reasonable deduction of input tax under a special method, the concept of economic use was applicable to SPCL's appeal.

65. As SPCL accepted that in the event of its input tax claim being successful, adjustments under the Capital Goods Scheme would be appropriate, Mr Thomas did not make submissions concerning such adjustments. For the same reason, he did not add to submissions contained in his skeleton argument concerning the Standard Method Override.

66. On the question of costs, he proposed to leave this until the substantive issue had been determined.

67. Following Mr Moll's written submissions made after the hearing, Mr Thomas made a written reply to those submissions. We take into account below the respective supplementary submissions made by each party.

Discussion and conclusions

The late appeals

68. At the beginning of the hearing, Mr Moll applied for seven appeals, ie all of those listed above, other than the principal appeal under reference LON/2008/1364

and TC/2013/01318 (for which two appeals Notices of Appeal had been lodged within the time limit) to be entertained out of time. (For convenience, in this section of this decision we refer to the appeal under reference LON/2008/1364 as "the principal appeal".) It had been directed by Judge Berner that this application should be considered at the main hearing. Mr Moll explained that Mr Gamiet had thought that all the decisions and assessments would be covered by the principal appeal. In December 2012, following the decision in *Field Fisher Waterhouse* (behind which the present appeal had been stayed), SPCL had taken advice from Tax Counsel. Counsel had advised that appeals should have been made against all the decisions. The Notices of Appeal had therefore been given in January 2013.

69. Mr Moll referred to the "overriding objective" in Rule 2(1) of the Tribunal Rules, and to the decision of the Tribunal in *Former North Wiltshire District Council* [2010] UKFTT 449 (TC) (TC00714), in particular at paragraph 68. It was necessary to look at the applicant's culpability. Here considerable correspondence had been continuing as between SPCL and HMRC. He submitted that Mr Gamiet had had no reason to know that the separate decisions would not be considered as part of the appeal. Mr Moll's own role had been limited to giving advice in respect of normal appeal matters, whereas the conduct of the case had been retained by Mr Gamiet.

70. The second question to be considered was whether HMRC were prejudiced. This was not a case where HMRC had closed their files; they had made a further decision in relation to the Capital Goods Scheme. SPCL was not being asked to repay money; all repayments of input tax which it had claimed had been inhibited. HMRC's skeleton argument dealt with all the matters raised by all the appeals, including those covered by the application. Mr Moll submitted that despite contrary indications by HMRC, admitting the late appeals would not result in the matter being made more complicated, given that the matter had not yet been heard. He questioned whether it would be fair and just if the Tribunal were not to consider all the matters. He acknowledged that in Mr Thomas's skeleton argument relating to the applications, HMRC had withdrawn their objections to certain of the appeals being made out of time.

71. In summary, he submitted that it would not be fair and just if all matters arising out of the original decision were not considered in a single hearing, especially as the full range of such matters had been covered in both parties' skeleton arguments.

72. Mr Thomas referred to the legislative framework governing time limits for making appeals, and the discretion of the Tribunal to extend the time for complying with the time limit for bringing an appeal. The first three of the appeals related to decisions which gave effect to the original HMRC decision on 16 January 2008. As an appeal had been made in time against the decision on the question of principle, he confirmed that HMRC did not object to these three appeals being made out of time and consolidated with the principal appeal.

73. Appeal TC/2013/00067 was against a decision dated 22 September 2011 confirming the decision dated 15 August 2011 relating to freestanding equipment and telephone and other services and the adjustments made to returns for periods 02/08

and 02/09. It concerned matters which were not known to HMRC when they made the January 2008 decision, and related to a period of time after the original Facilities Agreements. HMRC's skeleton argument had addressed these matters. It was accepted that the evidence on these issues had been presented and considered by HRMC, and therefore, despite the appeal being on any view woefully late, HMRC did not intend to maintain its objection to the appeal being made out of time. Mr Thomas emphasised that this agreement was being made by concession only, and that it should not be assumed that HMRC would be prepared to make such a concession in any other case.

74. The remaining three appeals were all against protective assessments which had been issued to protect HRMC's position in the event that the Tribunal were to decide against the position being maintained by HMRC in respect of the principal appeal. They had thus been calculated on the basis that SPCL's contentions were right. That being the case, Mr Thomas argued that these appeals as submitted were also defective in failing to set out the grounds of appeal. No independent basis had been set out for challenging the decisions made. As HMRC's objection was only to these assessments which would only become relevant if the decision in the principal appeal went against HMRC, he submitted that there was no need to make a decision on these at this point; directions would have to be made concerning them if SPCL were successful in relation to the principal appeal.

75. In relation to *North Wiltshire*, he emphasised that the Tribunal was not bound by that decision, and that the issue was pre-eminently within the discretion of the Tribunal; this involved no principle of law.

76. Mr Moll responded that SPCL's position was very similar to that of HMRC's; if the Capital Goods Scheme assessments were ultimately to be applied, SPCL would not contest them. SPCL's position was that on these three disputed assessments, it would want them included in the list of appeals covered by the Tribunal's decision, but accepted that if the principal appeal was successful, these three appeals would be withdrawn.

77. We must emphasise that, although HMRC indicated that they would not object to the majority of the appeals being admitted out of time, the decision whether to admit any appeal out of time is entirely a matter for the discretion of the Tribunal in the light of the circumstances of any particular case. As Mr Thomas submitted, this discretion is provided by Rule 5(3)(a) of the Tribunal Rules, and is to be exercised in conformity with the overriding objective set out in Rule 2.

78. We deal first with the appeals other than the three against the protective assessments (the latter being numbered TC/2013/00065, TC/2013/00237 and TC/2013/00066). We are persuaded, in the particular circumstances of the present case, that the various and lengthy delays in the giving of notice of these appeals are outweighed by the importance of resolving all the matters in the context of the principal appeal. We would regard it as unsatisfactory for a series of separate hearings to be required, dealing with what are in essence similar issues, particularly as these separate hearings might take place before various differently constituted Tribunals.

79. We therefore accept SPCL's application for extension of time to appeal and consolidate the appeals (other than those against the protective assessments) with the principal appeal.

80. In accepting the application, we emphasise that our decision should not be taken as any indication of the way in which any other similar application may be treated in the future. As the Tribunal indicated at paragraph 68 of the *North Wiltshire* decision, a balancing exercise is necessary as between an assessment of an appellant's culpability in delaying the lodging of notice of appeal and the prejudice to HMRC in terms of the public interest in good administration and legal certainty, weighed against the loss and injury to that appellant if an extension of time is refused.

81. In relation to the three appeals against the protective assessments, we need to take into the account the possibility that, even if SPCL's appeal before us is not successful, our decision might be reversed or amended as a result of a further appeal. The practical answer is for us to accept SPCL's application for extension of time in respect of these three appeals, but not to consolidate them with the principal appeal. In the event that any further proceedings were to prove necessary in relation to those appeals, appropriate directions would have to be given in relation to such proceedings.

The consolidated appeal

82. Before considering the detailed factual evidence relating to SPCL's claims for recovery of input tax, we review the relevant legal principles.

The law relating to the "single or multiple supply" issue

83. Rather than producing our own summary of the principles to be derived from a number of the CJEU cases which Mr Moll and Mr Thomas took us through, we think it appropriate to use the definitive statement of those principles as set out by the Upper Tribunal in the *Middle Temple* decision at [60]:

> "60. The key principles for determining whether a particular transaction should be regarded as a single composite supply or as several independent supplies may be summarised as follows:
>
> (1) Every supply must normally be regarded as distinct and independent, although a supply which comprises a single transaction from an economic point of view should not be artificially split.
>
> (2) The essential features or characteristic elements of the transaction must be examined in order to determine whether, from the point of view of a typical consumer, the supplies constitute several distinct principal supplies or a single economic supply.
>
> (3) There is no absolute rule and all the circumstances must be considered in every transaction.
>
> (4) Formally distinct services, which could be supplied separately, must be considered to be a single transaction if they are not independent.

(5) There is a single supply where two or more elements are so closely linked that they form a single, indivisible economic supply which it would be artificial to split.

(6) In order for different elements to form a single economic supply which it would be artificial to split, they must, from the point of view of a typical consumer, be equally inseparable and indispensable.

(7) The fact that, in other circumstances, the different elements can be or are supplied separately by a third party is irrelevant.

(8) There is also a single supply where one or more elements are to be regarded as constituting the principal services, while one or more elements are to be regarded as ancillary services which share the tax treatment of the principal element.

(9) A service must be regarded as ancillary if it does not constitute for the customer an aim in itself, but is a means of better enjoying the principal service supplied.

(10) The ability of the customer to choose whether or not to be supplied with an element is an important factor in determining whether there is a single supply or several independent supplies, although it is not decisive, and there must be a genuine freedom to choose which reflects the economic reality of the arrangements between the parties.

(11) Separate invoicing and pricing, if it reflects the interests of the parties, support the view that the elements are independent supplies, without being decisive.

(12) A single supply consisting of several elements is not automatically similar to the supply of those elements separately and so different tax treatment does not necessarily offend the principle of fiscal neutrality."

84. Although Mr Thomas did not make submissions on *Middle Temple* at the hearing, we are satisfied that, as a result of his subsequent written submissions, he gave sufficient opportunity to Mr Moll and to us to consider the implications of the Upper Tribunal's decision. In our consideration of the application of the legal principles to the facts, as set out in the next section of this decision, we take the above principles into account. Mr Thomas submitted that the decision in *Middle Temple* was directly analogous to this appeal and showed the effect of applying the decision in *Field Fisher Waterhouse* in circumstances of this nature.

85. Both parties referred to other cases not specifically mentioned by the Upper Tribunal in *Middle Temple*, both CJEU and domestic, relating directly or indirectly to single or multiple supplies, and we therefore consider those before dealing with the factual issues.

86. Mr Moll relied on *Aktiebolaget NN* as supporting the proposition referred to in *Everything Everywhere* at [21] that:

> "It follows from art 2 of the Sixth Directive that every transaction must normally be regarded as distinct and independent . . ."

Mr Thomas submitted that *Aktiebolaget NN* at [25] supported HMRC's position:

> "It follows therefrom, firstly, that all the elements of the transaction at issue in the main proceedings appear to be necessary to its completion and, secondly, they are all closely linked. In those circumstances, it is not possible, without undue contrivance, to take the view that such a consumer will acquire, firstly, the fibre-optic cable and, subsequently, from the same supplier, the supply of services relating to the laying thereof (see, by analogy, *Levob Verzekeringen and OV Bank*, paragraph 24)."

87. We are satisfied that both these propositions are consistent with the relevant principles summarised by the Upper Tribunal in the *Middle Temple* case. Further, the statement in *Everything Everywhere* at [21] is balanced by the comments at [22]-[26], so again the views of the CJEU are appropriately reflected in the Upper Tribunal's summary of the applicable principles.

88. In relation to *Don Bosco*, the position is similar, with the CJEU balancing the respective "independence" and "indivisible economic supply" principles; Mr Thomas relied on the comments in the CJEU's judgment at [39] referring to "undue contrivance".

89. In his written submission in response to HMRC's submissions, Mr Moll argued that one of the factors in deciding whether there was a single supply or multiple supplies was the customer's choice. He relied on *Weald Leasing* at [27] for the proposition that the taxable person had the choice of transactions and did not have to choose the one that produced the highest return of tax.

90. In his written reply, Mr Thomas argued that Mr Moll's latter submission was misconceived. The relevance of choice in the context of the application of *CPP/Levob* had been well summarised by the UT in *Middle Temple*. It was not concerned with the application of the EU principle of abuse of law. The reference to choice in the context of *CPP/Levob* was that it was a relevant but not decisive factor in determining the single/multiple supply question that a customer had a real choice as to who provided the goods or services in question.

91. Nor was the reference to choice concerned with the intention of the parties to particular transactions to designate them in a particular way. If parties to transactions could split what would otherwise be a single supply into multiple supplies simply by choosing to sign two agreements rather than one the uniform application of VAT would be undermined. The application of *CPP/Levob* was a test of substance, not of form.

92. We accept Mr Thomas's reply submissions concerning the issue of choice, which we consider to be entirely in accordance with the Upper Tribunal's analysis in *Middle Temple*.

93. Mr Moll referred to the decision of the First-tier Tribunal in *Antiques Within Ltd*, in which the Tribunal had concluded, without either party having sought such a conclusion, that the stallholders were receiving two separate and independent supplies, neither of which could be seen as merely incidental to or ancillary to the other. He submitted that the Tribunal had looked at the position from the "customer's" point of view, and that the customer's intention therefore had to be taken into account.

94. In his reply, Mr Thomas submitted that the *Antiques Within* case was not analogous with the present case; it was simply an application of the *CPP/Levob* principle in another context.

95. We do not consider that *Antiques Within* is of assistance in the present case. The principles set out in *Middle Temple* at [60] sub-paragraphs (10) and (11) are clear, and we agree with Mr Thomas's comments on *Antiques Within*.

96. In relation to Mr Thomas's submissions concerning economic reality rather than legal form, we accept that these are supported by the respective CJEU authorities which he cited, and that the economic reality of the transaction is the key to the analysis.

97. Mr Thomas referred to *Loyalty Management and Baxi*, with the CJEU's emphasis on the importance of economic realities. Although neither party to the present appeal made any mention of it, it is clear from the judgments of the majority in the Supreme Court (under the amended name *HMRC v Aimia Coalition Loyalty UK Ltd* [2013] UKSC 15) that there had been difficulties as a result of the form of the reference made to the CJEU by the House of Lords, and that the CJEU had not addressed the facts on the basis of which the Supreme Court had to proceed or the issues at the heart of the dispute. However, in the context of Mr Thomas's submissions, we do not think that this affects the authority of the statement made by the CJEU at [39]:

> "It must also be recalled that consideration of economic realities is a fundamental criterion for the application of the common system of VAT . . ."

The law relating to Attribution of Input Tax/Deductibility of input tax on the costs of refurbishment

98. Mr Moll submitted that SPCL fulfilled the "direct and immediate link" test set out by the CJEU in its judgment in *BLP* at [19]. Mr Moll acknowledged the Advocate General's statement in his Opinion at [33] that:

> "Those details logically do not change the fact that input tax can be deducted only to the extent that the goods or services on which it has been paid are 'cost components' of a taxable transaction. On the contrary, the identification of goods and services as such cost components becomes all the more important with the introduction of the category of exempt transactions, since those transactions do not give the right to deduct input tax, any more than economic operations

> do which are outside the VAT system and thus even under the First Directive confer no right to deduct input tax."

99. Mr Thomas emphasised the Advocate General's statement at [31] that:

> ". . . the amount which is to be deducted as input tax must have been 'borne directly by the various cost components'."

Mr Thomas also referred to the Advocate General's comment at [34]:

> "In particular, as follows from the system which has been demonstrated, in applying Article 17(2)(a) goods or services which have been identified as cost components of a specific exempt supply of services cannot be attributed to other supplies of services which are subject to VAT."

100. Mr Thomas submitted that the comments in the CJEU's judgment at [19]-[20], that the goods and services must have a direct and immediate link with the taxable transactions and that the ultimate aim pursued by the taxable person was irrelevant, showed that an ultimate intention to make taxable supplies was insufficient to give a right to deduct. The position had been confirmed in *Abbey National plc v Customs and Excise Commissioners* (Case C-408/98) 1 WLR 769, [2001] STC 297, in which the Advocate General had commented in his Opinion at [35] that:

> ". . . the 'chain-breaking' effect which is an inherent feature of an exempt transaction will always prevent VAT used on supplies used for such a transaction from being deductible from VAT to be paid on a subsequent output supply of which the exempt transaction forms a cost component. The need for a 'direct and immediate link' thus does not refer exclusively to the very next link in the chain but serves to exclude situations where the chain has been broken by an exempt supply."

101. We accept Mr Thomas's submissions as to the law concerning this issue; we consider the relevant factual questions later.

102. Mr Moll referred to the decision of the Tribunal in *Gosling Leisure Ltd* [2012] UKFTT 170 (TC), TC01866 as authority for the proposition that capital costs incurred by the appellant ("GLL") were directly and immediately related to supplies made by GLL, so as to rank as deductible input tax, the chain break in GLL's case being that it was a tenant in a building owned by its parent company. In reply, Mr Thomas commented that Mr Moll's analysis of *Gosling Leisure* in the context of chain breaking supplies was wrong; there was no lease in *Gosling Leisure*, and therefore no exempt supply. We accept Mr Thomas's submission that the decision cannot be taken as authority in the context of SPCL's position.

103. We accept Mr Thomas's remaining submissions (set out at paragraphs 61 to 64 above) on the law relating to the deductibility of input tax and the attribution of input tax.

104. On the basis of our conclusions on the law applicable in SPCL's circumstances, we consider the facts in the light of the relevant principles.

Whether on the facts there was a single or multiple supply

105. Mr Moll argued that there were two separate agreements, a lease agreement for the bare rental of the property (which was an exempt supply), and a facilities agreement for various additional services, which he submitted were taxable supplies.

106. Mr Thomas submitted that on a conventional application of the relevant tests, the supplies made under the lease dated 1 April 2006 and the Facilities Agreement of the same date constituted a single exempt supply for VAT purposes, and that in the same way, the supplies made under the lease dated 1 April 2006 and the Facilities Agreement dated 1 June 2008 constituted a single exempt supply for VAT purposes, the authorities in each case being *Card Protection Plan* and *Levob*. He argued that there was nothing in the latter conclusions which was in conflict with any decided case or principle, and that the VAT treatment contended for by HMRC was in line with that of (for example) furnished leases.

107. In cross-examination, Mr Gamiet confirmed that when SPCL had taken over the Iver property in 2003, no written lease had been entered into. The annual rent had been around £35,000. SPCL had made no separate charge for the kitchen, and had not made any supplies relating to the utilities. The telephone system had not been sold back from SPNH to SPCL; Mr Gamiet had not known that it needed to be. He accepted that it had been owned by SPNH. There had been no separate charge to SPNH for the kitchen, utilities or equipment of any description, nor was there any charge for facilities even afterwards. SPNH was invoiced directly by the utility providers and by the provider of telephone services. We are satisfied that this evidence is correct, and also find that in correspondence with HMRC, Mr Gamiet confirmed that no part of the property was excluded from the (unwritten) lease.

108. Before the building works, the offices on the top floor of the Iver property owned by SPCL were used by the directors of TGL and the other group companies and by other personnel working for TGL. There was no evidence of any formal arrangement for this use, or of any payment being made to SPCL.

109. We find that, before VAT advice was sought in 2006, arrangements between SPCL and SPNH were dealt with on a very informal basis, as shown by the absence of written lease documentation. As confirmed by the various accounts of SPCL, SPNH, and TGL included in the evidence, the companies in the TGL group are "related parties". The companies in the TGL group do not operate on commercial arm's length terms. We are satisfied that the activities of SPCL and SPNH are largely, if not entirely, directed by Mr Gamiet.

110. In relation to the obtaining of VAT advice, Mr Gamiet stated that he had been put in touch with Mr Moll by his accountants, Eacotts. On 10 February 2006 Mr Gatehouse of Eacotts had written to Mr Gamiet referring to his recent meeting with Mr Moll. Mr Gamiet confirmed that he and Eacotts had been at the meeting. He had requested that the letter should set out a summary of what he described as Eacotts' suggestions for VAT saving. The first three paragraphs of the Summary stated:

> "It is not possible to VAT register [SPCL] to charge VAT on the rental payments made by [SPNH]. In that event, an alternative means of creating vatable income needs to be established.
>
> One such method is to have separate rental and facilities agreement. The rent will be VAT exempt but the facilities charge should be subject to VAT at the standard rate. In principle, this will give [SPCL] a right to recover some of the VAT incurred on its redevelopment.
>
> The standard method to recover VAT on a mixed use asset is based on income ratios. If [SPCL] increases the amount of VATable income, the recovery of VAT will increase. [SPCL] could increase its VATable income by being the central supply point for food and other expenditure currently paid for by the individual home operating companies (except wages)."

(We do not find it necessary to quote further from this letter, which indicated that a challenge by HMRC to SPCL's input tax recovery was likely, and continued by setting out in greater detail both information concerning the matters covered in the summary and the steps which would be required to implement the suggested arrangements.)

111. Mr Gamiet stated in cross-examination that the proposals had been put forward by him. He had not produced a written business plan, and the letter from Eacotts had been the only contemporaneous evidence of the proposals. The reference on the final page of the letter to "David's suggestions" had been to the matters on which he had taken advice in the discussion with Mr Moll. Subsequently he had tried to arrange a conversation between Mr Moll and the lawyers, but he did not know whether this had happened.

112. On 10 March 2006 Mr Gatehouse wrote to Mr Gamiet; the enclosure to his letter was described as "an implementation programme for the VAT planning arrangement". The name at the bottom of the enclosure was "David Moll". In cross-examination, Mr Gamiet stated that he had not written to suppliers in March 2006 as recommended to notify them of the change of accounts to SPCL with effect from 1 April 2006, as he had been busy with the building project and the sale of the FANHL business. He referred to letters eventually sent to the suppliers, and indicated that he accepted these to have been undated; he stated that this had been an oversight. (We make findings below as to the existence of any such letters.)

113. Mr Thomas invited us to make various findings concerning the obtaining of VAT advice. To a substantial extent, we agree with the points which he raised in this context. We find that, before entering into the arrangements in question in this appeal, SPCL sought and obtained VAT advice, that the suggestion of splitting the lease from services provided to SPNH was made by Mr Moll, that the detail of the structure was set out by Eacotts in their letters dated 10 February and 10 March 2006, the latter containing a timetable for the completion of the arrangements set out by Mr Moll, and that on 14 March 2006 Mr Gamiet sent an email to solicitors requesting them to draw up agreements between SPNH and SPCL to implement the arrangements as set out in the two letters from Eacotts as attached to the email.

114. We also find that there is no contemporaneous evidence to show that SPCL had independently considered entering into the arrangements set up in 2006 for any reason other than the possibility of saving, or at least deferring, VAT.

115. In his arguments on behalf of HMRC, Mr Thomas did not seek to argue that what had been put in place was an abusive arrangement; in particular, he argued that *Weald Leasing* was of no assistance in the context of SPCL's case. We would not go as far as to describe the arrangements as abusive, despite the clear intention to take advantage of the VAT legislation in order to seek recovery of input tax which in all probability would not otherwise have been recoverable. Thus in this appeal the intentional setting up of the arrangements is not relevant in the context of abuse. We consider below whether it may have relevance to the question of "contrivance", an expression used in certain CJEU cases, or to the issue of economic reality.

116. On this basis, the two questions raised by this aspect of SPCL's appeal are:

(1) Whether the arrangements were in principle capable of achieving their desired effect, namely to enable SPCL to recover a significant proportion of the VAT incurred on the construction project; and, if so,

(2) Whether the way in which the arrangements were actually implemented was such as to produce that intended result.

117. On the first question, we agree with Mr Moll's submission that the starting point is the first of the key principles set out by the Upper Tribunal in *Middle Temple* at [60] (see paragraph 83 above). However, the principle that every supply should normally be regarded as distinct and independent is qualified by the requirement to examine the particular circumstances of the transaction, as demonstrated by the questions raised by the second part of principle (1) and by principles (2) to (12). We therefore consider the terms of the arrangements in the light of those principles.

118. In terms of the second part of principle (1), that a supply which comprises a single transaction from an economic point of view should not be artificially split, Mr Thomas submitted that the contractual arrangements were an unreliable and incomplete account of the economic reality. He emphasised that the parties were all related parties, that there was no evidence that the agreements had been negotiated at arm's length, and that the purported contractual separation did not reflect any real choice on SPNH's part as to the party or parties from which it was to purchase utility services or kitchen and any other facilities.

119. In *Middle Temple*, the Upper Tribunal agreed (at [66]) that water is not normally supplied under a lease. At [70]-[71], It found that the choice was to take a lease of the premises which included the provision of water by the Middle Temple or not to take any lease at all, and concluded that the two elements were not only inseparable but also indispensable in relation to the letting and use of the premises from the point of view of a typical tenant. It followed (in the light of *Levob*) that those elements formed a single indivisible economic supply which it would be artificial to split.

120. The circumstances in *Middle Temple* were unusual, in that there was no possibility of tenants obtaining water supplies from other suppliers. We find that in the present case, SPNH was originally obtaining its water supplies from an external third party utility supplier. The 2006 Facilities Agreement made no change to this arrangement. It was not until the entering into of the 2008 Facilities Agreement that water became one of the services listed in Schedule 1 to that agreement. (We consider separately below whether in practice the provisions of that Schedule were properly implemented.) In the same way, water was listed in Schedule 1 to the 2010 Facilities Agreement as a service to be provided by SPCL pursuant to clause 2 of that agreement.

121. In the 2006 Facilities Agreement, the services listed in Schedule 1 were gas, electricity, and "kitchen". There is a lack of clarity in the latter expression, and in the course of Mr Moll's presentation at the hearing there appeared to be some variation in the interpretation to be put on it.

122. In Schedule 1 to both the 2008 Facilities Agreement and the 2010 Facilities Agreement, the services listed were gas, electricity, water, kitchen equipment usage, furniture and equipment usage, telephone services for [SPNH], telephone services for residents, satellite TV for residents and internet services for residents. (Separate questions concerning the facilities for residents are considered below.)

123. The question arising from SPCL's submissions on the single or multiple supply issue has some similarities to that considered by the Upper Tribunal in *Middle Temple*; was the choice for SPNH either to take the lease of the premises together with the benefits and commitments under the Facilities Agreements, or not to enter into either? We are not satisfied that SPNH had any such choice. We accept Mr Thomas's submissions concerning the absence of economic reality in the contractual arrangements. SPNH's objective was to continue its nursing home business. It could only do so with the benefit of the services which had been separated out in order to be covered by the Facilities Agreements.

124. At one stage in correspondence, HMRC had referred to the provision of a "fully functioning" nursing home. Mr Moll cited this reference, indicating that Mr Thomas had made a similar point in summarising HMRC's case. Mr Moll submitted that SPCL could not possibly be providing a fully functioning nursing home to SPNH under the lease agreement, because SPNH continued to procure equipment from third party suppliers (such as laundry equipment). He argued that this involved HMRC in claiming that SPCL was providing a partially functioning nursing home, as to (say) 90 per cent and that in some way there was something special about the supplies made under the Facilities Agreement which meant that they were part of a single exempt supply. This was inconsistent with the treatment of other supplies made by SPCL and other suppliers.

125. We think it misleading to test the issue by asking whether SPNH was being provided with a fully functioning nursing home. The appropriate question is whether SPNH could continue to run its nursing home business without the services specified in the Facilities Agreements. Whether it needed to have other services provided to it

(either by SPCL or third party suppliers) in order to continue to carry on that business is a separate issue which does not affect that main question.

126. We find that the basis on which the rent for the Iver property was determined is relevant to that question. Mr Gamiet stated in evidence that once the properties had been transferred after the restructuring, a rent was paid from the nursing home trading companies to the property companies; at that stage there was no formal lease. We accept that evidence.

127. The timing of the Weatheralls valuation was such that it was available when the rent payable by SPNH to SPCL was determined. Taking the valuation of Sunnyside Nursing Home at £625,000, our calculation shows that the rent of £35,000 per annum represents a yield of 5.6 per cent. When the lease was entered into on 1 April 2006, the rent was kept at the same level. It follows that the rent charged under the 2006 lease must have been arrived at on the same basis, namely viewing Sunnyside Nursing Home as a "fully operational business unit" as referred to in the Weatheralls valuation. According to the notes of the meeting with HMRC on 1 February 2007, Mr Gamiet thought this to be a market rent. When subsequently asked to explain why he took this view, he responded in his letter dated 23 February 2007:

> "A valuation of £625,000 was used. This was the value used when the property was transferred from [SPNH] to [SPCL]. The figure came from an independent valuation. We took a rental value of £35,000 which represents a rental yield of 5.65% which we felt was appropriate.
>
> . . .
>
> It is notoriously difficult to determine a "market rent" for a care home. We have observed that conventional commercial property rental yields typically range from 1% or so below the 5 year swap rate up to 4% or 5% above the 5 year swap rate. Care home valuations however are heavily dependent on the performance of the care service itself and it can be difficult to determine what element is due to the freehold property and what is due to the care element itself. We felt that the rent levels selected broadly reflected a commercial property yield."

128. Subject to our slightly different conclusion as to the yield percentage, we find that the above statements support our view that the rental valuation was based on the valuation of Sunnyside Nursing Home as a "fully operational business unit", so that in economic terms the rent reflected significantly more than the provision of what Mr Gamiet described in his witness statement as "the bare hire of the premises". Further, that rent was determined at the point when there was no separate provision of facilities, and was continued at the same level (subject to the rent-free period, considered below) during the three year term of the lease. As the rent took into account the value of Sunnyside Nursing Home as a fully operational business unit (a concept which we consider to be different from that of a "fully functioning nursing home"), the level of that rent necessarily implied that SPNH would be provided with something more than "the bare hire of the premises".

129. In their valuation, Weatheralls stated:

> "The properties fall into a category which normally changes hands in the open market as fully operational business units. Our valuations, therefore, include all plant, machinery, fixtures and fittings, furniture and moveable items as these are usually included in the sale."

Clearly, therefore, the rent based on their valuation would be expected to entail the provision of such items, rather than these being provided under a separate agreement as part of matters covered by an additional charge for the provision of facilities.

130. We find that SPNH could not have continued to run its business without the services specified in the Facilities Agreements, and that the way in which the rent under the 1 April 2006 lease was calculated took no account of the effect of this on the valuation forming the basis for that calculation.

131. On the issue of whether SPNH had any genuine choice as to its suppliers, Mr Thomas invited us to make the following findings:

(1) Any choice which SPNH might have made to receive from elsewhere the services under the 2006 Facilities Agreement (and similarly in relation to the 2008 and 2010 Facilities Agreements) would have negated the whole point of the arrangements;

(2) Any choice which SPNH might make to receive from elsewhere the services of equipment hire would have been directly contrary to the interests of SPCL as the asset owning company;

(3) The decision of SPCL to enter into these arrangements required SPNH to change its arrangements for the supply of utilities;

(4) The kitchen work had been part of the contract since its inception and SPNH had no realistic option not to take the whole of the kitchen supplied by SPCL;

(5) At no point had SPNH sought to have any of the services referred to under the Facilities Agreements supplied by any other person, and there was no evidence of it having considered obtaining these services from a third party;

(6) The supplies were not, in any event, "take it or leave it" supplies; they were all essential to SPNH's activities.

132. As the motivation of Mr Gamiet, who clearly acted as the principal director of both SPCL and SPNH, was to follow the VAT advice which he had sought, we are satisfied that in practice SPNH had no choice but to enter into the arrangements made pursuant to that advice, and we accept Mr Thomas's invitation to make the findings set out in the preceding paragraph.

133. In making those findings, we also take into account the effect on SPNH as the "consumer" of the arrangements. As Mr Thomas submitted, its business as a nursing home is exempt under Item 9(b) of Group 7 of Sch 9 VATA 1994 (taking into account Notes 6 and 8 to Group 7, and SPNH's registration with the Commission for Social Care Inspection). Any VAT which it incurs is therefore likely to prove irrecoverable, because it makes exempt supplies. Thus any arrangement under which supplies to it

are taxable supplies, rather than exempt supplies, will add to its irrecoverable input tax. Separate provision of facilities under a Facilities Agreement which might otherwise have been provided as part of the exempt supplies under a lease will therefore result in a disadvantage to SPNH. Under the 2006 Facilities Agreement, the provision of "Kitchen" appears to us to have this result. Under the 2008 and 2010 Facilities Agreements, this appears to be the case for "Kitchen Equipment Usage" and "Furniture and Equipment Usage". We find that, if SPNH had been negotiating at arm's length, it would have wished to take into account any such potential disadvantages before agreeing the terms of the lease and the Facilities Agreements.

134. Thus the arrangements lacked commerciality, and did not reflect economic reality; we find that the split between the supply of the property under the lease and the supply of services under the Facilities Agreements was artificial.

135. In *Middle Temple*, the First-tier Tribunal had found that the supply of water was an aim in itself for the tenants. The Upper Tribunal did not interfere with that finding of fact, but stated (at [62]) that the fact that the supply of water was an aim in itself did not mean that such supply was not indivisible from the supply of the premises. The Upper Tribunal continued:

> "The FTT's finding means that the supply by the Middle Temple cannot be regarded as a composite single supply under a *CPP* principal/ancillary analysis but still leaves open the possibility of a *Levob* indivisible/artificial to split single supply."

136. In the present case, we do not consider it possible to find that the provision of water, other utilities and kitchen-related services amounts, from SPNH's point of view as the recipient of all such services, to an aim in itself. We regard these services as essential to the carrying on of the nursing home business. Even if we were considered to be wrong in our view that they are essential, we would still regard them as a means of enjoying the principal service, namely that of the provision under the lease of the premises for use by SPNH in carrying on its nursing home business.

137. Ignoring for the present the question of implementation, we find that there was separate invoicing and pricing in respect of the services provided under the Facilities Agreements. However, it is clear from *Middle Temple* at [60], sub-paragraph (11), that separate invoicing and pricing only supports the "independent supplies" view "*if it reflects the interests of the parties*" [our emphasis]. We do not consider that separate invoicing and pricing can be said to reflect the interests of SPNH; for the reasons already considered above, we find that the arrangements were made for the benefit of SPCL, and in certain respects they were to the detriment of the interests of SPNH.

138. We have made findings concerning the obtaining and following of VAT advice. The use of the word "contrivance" in judgments of the CJEU might appear to suggest that if parties enter into an arrangement which could be seen as contrived, this may have some effect on the conclusion whether the supplies in question are or are not independent. As an example, in *Aktiebolaget NN* at [25] (cited at paragraph 86 above) the CJEU referred to "undue contrivance". In the same way, the CJEU used that

expression in *Don Bosco* at [39]. However, it appears to us that in making these references, the CJEU was seeking to stress that treating the particular supplies under examination in those cases as separate and independent would amount to an artificial split of what it considered to be a single economic transaction. We do not read these comments as indicating that any contrivance on the part of those involved in the transaction or transactions concerned might affect the position; the requirement is to examine the essential features or characteristic elements of the transaction (*Middle Temple* at [60], principle (2)).

139. Thus we do not consider that the deliberate decision to enter into the arrangements in question in this appeal, pursuant to the VAT advice which had been obtained, affects the conclusions to be derived from the evidence on the "single or multiple supplies" issue.

140. However, that decision is relevant to the analysis of the arrangements from the "economic reality" point of view; their commercial effect must be considered in the context of the underlying desire to achieve a particular VAT result.

141. Mr Moll argued that it would not be correct to arrive at a decision which treated the supply of a series of items which were normally taxable as, instead, an exempt supply. We disagree; in *Middle Temple* at [60], principle (12), the Upper Tribunal made clear that as a result of treatment as a single supply, the constituent elements of that supply may be treated differently from the way in which they would have been regarded if they had been the subject of individual separate supplies.

142. In response to the first question set out at paragraph 116 above, and having applied all the principles set out in *Middle Temple* at [60], we find that:

(1) The supplies under the lease dated 1 April 2006 and the Facilities Agreement of the same date constitute a single exempt supply for VAT purposes;

(2) The supplies under the lease dated 1 April 2006 and the Facilities Agreement dated 1 June 2008 of utilities, kitchen equipment usage and furniture and equipment usage constitute a single exempt supply for VAT purposes;

(3) The supplies under the renewed lease agreement dated 1 April 2009 and, respectively, the Facilities Agreement dated 1 June 2008 and the subsequent replacement Facilities Agreement dated 1 June 2010 of utilities, kitchen equipment usage and furniture and equipment usage constitute a single exempt supply for VAT purposes.

143. For completeness, we deal with a point raised by Eacotts in correspondence. They argued that the approach being taken by HMRC appeared contrary to what was stated in paragraph 11.7.5 of HMRC's Notice 742:

> "Fixtures and fittings are regarded as part of the overall supply of the accommodation and any charges for them are normally included in the rent. However if you provide fixtures and fittings under a separate agreement your supply will normally be standard-rated."

As illustrated by our above findings, the mere use of a separate agreement is not sufficient to result in the provision of items under such an agreement becoming a separate supply. Whether it does amount to a separate standard-rated supply will depend on the facts and circumstances of the particular case. We find that paragraph 11.7.5 has no relevance to the supplies made by SPCL.

The implementation of the arrangements

144. Our above findings determine the principal question in this appeal. However, we think it appropriate to allow for the possibility that those findings might not be upheld. We therefore turn to the second question set out at paragraph 116 above.

145. Mr Thomas submitted that the contractual separation of the Facilities Agreements from the lease was ineffective. Before considering the factual position, we should comment that the formal contractual position is not necessarily determinative of the VAT analysis. This is clear from the comment of Laws J in *Reed Personnel Services* [1995] STC 588 at p 591 that the true construction of a contractual document may not always answer the question as to the nature of the VAT supply in the case being considered. This comment is consistent with the views of the CJEU in such cases as *MacDonald Resorts*, *Maierhofer* at [39] (see paragraph 49 above), and *Part Service*; in all these cases, the CJEU considered it appropriate to look beyond the terms of the relevant contracts to arrive at the true analysis of the activities concerned.

146. Clause 1.18 of the lease is as follows:

> "**Interpretation of 'this Lease'**
>
> Unless expressly stated to the contrary, the expression 'this Lease' includes any document supplemental to or collateral with this document or entered into in accordance with this document."

147. Clause 3.3 of the lease states:

> "**3.3 Cost of services consumed**
>
> The Tenant and the Landlord may enter into a separate facilities agreement by mutual negotiation. The Tenant must pay to the suppliers, and indemnify the Landlord against, all charges for any services consumed or used at or in relation to the Premises not covered by a separate facilities agreement, including meter rents and standing charges, and must comply with the lawful requirements and regulations of their respective suppliers."

148. In his written response, Mr Moll stated that it had been the intention of SPCL and SPNH that anything included in the Facilities Agreement should be excluded from the lease. When asked in cross-examination whether there was anything in the Facilities Agreement outside the lease, Mr Gamiet's evidence was that he had inserted a clause in the lease to exclude the matters covered by the Facilities Agreement.

149. We interpret Mr Gamiet's answer as meaning that he had instructed the solicitor drawing up the lease to include such a clause; the drafting of Clause 3.3 appears to us

to be in the formal language which would be expected to be included in a document such as a lease drawn up on legal advice. In his written response, Mr Moll reported Mr Gamiet to have said that he had made the amendment to clause 3.3 (which he had amended, not added) so that anything in the Facilities Agreement would be excluded from the lease. The original drafts of the two agreements had made no mention of each other. The amendment to the clause had been made so that if there was any overlap between the two agreements, the Facilities Agreement would take precedence by excluding those items from the lease. Mr Moll also commented that the lease referred to "the Landlord" and "the Tenant", while the Facilities Agreement made no mention of either a Landlord or Tenant.

150. We do not find the latter comment persuasive; the parties to the Facilities Agreements are defined by reference to their initials, in a manner conventionally used in commercial agreements. Whatever the intention behind the drafting, if it is sufficiently clear on its face to be interpreted without resort to surrounding evidence, it falls to be construed according to the words actually used. We find that the Facilities Agreements, despite being described as separate, fall within the definition of 'this Lease' in clause 1.18 of the lease. We accept Mr Thomas's submissions that there is no contractual separation of the services as between the two, and that there is nothing in any of the Facilities Agreements to suggest that they were not entered into in accordance with clause 3.3 of the lease.

151. Mr Thomas also referred to the description of the facilities. Clause 1.29.1 of the lease provides a definition of 'the Premises', using the address of the Iver property. Clause 1.29.2 is as follows:

> "**1.29.2 Interpretation of 'the Premises'**
>
> The expression 'the Premises' includes—
>
> 1.29.1 all buildings, erections, structures, fixtures, fittings and appurtenances on the Premises from time to time,
>
> 1.29.2 all additions, alterations and improvements carried out during the Term, and
>
> 1.29.3 the Conduits,
>
> but excludes the air space above and any fixtures installed by the Tenant or any predecessors in title that can be removed from the Premises without defacing the Premises. Unless the contrary is expressly stated, 'the Premises' includes any part or parts of the Premises."

152. In his response, Mr Moll argued that the reference to "any fixtures installed by the Tenant" could be regarded as extending to all group companies, pursuant to clause 3.9.14 of the lease. We do not accept this argument; clause 3.9.14 deals only with sharing of the occupation of the Premises (in whole or in part) with a group company. This does not have the effect of extending the definition of 'the Tenant' under the lease. Mr Moll also argued that HMRC had been inconsistent in the approach which they had taken in relation to the question of fixtures. We do not think it appropriate to enquire into the latter issue; the question before us is the VAT analysis based on the

facts as we find them. Mr Moll further argued that, regardless of the wording of clause 1.29.2, it had always been SPCL's case that anything included in the Facilities agreement was excluded from the lease.

153. He commented that some of HMRC's arguments required the Tribunal to ignore the contractual arrangements, while others required it to ignore economic reality and apply extreme interpretations of the contractual arrangements. Our response to that comment is that we start by looking at the contractual arrangements actually made, but that we also have to have regard to economic reality; the interpretation to be given to the terms of the arrangements is a matter for us, including our decision whether any interpretation might be regarded as extreme.

154. Our view on the question of SPCL's "case" or intention is the same in this context as our view on clause 3.3 of the lease. We accept Mr Thomas's submissions that no part of the premises was excluded from the ambit of the lease, and that (in particular) there is no mention of the kitchen or kitchen equipment being separate from 'the Premises'. Thus the lease includes fixtures and fittings as defined, as well as the conduits as defined in clause 1.1:

> " 'The Conduits' means the pipes, sewers, drains, mains, ducts, conduits, gutters, watercourses, wires, cables, laser optical fibres, data or impulse transmission, communication of reception systems, channels, flues and all other conducting media—including any fixings, louvres, cowls, covers and any other ancillary apparatus—that are in, on, over or under the Premises."

155. Mr Thomas argued that, despite the 2008 Facilities Agreement defining as services supplied from SPCL to SPNH the telephone services for residents, satellite TV for residents and internet services for residents, SPCL appeared to contend that these services had not been supplied to SPNH. He submitted that this showed the artificial nature of the arrangements and the absence of economic reality. Mr Moll's response was to rely on the intentions of SPCL and SPNH to exclude from the lease all matters contained in the Facilities Agreements.

156. In the light of our earlier finding that the 'Conduits' were included in the demise under the lease, there is an obstacle to any argument that SPCL was providing such services to any party, whether this was SPNH or the residents. By entering into the lease as drafted, SPCL had parted with its rights to use the means of transmitting these services to the intended recipients. In the 2008 Facilities Agreement (and correspondingly in the 2010 Facilities Agreement), SPCL entered into commitments to provide telephone services for SPNH, and telephone, satellite TV and internet services for residents. (We leave aside for the present the commitments set out in these agreements relating to gas, electricity and water, and the commitments in respect of other items not requiring the use of the 'Conduits'.) SPCL could only fulfil its obligations to SPNH by infringing or compromising SPNH's rights under the lease in respect of the 'Conduits'. (We are not satisfied that this difficulty could have been resolved by relying on the "shared occupation" provision at clause 3.9.14 of the lease.) We find that this demonstrates both a degree of artificiality in the arrangements, and a lack of economic reality, as such an arrangement would be

unlikely where the parties were acting independently at arm's length; SPCL and SPNH were clearly not acting on that basis.

157. Apart from the question of the use of the 'Conduits', there is also artificiality in an arrangement under which one party (SPCL) puts itself under an obligation to another party (SPNH) to provide services to third parties, namely the residents; the contractual standing of SPNH in the event of complaints by residents about problems with the services is unclear, particularly as the documents in evidence setting out details of these services for residents are headed "Trustworth". We accept that the "Terms" at the foot of the page of each of these documents refer to SPCL, but apart from the reference to equipment owned by SPCL, there is no explanation of SPCL's role.

158. Turning to the 2006 Facilities Agreement, the services to be provided requiring use of the 'Conduits' were gas and electricity. As we have already found, there was no mention of water in Schedule 1 to this agreement. We make the same findings in relation to the use of the 'Conduits' as those above in respect of the 2008 and 2010 Facilities Agreements. The other service, "kitchen", does not involve the use of the Conduits, but the kitchen is part of the premises subject to the lease, as are any kitchen items amounting to fixtures and fittings falling within the definition of 'the Premises' in clause 1.29.2 of the lease. If the intention was to refer to the use of kitchen equipment, whether or not forming part of 'the Premises', this is not clear from the 2006 Facilities Agreement.

159. The price of what was referred to in Schedule 2 of this agreement as "Kitchen Usage" was £500 per quarter, excluding VAT. The price of gas and electricity was calculated by reference to a formula, again on a quarterly basis, exclusive of VAT. Under Part II of Schedule 2, SPNH was required to make payment of "The Price" (ie the combination of both these charges) on a quarterly basis. At the meeting with HMRC in February 2007, Mr Gamiet stated that the charge for the kitchen was nominal, and that the charge for the new kitchen would be based on the total cost of the new kitchen over its life. When the 2008 Facilities Agreement was entered into following substantial completion of the refurbishment project, the price of "Kitchen Equipment Usage" remained unchanged at £500 per quarter. The 2010 Facilities Agreement increased the price slightly to £518 per quarter; we do not regard this change as significant.

160. Although the payments for facilities were required to be made quarterly, this did not happen. In his letter to Mr Taylor of HMRC dated 28 April 2008, Mr Gamiet stated:

> "With regards [*sic*] to receipts by SPCL from [SPNH] for the kitchen charge and utilities these have been paid as bulk payments on account rather than payment of individual invoices. I draw your attention to various payments made, for example £16,000 on 12/01/2007."

161. From the bank statements included in the evidence, we are satisfied that a payment of this amount, described as "EBP Sunnyside Nur BCA", was made on this date. There is no surrounding evidence to verify the reason for this payment, and thus

we are unable to make a specific finding that this corroborates Mr Gamiet's statement. We accept that this may have been the reason for the payment, but the absence of any formal paperwork recording the transactions between SPCL and SPNH prevents us from arriving at a firm view. We note that a similar transfer, of £5,000, was made by SPNH to SPCL on 15 December 2006, and one of £9,000 was made by SPNH on 24 July 2007. A further transfer of £8,000 was made on 27 September 2007, and one of £7,000 on 22 October 2007. On 13 November 2007, the amount transferred was £20,000, and on 13 December 2007, £10,000. On 25 March 2008, SPNH transferred £10,000 to SPCL. The two later transfers by SPNH to SPCL shown in the statements included in the evidence appear to relate to Volker beds, being a refund of £19,017.38 and a grant of £8,000; it is not clear to us why SPNH made these transfers, if the intention was (as we would assume it to be) for SPCL to bear the cost of such items and provide them to SPNH pursuant to the 2008 Facilities Agreement.

162. Although the intention was that the costs of electricity and gas should be dealt with through the respective Facilities Agreements, the relevant utility company continued to charge SPNH until January 2007 in respect of electricity. SPCL's bank statement shows its direct debit payment to Southern Electric on 29 January 2007 as its "Initial Payment". In respect of gas, Mr Thomas requested in HMRC's proposed findings of fact that we should also find that the relevant utility company continued to charge SPNH until February 2008. From the bank statements in evidence, we are unable to verify which utility company provided gas, or when that company began to charge SPCL. The bank statements for 28 December 2007 to 26 February 2008 were not included in the evidence; there is a gap, and we have pages covering 27 February to 25 March 2008. Although Mr Gamiet referred in evidence and in correspondence to Powergen or Eon being the supplier of gas, there is no reference to either of those companies in the copy bank statements available to us.

163. Mr Gamiet told HMRC at the February 2007 meeting that the gas and electricity suppliers were billing SPNH, that SPNH was paying these bills and that he had written to the suppliers to ask them to bill SPCL. In his letter to Ms Powell of HMRC dated 23 February 2008, just over a year later, he stated that SPCL had informed suppliers of the change in arrangements. He had checked, and established that some suppliers had made the changes, and some had not. He continued:

> "We are in the process of telling those suppliers that have not made the changes to the invoices to do so with effect from the changes in legal agreements."

164. We find that there is no documentary evidence of Mr Gamiet writing to the utility companies to change the details, and that he had not considered doing so until HRMC raised questions enquiring into the case. In cross-examination he said that he believed that the suppliers had been contacted by phone; he would have asked the administrator to deal with this. In his letter to Ms Powell dated 24 May 2007, he had stated that he could not remember the exact date when the letters to suppliers had been sent, but he believed it had been around the beginning of September 2006. In view of the inconsistencies between his statements in February and May 2007 and his oral evidence, we do not accept that any letters were sent. As the utility companies eventually began to address their accounts to SPCL (see below), we accept that at

some stage there must have been some form of request to them to do so, but there is no evidence to demonstrate what reasons were given for such request, or to show who made it.

165. Although Mr Gamiet stated in evidence that inter-company charges had been raised as between SPNH and SPCL to regularise the position, there is no documentary evidence of this. Mr Gamiet stated that he had not been asked for evidence of such charges, which would be shown in the Sage accounts. Whatever the position may be in respect of the Sage accounts, we have examined the bank statements of SPCL from 27 April 2006 onwards available to us, and can find no evidence of any payments by SPCL to SPNH.

166. The utility companies agreed to refund VAT incorrectly charged. In August 2010, Eon sent SPCL (referred to as "Sunnyside Property Ltd") an "amended gas statement" showing a substantial credit balance. The adjustments related to the period from 18 August 2006. On 19 August 2010, Mr Gamiet had signed a certificate in the name of SPCL in respect of premises qualifying for the reduced rate of VAT. The first invoice from Eon to SPCL had been dated 21 March 2008, the previous invoice dated 21 January 2008 having been addressed to SPNH. In October 2010 Southern Electric issued to SPCL an account refunding the difference between VAT charged at the standard rate and VAT at the reduced rate; this covered the period from 6 January 2006 to 28 March 2008. The last invoice addressed to SPNH had been dated 3 January 2008. As SPCL and SPNH did not enter into the 2006 Facilities Agreement until 1 April 2006, it was inappropriate for that part of the refund which related to the period from 6 January to 31 March 2006 to be made to SPCL.

167. Mr Thomas argued that the invoices did not indicate agreement on the part of these utility companies that their energy was supplied to SPCL. We regard the position as neutral; by 2010, the companies were dealing as requested with SPCL, and if they received a request from SPCL for refund of excess VAT charged, it appears to us unlikely that they would raise any query as to the identity of the company receiving the refund.

168. In relation to water, SPNH paid water charges to Three Valleys Water until 4 April 2008. After that date, Three Valleys Water billed SPCL, even though water was not covered by the 2006 Facilities Agreement, which continued until 31 May 2008.

169. In the absence of evidence of reimbursement of SPNH for the utility payments that it had made after the commencement of the Facilities Agreements, we find that SPCL could not have been in a position to supply the services to SPNH while the utility providers were continuing to do so.

170. Each of the Facilities Agreements contained a clause providing for annual review of the operation of the agreement, and annual review of the price of the facilities. SSPCL and SPNH did not carry out any such reviews. Mr Gamiet explained in cross-examination that he was the only family member involved, and that he would not write a report to himself. He commented that he did have some records of the calculation of the utilities charge.

171. We find that this demonstrates a lack of commerciality in the arrangements. If SPCL and SPNH had been dealing with each other at arm's length, each of them would have been concerned to ensure that the prices being charged were and continued to be at a sensible commercial level.

172. The price of the utilities was calculated by reference to average percentage occupancy per quarter of the nursing home multiplied by a quarterly charge figure. In the 2006 Facilities Agreement this was £5,000, in the 2008 Agreement £7,660, and in the 2010 Agreement £6,810. (In the latter two agreements, water was included in the utilities charge.) The reason which Mr Gamiet gave for this formula was to protect the position of SPNH's nursing home business from volatility in the market. In relation to a transaction between two parties such as SPCL and SPNH, protecting one party (possibly to the disadvantage of the other) does not appear to be a basis for a commercial transaction such as would be agreed as a result of negotiation between independent parties. Before entering into the Facilities Agreement, SPNH had been used to variability in the costs of utilities. Even afterwards, SPNH appears to have been subject to such variability in costs, as it continued to pay for certain utilities and (as we have found above) there is no evidence that it received any reimbursement.

173. The 2006 Facilities Agreement provided SPNH with "kitchen usage", and the later Facilities Agreements provided for kitchen equipment usage and furniture and equipment usage. None of the agreements made any provision for repair, maintenance or replacement, as might be expected in a commercially negotiated agreement. The level of the charge did not vary by reference to the facilities actually provided. While the kitchen was being refurbished, a temporary kitchen was provided; the charge was not adjusted, nor was the charge increased when the newly fitted kitchen was made available to SPNH. According to a proposal and specification produced in early 2007, a significant quantity of the kitchen equipment was described as "existing", and so had previously been made available to SPNH pursuant to its informal lease. As such, SPNH's payments under that informal lease covered the cost of using those items; until 1 April 2006, there had been no separate facilities charge.

174. There was no specific evidence concerning the question whether items in the kitchen were or were not "fixtures, fittings or appurtenances" within the definition of 'the Premises' in clause 1.29.2 of the lease. We are therefore unable to make any findings as to the nature of particular items. Although in presenting SPCL's case Mr Moll drew a distinction between fixed and freestanding items, we do not consider this to be an appropriate distinction. It does appear to us that a number of items are likely to be fixtures, for example sink, taps, sink with taps, wall cupboards and worktops.

175. We find the absence of identification of the items to be provided pursuant to the Facilities Agreements is a further demonstration of the lack of commerciality in the arrangements, and another respect in which the arrangements were not properly implemented.

176. The 2008 Facilities Agreement added furniture and equipment usage to the services provided. Before 1 June 2008, SPNH had been continuing to carry on its business as a nursing home. There is no evidence to show whether any nursing home

equipment had been acquired (whether from SPNH or from elsewhere) by SPCL when it acquired the Iver property in 2003 pursuant to the reorganisation. If SPCL owned the equipment before entering into the 2008 Facilities Agreement, SPNH would either have been using it in its capacity as a tenant, or (for items not forming part of 'the Premises') on the basis of some kind of informal licence. Mr Gamiet confirmed to Ms Powell in an email dated 17 January 2011 that:

> "The equipment and furniture under the equipment lease were not part of the building contract. They were purchased by SPCL and supplied to [SPNH] in SPCL's role as a supplier and central purchaser that SPCL supplies food & provisions to [SPNH]. All of the equipment is removable. Some of the equipment was supplied prior to June 2008 i.e. prior to the updated June 2008 facilities agreement."

177. Mr Gamiet stated in evidence that before 2006, the furniture would have been bought by SPNH. He did not explain the position in respect of the period from 2006 to 31 May 2008.

178. The document headed "Implementation of VAT Planning" produced by Mr Moll on 10 March 2006 contained an item relating to furniture stating: "Appoint Solicitor to draw up leasing agreement for new furniture to be supplied once new facilities are complete." On the basis of the evidence, we find that this advice was not implemented. Leaving aside the document referred to in the following paragraph, no list of the equipment was produced, nor was there any document to show what equipment SPNH was entitled to use pursuant to Schedule 1 to the 2008 Facilities Agreement. The price of furniture and equipment usage was set at the very specific figure of £15,125.48, payable annually in arrears.

179. In the bundle of documentary evidence, there was a page entitled "Schedule of equipment leased from SPCL to [SPNH] as of 31 May 2008". Mr Gamiet confirmed in his oral evidence that this should have referred to the starting date of 1 June 2008. The schedule lists a series of items, all described as "new", including a total of 40 Volker beds. Although one of the headings to the spreadsheet includes the word "existing", there are no items falling within this description. The document shows the current value of each category of the items listed, together with the annual facilities charge. The charge for each category was based on a division of the current value by the expected useful life of the items in question, either seven years or ten years.

180. The difficulty which we have with this document is to establish the date at which it was produced. Apart from the total facilities charge corresponding to the figure of £15,125.48 appearing in the 2008 Facilities Agreement, there is nothing to show that this document was produced before or at the time when SPCL and SPNH entered into that Agreement. Even if this document was available from 31 May 2008 onwards, the information shown in it was not carried across into a schedule to any document recording what SPCL was providing to SPNH in return for that part of the facilities charge relating to furniture and equipment usage. In the absence of further evidence, the only reference being Mr Gamiet's acknowledgment that it should have referred to 1 June 2008, we are unable to make any finding as to the date on which this document was produced.

181. Mr Gamiet referred in oral evidence to some items having been bought by SPNH during the period of construction. He also referred to the Weatheralls valuation report, which had included all the assets including plant, machinery, fixtures, fittings, furniture, and moveable items. In response to Mr Thomas's question whether equipment had been transferred as a matter of legal title, he accepted that there had been no schedule listing fixtures and fittings. He thought that it had been SPCL which had owned the beds and baths before the transfer, but said that he would have to check this. He accepted that the ordering process had not been documented.

182. We find that there was no clear identification of the items to be covered by the "furniture and equipment usage" element of the 2008 Facilities Agreement; there may well have been other items apart from those described as "new" in the spreadsheet showing the calculation of the charge. Further, there was no provision for repair, maintenance and replacement. Nor was there any provision for SPNH to choose the equipment itself. Mr Gamiet accepted in evidence that SPNH had no say in the choice of equipment, but commented that ultimately the decision came down to him. We further find that the basis on which the charge was calculated did not provide any mark-up for SPCL; it simply returned the cost of each item over its assumed useful life, without providing any profit element.

183. In relation to the price of these items, the same provision described above for annual review applied; as we have found, no such reviews were carried out in practice. Changes to the equipment provided were made on an ad hoc basis from time to time depending on need, and there was no provision in the Agreement for the charge to be varied to take account of changes. As an example (in relation to the 2010 Facilities Agreement), a television cabinet was shown by a calculation schedule as at 30 November 2011 to be leased to LNH; it was described as "existing – Barons prev [ie previously] SNH" [ie SNHL]. There was no evidence of any adjustment having been made to the furniture and equipment charge payable by SPNH as a result of this item having been reallocated to LNH. We find that the relevant details in clause 4 of the 2010 Facilities Agreement were not completed, so that there was no formal basis for amending the price for any of the services during the life of this agreement. Despite this, in relation to kitchen equipment usage, the charge was amended from £518 per quarter to £416 per quarter from 31 May 2012. Mr Gamiet stated at the end of his oral evidence that the furniture and equipment charge changed in the year and was not fixed; this demonstrates that the terms of the Facilities Agreements were not always observed in practice.

184. In general, in relation to the Facilities Agreements, we find that they do not set out the full nature of the agreements between SPCL and SPNH. In practice, Mr Gamiet was the only person acting for both of these companies in relation to these agreements. As a result, the dealings between SPCL and SPNH were not conducted on the basis of a commercial arm's length relationship. Mr Gamiet's primary motivation was to carry on the nursing home business; as a result, he did not always observe the terms of the agreements when acting on behalf of either of the companies. In practice, SPNH did not have any choice as to the supplier of the services specified in the Facilities Agreements, but was not restricted in relation to obtaining other services from third parties. If SPNH had chosen to obtain from elsewhere the services

to be provided under the 2006 Facilities Agreement, this would have gone against the advice received from Eacotts and Mr Moll and so would have rendered pointless the exercise of SPCL and SPNH entering into that agreement.

185. In the same way, if SPNH had chosen to hire equipment from elsewhere, this would have prejudiced the interests of SPCL in respect of the assets which SPCL had acquired. SPNH had to accept the changes in the arrangements for the supply of utilities, this being in SPCL's interests. SPNH had no realistic option not to take the whole of the kitchen supplied by SPCL, as the work on the kitchen had been part of the contract for the refurbishment project from an early stage. SPNH had never sought to have any of the supplies referred to under the agreements to be supplied by any other party. As a policy decision had been taken that SPCL should be the asset-owning company in relation to the nursing home business, any decision by SPNH to acquire relevant assets itself would have been directly contrary to that policy. All the supplies concerned were essential to SPNH's activities as a provider of nursing home services.

186. The other issue which we need to consider in the context of implementation is the rent-free period. We emphasise that there was no reference to a rent-free period in the letters from Eacotts to Mr Gamiet setting out the VAT advice. There is no evidence that Mr Gamiet was given any advice relating to the decision to have a rent-free period.

187. Mr Gamiet made various references in correspondence with HMRC before November 2006 to SPCL making exempt supplies of rent. However, he gave no indication that rent was not being charged from 1 April 2006. At the meeting with HMRC on 1 February 2007, he indicated that no rent would be charged for the period to 30 September 2007. In his witness statement, he said that the decision was to suspend the payment of the rent during the period while building work was being undertaken at the nursing home, and that payment of rent had resumed (at the increased rate of £75,000 per annum) from 1 June 2008. We find that the rent free period was as Mr Gamiet stated; the first invoice for rent at the increased rate was dated 1 June 2008, the amount charged being £18,750.

188. The result of this rent-free period was that SPCL made no exempt supplies during that period. Clause 5.5 of the lease dated 1 April 2006 provides for suspension of the rent in the event that development by the landlord (SPCL) results in "substantial disruption to the Tenant's use of the Premises". In that situation, clause 5.5.2 provides that the rent, or a fair proportion of it "according to the nature and the extent of the damage sustained", is to cease to be payable "until the Premises, or the affected part, have been rebuilt or reinstated so as to render the Premises, or the affected part, fit for occupation and use". The proportion of the rent suspended and the period of the suspension are to be determined by 'the Surveyor'. The definition of 'the Surveyor' includes an employee of the landlord.

189. As Mr Gamiet is a director of SPCL, he falls within the latter definition. However, clause 5.5.2 of the lease requires 'the Surveyor' to make that determination "acting as an expert and not as an arbitrator". We find that Mr Gamiet was not in a

position to act as an expert. As he took the decision to suspend the rent, there was no external evidence to justify either the decision to suspend the rent or the duration of period of that suspension. Further, the decision was to suspend the rent altogether, rather than in proportion to the part or parts of 'the Premises' in respect of which there was substantial disruption to SPNH's use of those premises.

190. Despite the complete suspension of the rent, there was no adjustment to the amount charged to SPNH under the Facilities Agreement. The nursing home continued to operate throughout the period of the refurbishment, and occupancy levels during that period were in excess of 80 per cent and for some time in excess of 90 per cent. No rebate was given to the residents; as a result, SPNH continued to derive substantial income from charges to residents while having the benefit of reduced costs as a result of the suspension of the rent. We find that there was no commercial justification for this distorted arrangement, which affected only the two group companies involved, while providing no form of compensation to the residents for the disruption caused by the refurbishment work. The period of suspension continued beyond the completion of the building work in March 2008; Mr Gamiet's explanation was that he picked a date which was reasonable, being the start of the companies' financial year, and allowing time to build up occupancy.

191. We find that the suspension of rent was artificial and lacking in commerciality, both because it was in respect of the whole of the rent and because it extended beyond the period of the refurbishment work; any "snagging" work would not have resulted in substantial disruption.

192. Mr Moll referred us to various entries in the annual accounts of SPCL and SPNH for relevant years. Mr Thomas invited us to make various findings in respect of entries in those accounts. We do not derive any assistance from these accounts, which at best amount only to secondary evidence as to the transactions between these companies, and therefore make no findings by reference to these accounts.

193. Our conclusions on implementation are that in a wide range of respects, the steps actually taken by SPCL and SPNH were not in accordance with the terms of the documentation entered into between them, and that the dealings between them were, in a number of respects, lacking in commerciality and so did not reflect economic reality. We are not satisfied that the agreements were properly implemented in such a way as to achieve the intended results for VAT purposes. Thus on the basis of our findings, even if our conclusions on the single or multiple supplies issue are not upheld, we do not accept that SPCL has made separate supplies of, respectively, exempt rent under the lease and taxable services pursuant to the Facilities Agreements.

Attribution of Input Tax/Deductibility of input tax on the costs of refurbishment

194. Mr Moll acknowledged that there was a direct and immediate link between the redevelopment costs and the exempt supply of rent; the rent had been increased substantially following the redevelopment. However, he submitted that there was a direct and immediate link with taxable supplies made by SPCL. This was the case in

relation to the supply of telephone, internet and satellite services to SPNH's residents. There was a further direct and immediate link with the supply of telephones and kitchen equipment to SPNH.

195. In his final submissions, Mr Moll argued that SPCL had correctly deducted its input tax. SPCL had attributed input tax to its taxable supplies and deducted this in full; it had attributed input tax to exempt supplies and not deducted that input tax, and it had apportioned input tax that was attributable to both taxable and exempt supplies using the standard partial exemption method.

196. Mr Thomas confirmed in relation to supplies of food, medical supplies and consumables outside the terms of the Facilities Agreements that HMRC had always accepted that these were taxable supplies.

197. He referred to the arrangement for central purchasing by SPCL with a 5 per cent mark-up, and contended that this was artificial; the operating companies (SPNH and LNH) could simply do this with no mark-up. SPCL did not use these goods, but the nursing homes did. HMRC had seen no evidence to suggest that the operation of the central purchasing agreement resulted in any discount actually being achieved. In the absence of evidence to demonstrate commerciality, it appeared that the 5 per cent mark-up was another way of attempting to increase SPCL's taxable turnover by artificial means.

198. He submitted that the costs of the refurbishment were directly attributable to the making of the exempt supply of the lease. If the Tribunal decided that the supplies made under the lease and the respective Facilities Agreements constituted a single exempt supply for VAT purposes, the costs of the refurbishment were directly attributable to the making of that single exempt supply of the lease.

199. He further argued that the input tax on the refurbishment costs was not otherwise deductible, for a number of reasons. In relation to any taxable supplies by SPCL of telephone, television and internet services, the costs of the refurbishment work had no direct and immediate link with such taxable supplies, because of the chain breaking effect of the exempt lease. The supply of the lease was a conventional chain-breaking exempt supply which prevented input tax directly attributable to it from being directly and immediately linked to "downstream" taxable supplies. Such a conclusion was entirely in accordance with the relevant case law. He referred to *BLP*, *Midland Bank* and *Abbey National*. Whatever intervening transactions might be assumed to have taken place between SPNH and SPCL to put SPCL into a position to make such supplies, those transactions could have no effect on SPCL's ability to deduct input tax on the refurbishment costs.

200. In relation to any taxable supplies by SPCL of food, medical supplies and consumables, there was no direct and immediate link between those supplies and the costs of refurbishing and enlarging the building; he referred to *Dial-a-Phone Ltd* and *Southern Primary Housing Trust*. The building had been altered for the purpose of improving the nursing home facilities and did not represent a direct link to the supply of consumables or food to the companies operating Sunnyside or any other nursing

home. The only use of the building relied on by SPCL was a use by it under the terms of the lease for shared use. For that reason, this use suffered from the same difficulty as the supplies of telephone, television and internet services, namely that the premises had been demised in the lease. Further, there was no evidence that the costs of the refurbishment were in any way incorporated into the price of the food, medical supplies and consumables supplied pursuant to the arrangements between SPCL and the nursing home companies.

201. Mr Thomas also made submissions on the alternative hypothesis that the respective supplies were held to be separate supplies:

(1) Even if the supplies of furniture and equipment were separate supplies, there was no direct and immediate link between those supplies and the costs of refurbishing the building. The furniture and equipment were not supplied as part of the building contract. The only use of the building relied on by SPCL was a use by it under the terms of the lease for shared use.

(2) Even if the supplies of utilities were separate supplies, there was no direct and immediate link between the costs of the refurbishment and the supply of the utilities; the position was exactly the same as it would have been if those utilities had been supplied by an outside contractor. The fact that the utilities supplied passed through wires and pipes installed in the building did not mean that the construction costs, including the fitting of the wires or pipes, were a cost component of the supply utilities, whether that supply was made by SPCL or an independent utility company. Further, the lease had the same chain breaking effect so as to prevent the refurbishment costs from being a cost component of the supply of the utilities, as the premises had been demised to SPNH under the terms of the lease.

(3) Even if the supplies of the kitchen were to be characterised as SPCL contended and were found to be separate supplies, those elements of the building contract which related to the particular equipment concerned were separate supplies of equipment, and the remainder of the building contract services were directly attributable to the exempt supply of the lease. There was no rational basis for saying that the elements of the building contract could be separated out as between: (a) work done on the fabric of the kitchen; (b) the mechanical and electrical services; (c) the utility services; (d) the fixtures and fittings; (e) internal decoration; (f) fixed equipment installed; and (g) freestanding equipment, in such a way as to contend on SPCL's behalf that the supply of freestanding equipment could be a separate supply *by* SPCL but could not be a separate supply *to* SPCL.

202. In relation to Mr Moll's alternative argument based on the intention to make taxable supplies, Mr Thomas commented that although the words "to be used" in the primary legislation made intention relevant in determining whether VAT incurred constituted input tax, intention was not relevant in relation to deduction in a particular period. This was clear from the words "made in the period" at the end of reg 101(d) of the VAT Regulations.

Findings on deductibility and attribution of input tax

203. As Mr Moll acknowledged, there was a direct and immediate link between the redevelopment costs and the exempt supply under the lease. The question for determination is whether any part of the input tax incurred in respect of those costs can be regarded as attributable to any taxable supplies made by SPCL.

204. We have already found that the supplies under the lease and the respective Facilities Agreements were a single exempt supply. On that basis, the only taxable supplies being made by SPCL were those of food, medical supplies and consumables outside the Facilities Agreements. Was there any direct and immediate link between those supplies and the costs of refurbishing the building? We find that there was no such link. SPCL did not need to use the building in order to make those supplies to SPNH. Even if we were not correct in arriving at the latter conclusion, the only basis on which SPCL could have been using the building for such purpose would have been pursuant to clause 3.9.14 of the lease, which permits SPNH as tenant to share occupation with a group company. As the supply of the premises under the lease is an exempt supply, this "breaks the chain" as described in *Abbey National* and so would in any event prevent the input tax relating to the construction costs from being deductible.

205. To allow for the possibility that our finding that the supplies under the Facilities Agreements are part of a single composite supply of the premises might not be upheld, we deal with each of the questions raised by Mr Thomas on the hypothesis that the respective supplies might be held to be separate supplies. We accept his submissions on all of the matters raised at paragraph 201 above. Further, in relation to the supplies of telephone, television and internet services, these could only be provided by SPCL on the basis of an arrangement with SPNH by reference to the latter's rights to the use of the 'Conduits' under the lease; as a result, SPCL's exempt supply under the lease had the "chain-breaking" effect referred to above, and therefore the input tax on the refurbishment costs cannot be a component of the taxable supplies of those services.

206. We find that none of the input tax incurred in respect of the construction costs is deductible in computing SPCL's VAT liability in respect of its taxable supplies.

207. As a consequence, Mr Moll's alternative argument based on intended taxable supplies falls away. However, for the reasons given by Mr Thomas, we would not have accepted Mr Moll's argument in the circumstances of the present case. We prefer not to make any more general statement on the issue of intended taxable supplies, as the possibility that different circumstances might lead to a different conclusion cannot be entirely ruled out.

208. In the light of these findings, we do not consider it necessary to make any findings relating to the central purchasing of goods by SPCL with a 5 per cent mark-up on its onward supplies to the nursing home companies.

Summary of conclusions

209. Our conclusions in relation to the consolidated appeal are:

(1) The supplies under the lease and the respective Facilities Agreements constitute a single composite supply;

(2) The input tax incurred by SPCL on the construction costs has no direct and immediate link to any taxable supplies made by SPCL, and therefore is not deductible in calculating SPCL's net VAT liabilities;

(3) As a result of our findings, the assessments made to protect HMRC's position in the event of the principal appeal being determined in favour of SPCL cease to be relevant and we make no determination in respect of those assessments. The appeals numbered TC/2013/00065, TC/2013/00237 and TC/2013/00066 therefore remain open pending any further action being taken in respect of them.

210. We dismiss SPCL's consolidated appeal. Mr Thomas indicated that he proposed to leave the question of costs until the substantive issue had been determined. We direct that any application in respect of costs must be made within the period of 28 days from the date of release of this decision.

Right to apply for permission to appeal

211. This document contains full findings of fact and reasons for the decision. Any the 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.

JOHN CLARK
TRIBUNAL JUDGE

RELEASE DATE: 22 August 2013