[2018] UKFTT 0567 (TC)

TC06741

Appeal number: TC/2017/00384

VAT – disallowance of input tax credit – whether company had an interest in the land – no – whether supply could be zero-rated – no – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

HONEYGARTH LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE ANNE FAIRPO
Mr LESLIE HOWARD

Sitting in public at Leeds on 21 August 2017

Mr Julian Watson, director of the Appellant appeared in person

Ms Sinclair, presenting officer, appeared for the Respondents

DECISION

Introduction

1. This is an appeal against a decision by the Respondents ("HMRC") to:

(1) amend a VAT return to disallow input VAT of £1,770.51; and

(2) issue an assessment for £3,049.00 to reclaim a repayment of VAT.

Background

2. This appeal arises from development activity on a plot of land in the Harrogate Borough Council area. The land in question was originally owned by Mr Watson, a director and shareholder of the Appellant ("Honeygarth"), and his wife. Once outline planning permission was obtained to develop affordable housing on the land, Honeygarth was incorporated to facilitate the application for full planning permission and to undertake construction activity. Honeygarth was registered for VAT with effect from 1 December 2012.

3. Honeygarth submitted a repayment claim for £5,091.22 in its VAT return for the 08/15 period. Following a verification check by HMRC, credit for input tax of £1,770.51 was disallowed on the basis that it had been incurred on an exempt supply, being in relation to land which was not considered to meet the criteria for zero-rating. £3,320.71 of the repayment claim was repaid to Honeygarth.

4. Subsequent correspondence led to HMRC issuing an assessment for £3,049.05 of the amount previous repaid, on the basis that the input tax, and that previously disallowed, had been incurred on:

(1) invoices which were addressed to Mr and Mrs Watson, the directors and shareholders of Honeygarth, and related to a sale of land by them and not to a sale of land by Honeygarth; and

(2) personal items, items which could not be identified, and a purchase for which the relevant invoice was not a VAT invoice.

5. Honeygarth appealed both the disallowed input tax and the assessment to this Tribunal on 29 July 2016.

Appellant's case

Whether the land met the criteria for zero-rating

6. Mr Watson explained that the land, at the time of sale, had had the following works undertaken on it:

(1) it had been levelled off with a JCB digger in preparation for building works;

(2) the site had been marked out with pegs and string to set out the grids for plots and mark the plots and proposed roads in preparation for construction;

(3) trenches had been dug for foundations;

(4) the trenches had been pegged out to ensure that they were level prior to foundations being constructed;

(5) foundation quality concrete had been poured;

(6) bricks had been arranged on site to allow the local authority to approve the colour and other specifications. These had not been laid on the foundation but were set out in test panels elsewhere on the site;

(7) a site hut had been erected and connected to drains and other utilities;

7. The foundations were laid in order to prevent the planning permission from expiring; they had been approved by the local authority.

8. The site had been prepared and laid out for over two years whilst funding was sought for the development, in order that potential funders could view the site and understand the proposed construction.

9. During that time, substantial work had been undertaken in relation to the site in order to obtain easements and wayleaves from utilities companies, a local farmer and a neighbour. Environmental, archaeological, geophysical and other surveys had been obtained. All of this had entailed substantial numbers of calls, meetings, and legal and accountancy involvement.

10. Mr Watson submitted, therefore, that the criteria for zero-rating had been met as substantial work had been carried out on the site. He further submitted that this was supported by s56 of the Town and Country Planning Act 1990 (to which he had been directed by Harrogate Borough Council) which states that a development has begun when material operations begin to be carried out. "Material operations" include "the digging of a trench which is to contain the foundations, or part of the foundations, of a building".

11. Mr Watson submitted, therefore, that as the trenches had been dug, concrete poured, and substantial other work had been undertaken, the requirement for zero-rating that the building be in the course of construction was met. He submitted that HMRC's interpretation that walls had to under construction for a building to be in the course of construction was therefore incorrect and also could not be conclusive as their guidance said only that this would "usually" be the case. If there was any discrepancy between different government interpretations, he submitted that it should not create expense for an individual taxpayer.

Recipient of supplies

12. Mr Watson accepted that he and his wife had acquired the relevant land in 2004/5. They had continued to hold the land in their own names because private financiers preferred to lend on property held by individuals as they considered it

easier to enforce charges against individuals rather than against companies. In addition, the land included the accessway onto the land on which Mr and Mrs Watson's home was situated. Retaining the land in their own name ensured that they could ensure rights over that accessway until it was adopted by the local authority. Mr Watson also submitted that retention of ownership by individuals was very common due to issues which could arise during development, and the owner only releases the land at the point of sale in order to maintain control.

13. Mr Watson explained – with regard to HMRC's view that amounts incurred by Honeygarth were in relation to personal expenditure – that the relevant suppliers had dealt with him before the company was set up and so knew him as both himself, and as Honeygarth. He was acting as director of Honeygarth and it was sometimes difficult to get names changed on documents. Mr Watson submitted that it was a moot point as to where he started and where Honeygarth took over: sometimes people used his name, sometimes the company name. Whether payment were made through the company or on Mr Watson's credit card depended on who had money at the time.

14. Mr Watson accepted that there was no agreement between himself and Honeygarth as to work to be done by him on behalf of the company. He did all the work and so it would be difficult to describe, or produce a document setting out who did what, as it was all done by him.

Ownership of the land

15. Eventually, it was decided that the land should be sold to a developer in order to get the site built. Mr Watson explained that the land was sold to Honeygarth immediately before onward sale by Honeygarth to the developer to ensure that there was money in the company to pay amounts owing which had arisen over the course of time. The exchanges and completion were on the same day so that the company was the owner of the land for a split second of time.

16. Mr Watson produced an undated Declaration that recorded that Honeygarth had agreed to pay Mr and Mrs Watson an amount of money (the document mentions both £40,000 and £50,000) and they had agreed to assign their equitable interest in the land to Honeygarth. The only date on the documents is that of the witness' signature, 29 June 2015.

17. Mr Watson agreed that no documents had been provided which showed Honeygarth as the vendor of the land to the developer, and he could not recall whether Honeygarth was involved in the any documentation on the sale to the developer. He said that it was always the intention that Honeygarth would benefit from the sale. Originally, the intention was that this would be the sale of houses but the problems with obtaining funding meant that plans were changed.

HMRC evidence and submissions

18. HMRC's case was that the burden of proof is on Honeygarth to show that it is entitled to reclaim input tax. In particular, it must show that it was the recipient of the

relevant services, that the expenditure had a business purpose and that the services had a direct and immediate link with a taxable transaction.

19. HMRC argued that, in this case, the relevant supplies had not been made to Honeygarth but, instead, to Mr and Mrs Watson. Further, the supplies had no direct and immediate link with a taxable transaction as the land supply was exempt from VAT as it was not in relation to a building or a building under construction as the construction had not extended above foundation level at the time of sale. It had been confirmed during the hearing that no bricks had been laid on the foundation concrete.

20. A witness statement and oral evidence was provided by Ms Wakefield, an officer of HMRC.

Ownership of the land

21. HMRC submitted that there was no evidence that Honeygarth had sold the land to the developers: the Land Registry records showed the land as having been sold by Mr and Mrs Watson to the third party developer. Honeygarth was not recorded on the Land Registry records as having any interest in the land.

22. HMRC submitted that Mr Watson's contention that the land had been transferred to Honeygarth a "split second" before the transfer to the developer was not supported by the documentation provided.

Zero-rating the land

23. HMRC further submitted that zero-rating requires that a relevant building be completed or in the course of construction on the site and that, in this case, only the foundations had been laid. Mr Watson had confirmed in the hearing that no bricks had been laid on the foundation. HMRC submitted that the foundations alone did not amount to construction of a building.

Recipient of supplies

24. The relevant documentation provided showed the recipient of supplies to be Mr and Mrs Watson, not Honeygarth:

(1) The solicitors' invoice for "acting on your behalf in connection with the sale of [the relevant land]" was addressed to "Mr & Mrs J A Watson" with no mention of Honeygarth; and

(2) Invoices from an estate agent were addressed to Mr Watson only with no mention of Honeygarth

25. Accordingly, the VAT on the invoices should be disallowed in full as it related to costs incurred related to the land. As Honeygarth was not the owner of the land, it was not entitled to recover the input tax. The owners of the land were Mr and Mrs Watson, who were not VAT registered.

Relevant law

26. s24 Value Added Tax Act ("VATA") 1994 provides, as relevant:

> "(1) Subject to the following provisions of this section, "input tax", in relation to a taxable person, means the following tax, that is to say—
>
> (a) VAT on the supply to him of any goods or services;
>
> …
>
> being (in each case) goods or services used or to be used for the purpose of any business carried on or to be carried on by him."

27. s26 VATA 1994 provides, as relevant:

> "(1) The amount of input tax for which a taxable person is entitled to credit at the end of any period shall be so much of the input tax for the period (that is input tax on supplies, acquisitions and importations in the period) as is allowable by or under regulations as being attributable to supplies within subsection (2) below.
>
> (2) The supplies within this subsection are the following supplies made or to be made by the taxable person in the course or furtherance of his business—
>
> (a) taxable supplies …"

28. VATA 1994, Schedule 8 provides that the following (as relevant) shall be zero-rated:

> "Group 5—Construction of buildings, etc
>
> Item No 1
>
> The first grant by a person—
>
> (a) constructing a building—
>
> (i) designed as a dwelling or number of dwellings; or
>
> …
>
> of a major interest in, or in any part of, the building, dwelling or its site."

Discussion

Whether Honeygarth made a supply of the land

29. The first question to be considered in this appeal is whether the land was sold by Honeygarth: it is clear from s26 VATA 1994 that, it be credited, input tax must be attributable to taxable supplies made by the taxable person. The input tax in question in this appeal is that arising on purchases relating to the sale of the land. If Honeygarth had no interest in the land sold, it cannot have made a supply in relation to that land and so could not receive credit for any input tax incurred in relation to the sale of the land.

30. The questions as to the nature of the supply of the land and the identity of the person receiving the supplies purchased are only relevant in this matter if Honeygarth in fact made a supply of the land in the first place.

31. HMRC's evidence is that the Land Registry documentation shows no reference to Honeygarth having any interest in the land sold to the developers. Mr Watson does not dispute this but states that the land was sold to Honeygarth by himself and his wife "a split second" before the sale to the developer.

32. The undated document produced by the appellant purporting to show a transfer of the land to the appellant from Mr and Mrs Watson states as its "Operative Provisions" (in their entirety) that "Mrs and Mrs Watson agree that in consideration of the sum of £50,000 (paid to them by the Company) to assign their equitable interest in the Property to the Company with the intent that the Company henceforth shall own the whole of the equitable interest in the Property free of any interest of the Company [sic]". The only date on the document is that next to a witness' signature, which is 29 June 2015.

33. The date of the exchange of contracts on the land was not provided, nor was any copy of the contract provided, but a schedule of time spent by the solicitors which was provided records "exchange of contracts" on 28 June 2015. Mr Watson did not dispute that he and his wife were the contracting vendors on exchange of contracts (and subsequent completion) in relation to the sale of the land to the developer.

34. Although no specific submissions were made on this point and no copy of the contract was provided, we note that, in property law, the effect of an exchange of contracts in relation to land is that the purchaser acquires an equitable interest in the land at exchange.

35. The burden of proof is on Honeygarth to show, on the balance of probabilities, that it made a supply of the land before any consideration can be given to the question of whether it is entitled to a credit for input tax in relation to costs of sale of that land.

36. We find that Honeygarth has not discharged that burden of proof: the only evidence put forward to show that it had any interest in the land is an "assignment of equity" which is undated and so appears not to have been completed; the internal evidence on that document also shows that it was witnessed on 29 June 2015 and so, even if the document had been completed, could not have been completed before exchange of contracts on the land on 28 June 2015. As a contracting purchaser acquires an equitable interest in the land on exchange of contracts, Mr and Mrs Watson would not have been able to transfer an equitable interest to Honeygarth once exchange of contracts had taken place without the involvement of the purchasing developer. No evidence was put to forward to suggest that the developer was involved in the purported assignment.

37. We also note that Mr Watson's evidence is that the land was transferred to Honeygarth a "split second" before completion; the date of completion appears, from the solicitors' records, to have been 24 August 2015. Nothing on the evidence

provided supports any such transfer and, as noted above, there is no evidence that Honeygarth was involved – as it would have been required to have been – with the transfer to the developer.

38. We find that Honeygarth did not make a supply of the land and so is not entitled to any input tax credit in relation to any costs incurred in relation to that supply.

Whether the supply was capable of being zero-rated

39. As we have found that the supply of land was not made by Honeygarth, it follows that the supply of the land to the developer must have been by the persons named as the vendors: Mr and Mrs Watson. The Watsons are not registered for VAT and so the question of zero-rating the supply is not strictly relevant. However, in case our finding that Honeygarth did not make a supply of the land is incorrect, we have considered the parties submissions as to whether the land supply could have been zero-rated.

40. Honeygarth's contention was that the Town and Country Planning Act 1990 defines a development as having commenced once material works have begun, and material works include the digging of trenches for foundations, so that the fact that trenches had been dug and foundation concrete poured meant that the site should be regarded as being in the course of construction and so within the scope of zero-rating under Group 5.

41. HMRC's case was, in summary, that zero-rating under Group 5 requires that a "building" be under construction and that, until the walls have started to be constructed, it cannot be said that a building is under construction.

42. Having considered the parties' submissions in the hearing and subsequently, as agreed, in writing, we find that the zero-rating under Group 5 clearly refers to "buildings". It makes reference to a "site" as well, but we find that, on review of the legislation and submissions, the word "site" does not stand alone but, instead, is clearly linked to the requirement for a "building" so we find that that a grant of a major interest in a site which is not related to a building which is completed or in the course of construction cannot be zero-rated.

43. We note Mr Watson's submissions as to the terms of the Town and Country Planning Act 1990 but note that that legislation is defining the start point of a "development" and not the start point of construction of a "building". We consider that the term "development" is considerably broader than the term "building" and so find that the quoted provisions of the Town and Country Planning Act 1990 do not assist with determining when construction has started on a building.

44. In *Stapenhill Developments Limited v Commissioners of Customs and Excise* [1984] VATTR 1, quoted by HMRC, the Tribunal concluded that a building must be seen to be under construction on the land in order for zero-rating to be available and that foundations alone did not amount to a "building in the course of construction". Although *Stapenhill* is not binding on us, agree with that analysis and

find that the establishment of foundations on the site is preparatory to construction of a building and does not amount to the start of construction of a building.

45. Accordingly, even if Honeygarth had made a supply of the land, it did not make a supply of the land which was capable of being zero-rated. As no evidence of an option to tax the land was presented to us, we find that, if Honeygarth had made a supply of the land, it would have been an exempt supply for VAT purposes such that no entitlement to an input tax credit would have been available in relation to any purchases made in relation to that supply.

Recipient of supplies

46. The input tax disallowed is made up as follows:

(1) £1,070.51 in relation to solicitors' fees in respect of the sale of the land, relating to an invoice addressed to Mr and Mrs Watson

(2) £700.00 in relation to estate agent fees in respect of the sale of the land, relating to an invoice addressed to Mr Watson

(3) £2,944.00 in relation to solicitors' fees in relation to the land, relating to an invoice addressed to Mr and Mrs Watson

(4) £105.00 in relation to personal and unidentified costs

47. Mr Watson made no submissions with regard to the smaller disallowance of £105.00 of input tax on various invoices which were considered to relate to personal expenditure, unidentified supplies, and for one item in respect of which the supplied document was not a VAT invoice. We have concluded that, as there were no submissions with regard to these amounts, that this element of the disallowance is not in fact disputed by Honeygarth.

48. As the remaining amounts relate solely to the land which, as noted above, was not supplied by Honeygarth we do not need to consider whether Honeygarth could be entitled to an input tax credit for these costs. Indeed, the fact that the relevant invoices – issued by professionals, who will be aware of the requirement to properly identify their clients – are addressed to Mr and Mrs Watson further supports the finding that they were the owners of the land and made the relevant supply of the land.

49. Even if some of the solicitors' fees related to development costs, it is clear that the invoices were made out to Mr and Mrs Watson alone and not to Honeygarth and further made no mention of Honeygarth. There was no evidence put forward of any agreement between the Watsons and Honeygarth that would support the view that the Watsons were merely agents in relation to any supply to the company.

Decision

50. The appeal is dismissed and the amounts disallowed confirmed in full.

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

ANNE FAIRPO
TRIBUNAL JUDGE

RELEASE DATE: 1 October 2018