

## **Lime Avenue Sales and Services Limited and Benenden School Trust v Revenue and Customs Commissioners**

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**First published by DeVoil Indirect Tax Intelligence, Issue 133, June 2007.**

*Lime Avenue Sales and Services Ltd and Benenden School Trust v Revenue and Customs Commissioners (2007) VAT Decision 20140* was a Tribunal appeal concerning alleged abusive practices in the education sector. HMRC refused claims by 2 companies to deduct input tax incurred in the construction of school buildings. The Tribunal chairman was the President, Sir Stephen Oliver, who had made the reference in *Halifax* (C- 255/02) [2006] STC 919). The Tribunal dismissed the appeals. Approaching the arrangements in 2 parts, it found that the abuse principle applied. It redefined the "Initial Arrangements", practically compelling a view that the "Further Arrangements" were also abusive. The Decision was released on 3 May 2005 (Ref: v 20140).

The School, which predominantly supplied exempt education, needed to build a new study centre. In the Initial Arrangements LASS, a wholly owned subsidiary of the School contracted with builders for the construction work, its financial position "underwritten" by the School. It then purchased the development land from the School, which retained rights to repurchase it. The School Trust made loans to LASS to fund the project. The original intention was that LASS would sell the developed land to the School, with the consideration paid in annual instalments. LASS's claims to recover input tax on the builders' services were refused by HMRC.

The further arrangements were then entered into. LASS sold the land to the Trust, purportedly charging VAT. The School maintained a repurchase right. The Trust leased the Study Centre to the School for a low rental. LASS and the Trust sought to deduct their input tax.

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The Appellants' evidence was directed at showing commercial reasons of sufficient significance to displace tax avoidance as the essential aim. Advice given by the School's accountants was in evidence. Notably, they had expressed a wish "*to suggest commercial reasons*".

On the proper approach, the Tribunal cited paragraphs 74-76, 80-81 and 94-97 from ECJ in *Halifax*. *Halifax* required it to determine whether, in the context of their normal operations, the School, LASS, or the Trust would have been entitled to deduct the VAT on construction services. "Links" between the transactors had to be examined to identify any artificiality, looking behind the surface to determine the real substance and ascertain the essential aim. On finding abuse, the Tribunal had to "*identify the situation that would have prevailed in the absence of the transactions constituting the abusive practice*".

The Tribunal found no commercial reasons of substance for LASS being developer. In the context of its "normal commercial transactions" (operating the school shop) LASS's role "*was so "abnormal" as to call aloud for an explanation*". In the context of the Schools normal operations it could not have created and used the Study Centre without incurring irrecoverable input tax on construction costs. The Initial Arrangements were the implementation of a scheme designed to achieve the tax advantage of recovering otherwise irrecoverable input tax. The scheme was only possible because of the links between the transactors. Setting up LASS as the developer and propping it up financially to enable it to contract with the builders were self-evidently artificial.

The Appellant had a particular legal argument in relation to the Initial Arrangements, recorded by the Tribunal at para 33 as "*the Halifax principles only apply to actual transactions. There were none until the Further Arrangements when LASS made a relevant supply [to the Trust]*" (emphasis added). The reasoning was that, absent actual supplies by the input tax claimant, the aim could not be determined. The Tribunal rejected this argument as wrong in principle.

The Tribunal held that the abuse principle applied to the Initial Arrangements. They were contrary to the purpose of s 25-26 VATA 94 and article 17 of the Sixth Directive. Redefinition proved easy; the relevant transactions were supplies by the builders to the School.

A reasonable reader might think the matters recited by the Tribunal in relation to the Further Arrangements showed them to be contrived from first to last, designed to secure the tax advantage withheld by HMRC's refusal to pay LASS's input tax claims. The Trust purchased the Study Centre from LASS for nearly £3 million. The lease to the School was for an initial rent of £5000. The Tribunal rejected evidence that it was commercial concerns regarding LASS's insolvency that were the essential aim of the Further Arrangements. The Tribunal placed weight on lack of evidence of advice on insolvency sought by LASS's directors, but emphasised inherent implausibility, given the links and that the Trust was LASS's major creditor.

It held that the abuse principle also applied to the Further Arrangements which had the same aim as the Initial Arrangements. The consequence of the redefinition of the Initial Arrangements was that the Further Arrangements could have no commercial justification. The VAT on the construction services was irrecoverable.

The Tribunal also concluded, applying *CCE v Yarrowburgh Trust* [2002] STC 207, and noting the "microscopic" rent, that the Trust did not exploit the study centre for the purposes of obtaining property from it, finding no supply by the Trust on that basis in the alternative.

### **Comment**

The Appellant's argument on "actual supplies" can be judged out of step with a principle that seeks to protect the integrity of a legal system, here the VAT system. It seems an arbitrary restriction on objectively assessing the facts, with no real support from the principle of legal certainty. Indeed, as the Tribunal observed, it is a feature of the system that input tax deduction has to be carried out taking into account supplies yet to be made. Whilst the Tribunal identifies the purpose of article 17 as being threatened, it is notable that it sees its decision as supporting fiscal neutrality. The conformity of the VAT system to that principle was being safeguarded. The Tribunal focused on "normal commercial transactions" and emphasised the development was a "new departure" for the *particular* trader, LASS, unlike anything LASS *itself* had done before. It looked to artificiality arising from the *links* between the transactors. The Appellant had tried to draw a distinction between sales and leasing, relying on *Weald Leasing Ltd* (chairman Mr Wallace) (Ref v 20003). Reading between the lines, this Tribunal clearly saw the reasoning in that decision, which is under appeal, as suspect. It effectively ignored it. As concerns over ensuring legal certainty within the VAT system should be a constraint on the avoidance principle, continuing uncertainty arising from Halifax is unwelcome. The conclusion on the *Yarburgh* point, "*that the lease made by the Trust to the School was not an economic activity*", comes after the answer to Question 1(a) in the *Halifax* reference and shows this Tribunal not taking the satisfaction of the objective criteria of article 4(1)-(2) of the Sixth Directive for granted.

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