Neutral Citation: [2023] UKFTT 01042 (TC)

Case Number: TC09013

FIRST-TIER TRIBUNAL
TAX CHAMBER

Taylor House, London

Appeal reference: TC/2019/06645

VALUE ADDED TAX – supplies of serviced apartments – whether excluded from the exemption in Item 1, Group 1, Schedule 9, Value Added Tax Act 1994 by paragraph (d) of that Item – yes – operation of paragraph 9, Schedule 6 VATA where accommodation and ancillary services supplied by separate persons considered - whether taxpayer careless in submitting VAT returns – paragraph 1, Schedule 24, Finance Act 2007 – yes – appeals dismissed.

Heard on: 5-8 September 2023
Judgment date: 15 December 2023

Before

TRIBUNAL JUDGE MARK BALDWIN
MR DEREK ROBERTSON

Between

REALREED LIMITED

Appellant

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: Kieron Beal KC and Tom Lowenthal, of counsel, instructed by BDO LLP

For the Respondents: Isabel McArdle, of counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs

DECISION

INTRODUCTION

1. The Appellant ("Realreed") owns a property called Chelsea Cloisters in Sloane Avenue, London. The property comprises 656 self-contained apartments and some commercial units. 421 of these apartments are let on long leases, as to which no issue arises. This appeal is concerned with the VAT treatment of the letting of the remaining 235 apartments, which include studio, one-bedroom or two-bedroom self-contained Apartments ("the Apartments").

2. Realreed contends that the letting out of the Apartments is a supply of accommodation that is exempt from VAT under Item 1, Group 1, of Schedule 9 to the Value Added Tax Act 1994 ("VATA 1994"). Related services at all material times were separately provided by Chelsea Cloisters Services Limited ('CCSL'), a company under common ownership with Realreed, to the occupiers of the Apartments. Those supplies have throughout been treated as fully taxable at the standard rate for VAT purposes.

3. The Respondents ("HMRC") contend that the use of the Apartments is carved out of the exemption in Item 1 by excepted item (d), which applies to "the provision in an hotel, inn, boarding house or similar establishment of sleeping accommodation". Note 9 to Group 1 provides that "similar establishment" "includes premises in which there is provided furnished sleeping accommodation whether with or without the provision of board or facilities for the preparation of food, which are used or held out as being suitable for use by visitors or travellers".

4. Realreed challenges:

   (1) the review dated 12 September 2019 of HMRC's liability decision (that the letting out of the Apartments was subject to VAT at the standard rate) dated 14 February 2019;

   (2) consequential assessments (made using Realreed's data as to the value of the supplies), which have been amended following it coming to light that Realreed had included Apartments let on assured shorthold tenancy ("AST") terms in its calculation of VAT due, whereas HMRC accept that lettings on AST terms fall outside excepted item (d);

   (3) a related penalty which was suspended.

We refer to challenges (1) and (2) together as the "Liability Appeal" and challenge (3) as the "Penalty Appeal".

5. The total amount of VAT assessed was originally over £4.8m. The current (revised) figure is £4,572,415. The penalty was suspended, with the suspension ending on 15 January 2021. Realreed nevertheless maintains the Penalty Appeal, as it objects to HMRC's assertion that its behaviour was careless so as to engage the penalty in the first place.

6. In addition to its technical arguments on liability, Realreed submitted that the assessments should not have been raised as they departed from a legitimate expectation HMRC had engendered in RRL as a result of previous VAT inspections. We will need to return to the question of the previous VAT inspections, when considering the Penalty Appeal, but the legitimate expectation argument in relation to the assessments has been withdrawn and is not before this Tribunal. This is because, on 26 June 2023, Lavender J dismissed Realreed's application (sub nom *R (oao Realreed Ltd) v HMRC*) for judicial review of HMRC's decision to raise the assessments. The neutral citation of his judgment is [2023] EWHC 1572 (Admin).

7. We will deal with the Liability Appeal first and then move on to consider the Penalty Appeal. Before we do that, we should explain how we will use certain expressions in this decision. We will describe those who occupy the Apartments generically as "occupiers", without expressing any view as to whether they are tenants paying rent or occupying in some other capacity. Where occupiers do so otherwise than under ASTs, we refer to their occupation as being on "GRF" (guest registration form) terms. As we will see, initially occupiers were required to sign AST agreements, but that practice started to fall away from about 2001 and, as a general rule, occupiers now complete a GRF. Other terms of their occupation may be set out in emails or other communications. For the purposes of this decision, occupying on GRF terms (and cognate expressions) simply means occupying but not under an AST. Similarly, as a general rule, we use words such as "lease" and "let" simply to refer to (AST or GRF) terms of occupation and without passing judgment on the legal nature of those arrangements. Finally, when we refer to "premises" or Chelsea Cloisters we are generally referring only to the part of Chelsea Cloister which contains the Apartments and, in particular, we are not referring to the apartments which have been let on long leases.

8. For reasons which will become apparent, we will decide the Liability Appeal in principle, and leave it to the parties to revise the calculation of the amount of VAT due in the light of our conclusions. If they cannot agree the amount due, they may (of course) refer that question back to this tribunal.

THE LIABILITY APPEAL

The Evidence Before Us

9. We heard from Dr Charles Moran, who is the Chairman and Chief Executive Officer of the Chesterlodge Group, of which Realreed and CCSL are subsidiaries, and Mr Colin Reilly, who has been the Finance Director of Realreed and CCSL since May 2016. Both referred to witness statements prepared for this Tribunal and the judicial review proceedings. They were cross-examined by Ms McArdle.

Dr Moran

10. Dr Moran explained that Realreed's business model has remained constant since incorporation. However, over that period, the way in which people book accommodation, whether for business or pleasure, has changed significantly.

11. The business has, at all times, received a significant number of occupiers from corporate customers, such as banks, when they relocate their employees to London for a specified period, such as a secondment. Initially, those corporate customers liaised directly with Realreed to make bookings for their employees. This practice evolved over time to one where HR departments of corporate customers placed the sourcing of accommodation with letting agents or outsourced travel companies, who would handle all aspects of their employees' secondment arrangements.

12. This arrangement has further changed with the advent of and reliance on the internet to one which uses intermediary booking websites, such as booking.com and Expedia. Corporate customers now commonly allow their staff to find and book their own accommodation or, where outsourced agents are used, they use the same intermediary websites to source accommodation even where it is for multiple apartments. The use of intermediary websites has grown dramatically such that, for several years, accommodation bookings, whether for business or personal purposes, have been predominantly made through intermediary websites. Given the predominance of on-line booking websites, it would be uncommercial for any business providing accommodation of any nature not to be listed on intermediary websites. Realreed has therefore listed itself on intermediary websites in order to meet the changing booking behaviours of its potential customers, and not because it has changed its business

model. There are, however, a few corporate customers, in particular certain Japanese banks, which still adopt the traditional approach of making bookings directly with Realreed.

13. Chelsea Cloisters operates like a 'home from home' for its tenants: it provides residential accommodation. The physical appearance of the building is very similar to that of other residential buildings in the vicinity. It does not have signage suggesting the serviced accommodation is a hotel or similar establishment. It is rare for hotels (or similar establishments) at the booking point to offer long-term availability in the same way as Realreed does from the outset.

14. Chelsea Cloisters does not offer room service, or catering of any form, linked to the Apartments. Tenants have fully functioning kitchens and other self-catering facilities within their Apartments and have washing machines and dryers to do all their own laundry. Charges are not made on a per person basis, and there is no additional charge for overnight visitors, nor a requirement for visitors to be registered, as might be the case in a hotel.

15. In terms of council tax, all of the Apartments are rated for residential use, whilst the commercial units (the bar, two restaurants, and Realreed's offices) are rated for commercial use.

16. There is no requirement to drop off a room key at reception when leaving the building. Tenants can, and do, stay for extended periods of time. One tenant stayed in an Apartment for approximately 20 years. A deposit can be requested from an occupant upfront. Where relevant, the deposit will be held in escrow in accordance with relevant statutory obligations imposed on landlords of residential property.

17. Had he wanted to do so, and subject to obtaining necessary planning consents, Dr Moran said that he likely could have transformed the property into a hotel, including by adding facilities such as major catering facilities (e.g. a huge central kitchen), changing the nature of the accommodation offering (e.g. removing kitchens, ovens and clothes washing facilities from Apartments), amending marketing and so on. He never wanted to do so, and he never wanted to run a hotel. He wanted, and has always wanted, to offer a simple, residential service.

18. The report in Realreed's 2006 annual accounts (and in subsequent accounts), refers to "competitive pressures from providers of hotel and rental accommodation". This wording was inserted in response to changes required by the Companies Act 2006 that the report must contain a separate 'business review'. It does not indicate an acceptance by Realreed that it is providing hotel-type accommodation. What it does recognise is that wider market conditions will impact occupancy levels and rental charges. Dr Moran does not suggest that the hotel market, or other forms of accommodation, exercise no competitive constraint on the business.

19. Dr Moran says that the business has always involved the provision of residential accommodation on a longer-term basis than would typically be found in a hotel, with a much higher degree of personal autonomy for the occupant. He exhibited a marketing brochure from 2005, which described an offering that is materially indistinguishable from the service now provided. In cross-examination, Ms McArdle pointed out that this document referred to Chelsea Cloisters as “providing a more cost effective solution to similar standard hotel rooms.” It referred to the “personalised maid service” and listed the facilities on offer including a residents’ bar and three international restaurants. Later, under “Multilingual Services” it said that “Chelsea Cloisters employs a multilingual team of experienced staff who are happy to assist with any queries or translations. Our Japanese and Far East Department handle enquiries from large corporations through to the leisure traveller.” Later it noted that “For leisure and business travellers, London provides a wide variety of entertainment from museums and arts, parks and gardens, shopping, sightseeing through to a

variety of sporting activities. All easily accessible from Chelsea Cloisters." It concluded by observing that "We welcome every year thousands of professional and leisure travellers from around the world."

20. Dr Moran accepts that the advent of the internet has made the accommodation more accessible to short-term and/or leisure travellers, and Realreed has had to adapt somewhat to the new marketplace offered by the internet.

Mr Reilly

21. Mr Reilly explained that CCSL is an associated company of Realreed, with common directors. CCSL provides a maid service, along with dry cleaning Wi-Fi vouchers, key replacement, luggage storage and linen changes to guests. Realreed and CCSL's business activities are linked. CCSL has charged VAT on its services throughout. CCSL issues invoices for room rental as agent for Realreed. Realreed is contractually obliged to provide serviced accommodation to its tenants, but tenants pay CCSL directly for the services provided. At the end of each month, the total value of the room rental is accounted for by CCSL by way of inter-company adjustment to Realreed. There is no invoice raised and no VAT is charged.

22. As far as online third-party booking providers is concerned, Realreed did not sign up with these platforms to compete with hotels. It did so due to their popularity and evolving booking trends. If a customer filtered their choice, selecting 'hotels' only, they would not find Chelsea Cloisters on booking.com, hotels.com or expedia.co.uk. Chelsea Cloisters features only under "Apartments" on these websites. The agreements Realreed entered with these suppliers are generic agreements, not tailored to Realreed's accommodation offering, and Realreed is typically unable to change these terms. That is why words like "hotel" crop up in the agreements. The main purpose of the agreements is to enable Realreed to advertise the accommodation on popular websites that have a global customer reach. It does not matter to Realreed from a commercial perspective how it is defined in the contract by the intermediary.

23. The composition of Realreed's customer base has changed gradually over time. The earliest records of occupancy rates, for October 2007 to December 2008, show that 65% of stays were for 28 days or more. In the 2014/15 year, that percentage was 49.8%, and in 2018/19 it was 38.5%. Even though the figure has decreased, more than a third of the occupiers in 2019 stayed for more than 28 days; that is very different from the customer base that he would expect to find in a West End hotel or similar nearby establishment where he understands that any customer staying for 28 days or more would be a rarity. A GLA Working Paper published in April 2017 (Working Paper 88: Predictions of demand and supply for accommodation in London to 2050) indicated that, over the previous decade, international tourists spend on average 6.1 nights in London when they visit, whereas domestic tourists spend 2.27 nights per visit.

24. We were shown a note which calculated the average nights per stay in Chelsea Cloisters. The methodology is such that the author indicates that it should only be used to draw a high-level comparison between stays in Chelsea Cloisters and in hotels and similar establishments in London. Nevertheless, the paper shows that the average number of nights per stay was 16.66 in 2010/11, 15.39 in 2011/12, 10.92 in 2012/13, 9.25 in 2013/14, 11.55 in 2014/15 and 11.52 in 2015/16. If nothing else, the paper clearly shows that the average stay in Chelsea Cloisters is significantly longer than the GLA-calculated average.

25. Mr Reilly commented that Realreed's business model has always been, and remains, one which prefers longer-stay occupiers over short-stay occupiers. The preferred occupant is a corporate guest staying for an initial 7- or 28-day period, with 'open' plans to continue and re-extend as long as they require. These occupiers are more suited to Chelsea Cloisters, as

they are more like the wider resident community within the building and would use the facilities in the Apartments, e.g. kitchen and washing machine, which would not typically be found in hotel rooms. Use by longer-term occupiers avoids a build-up of check in and check out traffic that would be seen in a hotel, but would be inappropriate in a residential building such as Chelsea Cloisters. A benefit of renewing the occupiers' stays is that it allows Realreed to renew directly with the occupant at the end of an initial or extended stay and avoids the need to pay a commission on the extended stay. Longer-stay occupiers also reduce overhead costs as standard room facilities (such as shower gels shampoos toilet rolls etc) are not renewed at all during stays.

26. In terms of the differences between a typical hotel's offering and that of Realreed, Mr Reilly observed:

> (1) Occupiers are not provided with breakfast facilities. Even the most basic facilities provided by hotels, for example breakfast and tea and coffee making facilities, are not provided in Chelsea Cloisters. Occupiers are merely provided with a kettle. There is also no "room service'·. Mr Reilly mentioned that CCSL provided breakfast boxes, but only to a limited degree. 314 invoices were raised for breakfast boxes in the period 2013/14 to 2067/17 and one invoice was raised in 2019. He described this as an insignificant number, and the total quantum of the invoices is also immaterial to the company's revenue, considering how many occupiers stayed at Chelsea Cloisters in this period.
>
> (2) When supplies of provisions need to be replenished, it is the occupier's responsibility to purchase these. This includes the most basic provisions such as toilet paper. Indeed, occupiers have on occasion asked for replacement toilet rolls and soap and have been told that they are not provided.
>
> (3) Each apartment has its own separate postal address, to which occupiers will receive any post directly from Royal Mail (or a courier service). Mail (and parcels) are not collected at reception for onward distribution to occupiers.
>
> (4) All non-AST occupiers with Realreed. other than corporate groups with advance credit terms, must pay for their full booking prior to being provided access to their room. Occupiers have been denied access to Apartments when it has incorrectly been recorded that the occupant had not paid in advance. Further, Realreed does not hold a credit card charge for incidental extras as a hotel typically would.
>
> (5) Although there are commercial units in the Chelsea Cloisters building, these are operated by third parties targeting the local community, not occupiers staying at Chelsea Cloisters. Further, occupiers of Chelsea Cloisters are not provided with any centrally-negotiated discounts or preferential rate. Additionally, there is no facility to charge costs to an Apartment in the same way it is possible to charge, for example, food and drink costs to a hotel room.
>
> (6) As Realreed uses ASTs for longer-staying occupiers, it encounters circumstances where it is unable to simply remove a non-paying occupant in the way a hotel can. For example, a section 8 notice under the 1988 Housing Act has been lodged with the Courts for the eviction of a current occupant on an AST for non-payment of rent. A hotel in similar circumstances would imply disable the room key-card and remove belongings from the room. without requiring recourse to the Courts.

27. Both those occupiers with ASTs and those staying for a shorter period do not pay for utilities based on their usage. The price they pay to Realreed for the accommodation includes the provision of utilities. The reason for this was to simplify administration and to provide the

customer with certainty of the cost of their stay irrespective of their duration and usage. Each Apartment also requires its own television licence, which is paid in a group invoice.

28. Each Apartment is subject to Council Tax. We were shown sample Council Tax bills from The Royal Borough of Kensington and Chelsea addressed to Realreed (which described Apartments as "Unocc'd/furnished 2nd home"). We were also shown a sample electricity bill from SSE to Realreed which itemised the usage and amount due in respect of each Apartment. Thames Water sent Realreed a bill for Chelsea Cloisters made up of a series of amounts due in respect of each Apartment.

29. We looked at a typical AST agreement. This is much more formal in style than the guest booking form and contains the kinds of provision one might expect to see in a lease of residential premises. It runs to 8 pages (excluding the space for execution) and provides for rent, user and other covenants by the tenant. The landlord (identified as Realreed) covenants "to provide" a daily maid service. Although there is no prohibition on visitors, there is a limit on the number of people who can reside in the Apartment. In this case the limit was two and the Apartment was let to two individuals jointly. The term of the letting is 15 days short of six months. This is subject to what appears to be a one month tenant's break right, although the drafting of the provision is somewhat opaque. (Such a right would be consistent with Mr Cutting's evidence.)

30. In contrast a GRF runs to a single page. It has space for the guest's name (and company, if relevant), contact details and proof of ID, but the counterparty (the service provider) is not identified. It sets out the guest's dates of arrival and departure, check-in and check-out times. It states that the guest acknowledges joint and several liability for all "services rendered". Guests acknowledge that "Chelsea Cloisters" is not responsible for their belongings/valuables. There is a £80 charge for losing a key. Finally, the form indicates that "Chelsea Cloisters Serviced Apartments would like to keep in touch with you" and a guest gives permission for the use of their personal information for administrative and marketing purposes.

31. We reviewed a number of agreements with reservation service providers including Agoda (based in Singapore), Booking.com, Expedia, In1 Solutions, HotelDirect.co.uk. These agreements use vocabulary such as "hotel" and "room/s", but we agree with Mr Reilly that these agreements appear to be very much standard agreements with little more than the counterparty's details to be included. They certainly do not resemble bespoke agreements which are the subject of significant negotiation. One agency (Egencia) headed a document "Target Business Travellers with Egencia".

32. We reviewed pages for Chelsea Cloisters on Booking.com, Hotels.com, Expedia.co.uk. Ms McArdle made the obvious point, when cross-examining Dr Moran, that using Hotels.com rather suggested that Realreed was least to some extent in competition with hotels.

33. We also reviewed a large number of rate cards provided to corporate users, intermediaries and others, which set out the price for different combinations of lengths of stay and type of accommodation. Mr Reilly explained that they are sent to potential corporate customers and booking agencies at the beginning of each calendar year to provide information such as the relevant accommodation rates, booking procedures and the cancellation policy. The rate cards are also used internally by the marketing team to provide them with contact details of the potential corporate customers and booking agencies and also so they are aware of the room rates previously quoted. Prices included a "maid service Monday to Friday (except Bank Holidays) and weekly towel and linen change". The cancellation policy was explained as was the fact that payment was due in full on arrival and,

if a guest wanted to shorten their stay, no refund would be given. Some indicated that the quoted rates included utilities, 24hhr receptions, porters and security and an end of tenancy clean and laundry. None of these cards identified the service providers.

34. Mr Reilly explained that, to book Realreed's serviced accommodation advertised on a rate card, a customer needs to email or call a member of the marketing team who will then discuss the customer's requirements. When a booking is made, the email exchanges (or in some cases a booking form) would be regarded by Realreed as the formal agreement between the parties. Ultimately, Realreed would send out a booking confirmation by email (in past years by fax) to confirm the booking.

Mr Michael Cutting

35. Realreed put in the witness statements prepared for the judicial review proceedings. Primarily, these were the statements prepared by Mr Reilly and Dr Moran and they were cross-examined by Ms McArdle. A further witness statement was that of Mr Cutting, who was the Finance Director and subsequently Managing Director of Realreed from June 1989 until December 2014, when he retired. Although he was not cross-examined, he provided some useful background history of Chelsea Cloisters, as follows.

> (1) The split between Realreed's lettings business and the provision of services was one effectively inherited from the previous owner. Realreed and CCSL maintained this split between the provision of accommodation and the provision of cleaning and related services between two distinct (but related) companies. Realreed was the business that provided the accommodation, namely letting out the studio, one-bedroom and two-bedroom self-contained Apartments on a short- and long-term basis. CCSL provided services to the tenants of those Apartments, such as a maid service.
>
> (2) In 2005, bookings for Chelsea Cloisters were taken via their own website, via booking agent websites such as Euracom, via walk-ins, and they had a base of repeat corporate tenants. In 2005, the duration of tenants' stays was mixed. Some tenants would stay only a single night, and others would stay for lengthy periods.
>
> (3) With a change of personnel in or around 2001, the initial insistence on occupiers signing Assured Shorthold Tenancies ("ASTs") diminished, so that over time fewer and fewer occupiers would sign one. Those who did would sign with the benefit of a break clause, so that the term need not last for the full statutory period of 6 months. Occupiers staying for only a night or two would not be very willing to sign ASTs and the practice of requiring them to do so eventually fell into desuetude.
>
> (4) In terms of the VAT treatment of the two businesses, CCSL would provide tenants with two invoices.
>
> > (a) One invoice would be for the services provided by CCSL, and would include VAT at the standard rate. CCSL had always treated its provision of services to Realreed's tenants as a fully taxable one, and it accounted for VAT on the sums it received as consideration for those services. The tenants would pay CCSL directly for those services.
> >
> > (b) The second invoice would be for the room rental; that would be issued by CCSL as agent for Realreed. The invoices for rent did not include VAT. Likewise, no VAT was reclaimed by Realreed in relation to any purchase related to the provision of the accommodation, such as the purchase of beds.
>
> (5) At the end of each month, the total value of the room rental would be accounted for by CCSL by way of an inter-company journal adjustment to Realreed. There

would be no invoice raised and no VAT would be charged by CCSL to Realreed. CCSL and Realreed have accounted for the room rental in this way since Realreed began trading.

36. We were shown sets of invoices from CCSL, where the rental charges and those for the maid services over the same period were invoiced separately with VAT charged on the invoice for services but not on the invoice for accommodation.

37. We were shown extracts from the Chelsea Cloisters historical website. Under the heading "Luxury Serviced Apartments to Let" there is a picture of the entrance to Chelsea Cloisters. Beneath that, the text reads:

> "Situated in the heart of Chelsea, one of the most fashionable and cultural areas of London, bordered by the elegant shopping and gastronomic facilities of the Kings Road, South Kensington and Knightsbridge. Chelsea Cloisters invites you to visit our prestigious building, only minutes away from the London Underground and within easy reach of the city, the West End and international connections from Waterloo, Heathrow and Gatwick.
>
> Our International Management team are devoted to ensure your enjoyment of our hospitality in one of our luxury designed Apartments.
>
> Fine quality en-suite bathroom and fully fitted separate kitchen incorporating modern appliances are standard features in every apartment and full central heating with constant hot water add to your comfort."

38. The website says that "Chelsea Cloisters offers the following services" and goes on to list,

- 24 hour reception, security and porters
- Maid service
- dial telephone and message taking service
- Satellite television with 30 channels featuring 12 languages
- Three international restaurants
- Residents' bar
- Extensive range of business services
- Residents' parking
- Hairdressing and beauty salon
- Baby sitting/cot hire
- Laundry/dry cleaning service
- Theatre reservations
- Newspaper delivery
- Boardroom hire
- Welcome pack on request

The website contains a rate card and an ability to submit a booking request.

39. We also looked at a more modern (and very different) version of the website. It too refers to a daily maid service and weekly towel and linen changing. It refers to check in and check out times, cancellation policies. On-site facilities are listed as:

- Secure Parking
- 24-hour concierge
- check-in desk
- 24-hour security and CCTV
- 24-hour porterage

- Four lifts
- Secure underground parking
- In-house bar
- Satellite and Freeview TV with over 50 channels featuring 8 languages
- WiFi (chargeable)
- Safe

The Law

The scope of the exemption

40. In the UK section 31 VATA provides that a supply of goods or services is exempt if it is of a description specified in Schedule 9. Item 1, Group 1 (Land) of Schedule 9 applies to:

> "The grant of any interest in or right over land or of any licence to occupy land, or, in relation to land in Scotland, any personal right to call for or be granted any such interest or right, other than—
>
> …
>
> (d) the provision in an hotel, inn, boarding house or similar establishment of sleeping accommodation or of accommodation in rooms which are provided in conjunction with sleeping accommodation or for the purpose of a supply of catering;"

41. Note 9 provides:

> (9) "Similar establishment" includes premises in which there is provided furnished sleeping accommodation, whether with or without the provision of board or facilities for the preparation of food, which are used by or held out as being suitable for use by visitors or travellers.

42. Article 13B (Other exemptions) of Directive 77/388/EC ("the Sixth Directive") provided that:

> "1. Without prejudice to other Community provisions, Member States shall exempt the following under conditions which they shall lay down for the purpose of ensuring the correct and straightforward application of the exemptions and of preventing any possible evasion, avoidance or abuse:
>
> …
>
> (b) the leasing or letting of immovable property excluding:
>
> 1. the provision of accommodation, as defined in the laws of the Member States, in the hotel sector or in sectors with a similar function, including the provision of accommodation in holiday camps or on sites developed for use as camping sites;"

43. Article 135 of Directive 2006/112/EC ("the PVD") provides that:

> "1. Member States shall exempt the following transactions:
>
> …
>
> (l) the leasing or letting of immovable property
>
> 2. The following shall be excluded from the exemption provided for in point (l) of paragraph 1:
>
> a) the provision of accommodation, as defined in the laws of the Member States, in the hotel sector or in sectors with a similar function, including the

provision of accommodation in holiday camps or on sites developed for use as camping sites;"

44. The scope of the exemption for "letting of immoveable property" has been considered by the CJEU in a number of cases. In *Belgian State v Temco Europe SA* (Case C-284/03) a company refurbished office premises it owned and granted three group companies "assignments" (allowing them the use and enjoyment of premises on certain conditions). The CJEU, having observed that the exemptions in Article 13 of the Sixth Directive "have their own independent meaning in Community law", drew a distinction (at [20]) between "a transaction comprising the letting of immovable property, which is usually a relatively passive activity linked simply to the passage of time and not generating any significant added value" and "other activities which are either industrial and commercial in nature, such as the exemptions referred to in Art.13B(b)(1) to (4) of the Sixth Directive, or have as their subject-matter something which is best understood as the provision of a service rather than simply the making available of property, such as the right to use a golf course, the right to use a bridge in consideration of payment of a toll." Against that background, it held that the period of letting is not decisive "even if the fact that accommodation is provided for a brief period only may constitute an appropriate basis for distinguishing the provision of hotel accommodation from the letting of dwelling accommodation". Whilst a tenant would be expected to have an exclusive right of occupation, this can be restricted (e.g. the landlord might reserve the right regularly to visit the property let) and this will not stop the tenant having exclusive occupation as regards all other persons.

45. In *Walderdorff v Finanzamt Waldviertel* (Case C-451/06) Mrs Walderdorff granted a fishing club a 10 year right to fish in two ponds that she owned and in a third pond which was publicly owned but where she had registered fishing rights. The CJEU noted that the club only had the right to fish in the ponds and Ms Walderdorff reserved the right to fish in those waters for herself and for one guest per day authorised by her. It also noted (at [18]) that provisions granting exemptions are to be construed narrowly, as exceptions to the general principle that VAT is levied on all services supplied for consideration. On that basis the CJEU held (at [22]) that "one of the elements in the definition of the Community law concepts of leasing or letting immovable property which are employed within the Community system of VAT is lacking in the present case, given that the contract for that grant, at issue in the main proceedings, does not confer on the angling club the right to occupy the immovable property concerned and to exclude any other person from it."

46. The scope of the exception in Article 13B(1)(b)(1) was considered by the CJEU in *Blasi v Finanzamt München I* (Case C-346/95). The referred questions concerned the provision of furnished accommodation to refugees on lets that were formally concluded for less than six months, but where in practice the refugees occasionally stayed longer. The buildings used for accommodation were normal residential buildings each containing several dwellings. Fully furnished rooms equipped with cooking facilities were made available to the families. The rooms were cleaned by the refugees themselves. Mrs Blasi supplied and washed the bedlinen and saw to the cleaning of the landings, staircases, bathrooms and lavatories. Occupiers were not supplied with meals. There was no reception area in the buildings, nor any lounges or other common amenity rooms.

47. The German tax authorities assessed Mrs Blasi to VAT on the basis that her activities fell within the German law provision corresponding to Article 13B(1)(b)(1), which provided that, "The letting of living and sleeping accommodation which a trader keeps available for the short-term accommodation of guests ("Fremden") shall not be exempted". If, under the letting agreement, the period was less than six months, the provision of accommodation would be taxable. On that basis, the transactions carried out by Mrs Blasi could not be

exempted from VAT. Even if she intended the dwellings in question to be used for long-term lets (on her calculation, the average let was for 14.4 months), no long-term agreement was ever concluded.

48. The Court held that the exemptions provided for by Article 13 of the Sixth Directive are to be interpreted strictly, since they constitute exceptions to the general principle that turnover tax is to be levied on all services supplied for consideration by a taxable person, and the exceptions (which impose VAT) should consequently not be interpreted strictly.

49. At [20] the Court held that the words 'sectors with a similar function' should be given a broad construction since their purpose is to ensure that the provision of temporary accommodation similar to, and hence in potential competition with, that provided in the hotel sector is subject to tax. At [21]-[23] it was noted that:

> "21 In defining the classes of provision of accommodation which are to be taxed by derogation from the exemption for the leasing or letting of immovable property, in accordance with Article 13B(b)(1) of the Sixth Directive, the Member States enjoy a margin of discretion. That discretion is circumscribed by the purpose of the derogation, which, in regard to making dwelling accommodation available, is that the — taxable — provision of accommodation in the hotel sector or in sectors with a similar function must be distinguished from the exempted transactions of leasing and letting of immovable property.
>
> 22 It is consequently a matter for the Member States, when transposing Article 13B(b)(1) of the Sixth Directive, to introduce those criteria which seem to them appropriate in order to draw that distinction.
>
> 23 Where accommodation in the hotel sector (as a taxable transaction) is distinguished from the letting of dwelling accommodation (as an exempted transaction) on the basis of its duration, that constitutes an appropriate criterion of distinction, since one of the ways in which hotel accommodation specifically differs from the letting of dwelling accommodation is the duration of the stay. In general, a stay in a hotel tends to be rather short and that in a rented flat fairly long."

50. On that basis the Court concluded that Article 13B(b)(1) did not preclude taxation in respect of agreements concluded for a period of less than six months, if that duration is deemed to reflect the parties' intention. It was, however, for the national court to determine whether, in a case before it, certain factors (such as the automatic renewal of the letting agreement) suggested that the duration stated in the letting agreement did not reflect the parties' true intention, in which case the actual total duration of the accommodation, rather than that specified in the letting agreement, would have to be taken into consideration.

51. The Advocate General had commented to the same effect. He observed:

> "16. However, while generally exempting the leasing or letting of immovable property, Article 13B(b) also provides for exclusion of certain transactions from exemption. The common feature of those transactions is that they entail more active exploitation of the immovable property justifying further taxation in addition to that levied upon its initial sale.
>
> 17. With more particular reference to Article 13B(b)(1), it may be noted, first, that its terms, in particular the phrases `accommodation, as defined in the laws of the Member States' and `sectors with a similar function', are somewhat imprecise. It seems to me that the intention was to leave the Member States some latitude in defining the precise limits of the exclusion.

> 18. Secondly, as already noted, Article 13B(b)(1) lays down an exclusion from the exemption and therefore does not fall to be construed strictly. Indeed it seems to me that the words `sectors with a similar function' should be given a broad construction since their purpose is to ensure that the provision of temporary accommodation similar to, and hence in potential competition with, that provided in the hotel sector is subject to tax.
>
> 19. As regards the German provision, it is true that the short-term letting of residential property may not entail all of the additional supplies of goods and services, such as provision of meals and drinks, cleaning of rooms, provision of bed linen etc., normally provided in hotels. Nevertheless, there can be no doubt that a taxable person offering, for example, short-term holiday lets of residential property fulfils essentially the same function as - and is in a competitive relationship with - a taxable person in the hotel sector. The essential distinction between such lettings and exempt lettings of residential property is the temporary nature of the accommodation. In any event, short-term lets are more likely to involve additional services such as provision of linen and cleaning of common parts of buildings or even of the accommodation itself (indeed a number of such services are provided by Mrs Blasi); moreover, they involve more active exploitation of the property than long-term lets in so far as greater supervision and management is required.
>
> …
>
> 21. Moreover, it seems to me that the requirement flowing from the case-law of the Bundesfinanzhof that, in order for the letting of an immovable property to qualify for exemption, there must be an intention, evidenced by a lease or other agreement, to let the property for a minimum period of six months is not unreasonable. It provides a workable and legally certain means of distinguishing between short-term accommodation similar to that provided in the hotel sector and the longer-term letting of residential property for which the Directive provides exemption. A hotel or hostel will be willing to accept guests for potentially short stays, whereas a landlord interested in more passive longer-term lets will require an agreement providing confirmation of the tenant's intention to stay for a longer period. I see no reason to interpret the Directive as imposing a maximum of three months as the Commission suggests."

52. Turning to UK decisions, the first is a decision of the VAT Tribunal in *International Student House v CCE* (Case LON/95/3142). ISH provided accommodation to students from a range of foreign countries. It was described in evidence as providing a home from home for registered students who were here far from home. It provided accommodation, counselling and welfare services and a programme of activities. Students were expected to take part in these activities. The expression "participatory residents" was thought to be appropriate. Students stayed at ISH for at least one academic year, sometimes two, and, in rare cases if they made a great contribution to ISH for three. They were made welcome and given the best facilities to enable them to succeed in their studies. Two issues were considered. The first was whether ISH was providing education. The second was whether the supplies it made were grants of interests in or rights over land and, if they were, whether the exception in paragraph (d) applied. Focusing on the definition of "similar establishment" in Note 9, the Tribunal commented:

> Note 9 defines "similar establishment" as including "premises in which there is provided furnished sleeping accommodation … which are used by or held out as being suitable for use by visitors or travellers". … . It seems to the Tribunal that these words must be interpreted in their normal every day English sense in the context in which they find themselves. Thus the term

> "visitors" used in Note 9 cannot be intended to be used in the sense of "visitors to the United Kingdom". A visitor is, in the normal use of the English language, a person who visits a place or person. A traveller is one who travels from one place to another. Both these categories of persons require to be able to use sleeping accommodation. Those premises which provide furnished sleeping accommodation, and which are used or held out as being suitable for use by such persons come are included within the definition of "similar establishment". The question arises whether one who is a visitor to the United Kingdom is automatically a visitor throughout the period of his stay in the United Kingdom and whether one who has travelled to the United Kingdom is automatically a traveller throughout his time in the United Kingdom. This seems to the Tribunal to be an impossible conclusion. There must be a moment when a person who resides in a place which is not his home ceases to be a visitor to that place. In the normal everyday use of the English language a person whose residence has a degree of permanence is neither a visitor nor a traveller. It is true that in the appeal of Mrs McGrath the Tribunal refused to accept the argument that a guest house was distinguished from a hotel or boarding house by the fact that the guests considered the guest house to be their home. However the Tribunal's conclusion was based on the fact that the establishment was what it described itself to be in its title a "guest house". It mattered not to the Tribunal whether the residents in the guest house were long or short terms residents. This however is of no help in deciding on the meaning of the term "visitors or travellers" in the context of premises which are used or held out as being suitable for use by visitors or travellers. A further difficulty arises from the drafting of Note 9. Using the words "visitors or travellers" in isolation allows those words to be considered in a general sense. Reading them however in the context shows that the significance of those words relates to the nature of the premises, that is to say premises used or held out as suitable for use by visitors or travellers. That implies in the view of the Tribunal that the meaning of the word "visitors or travellers" is simply a description of the premises that is to say premises used or held out as being suitable for use by such persons. Therefore Note 9 means premises which, if one were to give a visual illustration, carry a notice to say "these premises are available for use by visitors or travellers" or which whether they are so held out or not are used by such persons. It is not possible to read the terms of Note 9 so widely as to include any guest room in a private house, used by a visitor, perhaps a member of the family, without there being any element of commercial exploitation. The same idea of commercial exploitation arises by implication from Customs and Excise Notice 709/3/93, and the earlier Notice 709/3/86."

53. The Tribunal held that ISH was not similar to a hotel because of its special purposes and way of working (it exercised choice over residents and there was a high degree of control over the students and an emphasis on corporate use). The Tribunal held that, to fall within Note 9 there had to be an element of commercial exploitation, which was lacking in that case.

54. Next, we have *Acorn Management Services Limited v CCE* (LON/00/534). The question here related to arrangements the appellant made with (usually) American universities under which students occupied accommodation (including accommodation sometimes used by tourists) in buildings owned by the appellant. The students attend courses in the United Kingdom run by those universities. Some of the accommodation was occupied by faculty members rather than by students. A university would message the appellant before the accommodation was required. The space was booked at that time and the university was given details (address, internal numbering of apartments etc) of the accommodation which

was reserved. The university paid the appellant in full before any student arrived to take up residence. On the question of whether the students were "visitors or travellers" the Tribunal set out the observations on this issue in *International Student House* (supra) and then went on to observe:

> "We can see the force of these observations. The students in that case were normally there for a course which would last several years of which at least one was spent in the accommodation in question. The student in this case is present in the United Kingdom (and usually at the accommodation as well) for, on average, only 15 weeks.
>
> It is difficult to say exactly when a person ceases to be a visitor on the basis that his stay has that degree of permanence referred to in *ISH* but we have concluded that whenever that time occurs it does not occur during the average stay of the student in this case. In finding this we have taken into account that the students in the present case are in the United Kingdom for a purpose. That expressed purpose is not to make a general visit to the United Kingdom (although the student may well take the opportunity to visit different places while he is here) but to pursue a course of study which happens to take place here. Even so, this does not in our view prevent him from being a visitor. Many visitors have a purpose in mind when they come to a place even when they intend to be in that place only for a short period. As the premises are clearly both used and held out as suitable for use by students and we have concluded that they will be visitors so that the expanded definition contained in note (9) applies."

55. In *Fortyseven Park Street Ltd v HMRC*, [2019] EWCA Civ 849, the taxpayer operated a property creating 49 self-contained furnished apartments, or 'residences'. The facilities at the property were said to be comparable with those of a small boutique hotel. The taxpayer sold fractional interests in the property which, under the terms of a membership agreement, entitled the purchaser (or 'member') to occupy a residence for a certain period each year. The property was managed by another company within the taxpayer's group, which provided certain services, relating both to the administration of the scheme, reservations and other customer services. Members paid an annual residence fee, which funded services such as a valet service, a 24-hour front desk, a concierge service and tour desk, a business centre, wi-fi, fax and photocopying services, a daily maid service and luggage storage. Other services such as room service and grocery deliveries, currency exchange, and a laundry and dry-cleaning service, were available on extra payment.

56. The FTT decided that the taxpayer supplied rights that fell within the land exemption but were excepted from it by paragraph (d). The Upper Tribunal agreed with the FTT on the land exemption issue, but disagreed on the hotel sector exclusion. The Court of Appeal reversed the Upper Tribunal decision. The Court of Appeal summarised the three issues they needed to decide as:

> (i) Was the land exemption inapplicable because 'the right to occupy property as if that person were the owner and to exclude any other person from enjoyment of such a right' was missing from FPSL's supplies to Members? (Issue 1.)
>
> (ii) Was the land exemption inapplicable because the supplies at issue did not involve merely a relatively passive activity but rather significant added value? (Issue 2.)
>
> (iii) Supposing that the supplies were in principle capable of falling within the land exemption, were they excluded from the exemption by item 1(d) ('Item 1(d)') in Group 1 of Pt II of Sch 9 to the VATA? (Issue 3.)

57. On Issue 1, the Court of Appeal agreed (at [33]) with the Upper Tribunal that the 'true underlying supply is of a licence to occupy, which a member can exercise by means of the reservation system'. In practice, members could always be accommodated, albeit that they would not always get their first choice of nights.

58. On Issue 2, the Court concluded that the grant of a fractional interest was more complicated than making space available in a passive manner (which is the essence of the land exemption) and so the supplies the taxpayer made were not within the land exemption. At [49] Newey LJ said:

> "In the end, I have concluded both that the grant of a Fractional Interest involved more than a mere letting transaction and that the obligations which FPSL undertook as regards the provision of hotel-type services cannot be regarded as ancillary or (in the words of the CJEU in *Temco*) 'plainly accessory'. The 'essential object' of the transactions was not, as I see it, 'the making available, in a passive manner, of premises or parts of buildings in exchange for a payment linked to the passage of time', but 'the provision of a service capable of being categorised in a different way' (to quote the CJEU in *Temco* once again). This was not 'simply the making available of property' (*Temco*, para 20 of the judgment), but pre-payment for accommodation 'in an environment similar to a hotel and with the services which can be expected in a hotel, repeatedly over a number of years' (para [289] of the FTT decision). As in the *Luc Varenne* case, what was being supplied was 'a more complicated service'. It is also not without relevance that the land exemption has to be construed strictly (see para [23](ii) above)."

59. On Issue 3, Newey LJ concluded that the Upper Tribunal was not entitled to interfere with the FTT's conclusion that the supply fell within paragraph (d). The Upper Tribunal had concluded that the taxpayer supplied 'a right which comprises more than something in the nature of short-term accommodation in the hotel sector' on the basis, essentially, that the supply was 'of a long-term right'. However, Newey LJ considered that the fact that such a right is of a long-term nature should not necessarily preclude application of the exclusion. The duration of the right was not of itself determinative but rather a factor which could properly be taken into account. He went on to conclude (at [60]):

> "In my view, it was open to the FTT to consider that the grant of a Fractional Interest, carrying with it rights to 'sleeping accommodation' in an establishment similar to a hotel, is appropriately characterised as 'the provision in an hotel … or similar establishment of sleeping accommodation' within the meaning of Item 1(d). … Issue 3 only arises at all if the supplies at issue are taken to have had as their 'essential object' the making available of premises 'in a passive manner': the supplies would not otherwise be capable of falling within the land exemption and the Item 1(d) exclusion would be immaterial. If, however, FPSL's role was sufficiently passive for the land exemption to be in point, it is hard to see how, leaving aside the Upper Tribunal's concern that the supply was 'of a long-term right' (which I have already commented on), 'sleeping accommodation' could be considered to have been provided as part of a wider supply in such a way as to render the exclusion inapplicable."

60. Finally, we come to *City YMCA London v HMRC*, [2021] UKFTT 0477 (TC). YMCA operated two hostels to provide temporary accommodation to homeless young people. The hostel comprised 87 single, uniformly furnished en-suite bedrooms with communal facilities (such as kitchens, eating areas, lounge, and laundry). There were two issues in this case. The first was whether the supply was of 'a licence to occupy land' within the opening words of

Item 1. The second was whether the hostel was a "similar establishment" to a hotel within paragraph (d).

61. The Tribunal held that the supply made by YMCA, namely the grant of a right for the use and enjoyment of a bedroom to the exclusion of all others, for an agreed term, in exchange for a payment linked to the passage of time, was a supply within the meaning of 'leasing or letting of immovable property' for the purposes of Article 135(1) of the PVD. HMRC's next argument was that the "added value" facilities provided by YMCA took the supply out of the exemption, because it was not 'a passive supply of exclusive possession of a specific part of a building'. The "added value" services were said to be matters such as access to communal facilities such as kitchens and lounges, and services such as signposting, and a degree of oversight and control. The Tribunal noted that, in *Temco* the CJEU held that, where the 'essential object' of a supply is the making available of premises, then the supply cannot be characterised as a provision of a different service. So, having found the essential object of YMCA's supplies to be the making available of a part of the premises (i.e. a bedroom) to each resident, in a passive manner, in return for a payment linked to the passage of time, the Tribunal went on to hold that YMCA's supplies could not be categorised in a different way.

62. The next question was whether the exclusion in paragraph (d) applied to YMCA's services. The Tribunal held (at [142]) that the critical factor in determining when the exclusion from the land exemption applies is the purpose of the provision of accommodation. At [142] the Tribunal went on to comment as follows:

> "The critical distinction is to be drawn between long-term lettings of residential accommodation (an exempt supply) and short-term lettings of accommodation as in the hotel sector (excluded from exemption). The rationale behind the exclusion is the economic reality associated with the provision of short-term accommodation, which invariably involves additional services, and greater supervision and management being provided for the purpose of providing the short-term accommodation."

63. In that case the temporary nature of the accommodation was the "very essence" of the supplies YMCA made. This was explained like this:

> "In reality, the length of stay of a resident varies from one week to two years, with about 30% of lets being less than 6 months. The fact that no assured tenancy can arise from the contractual arrangement, however long the overall duration of stay, allows [YMCA] to exercise its right to evict a resident with 24 hours' notice. While the majority of lets (70%) last for longer than 6 months, that does not change the short-term nature of the accommodation provision, given that there are multiple factors that enable [YMCA] and a resident to terminate the Agreement at short notice."

64. Looking at the question from a functional perspective (so as to achieve fiscal neutrality between hotels and providers of accommodation similar to the hotel sector), the Tribunal noted (at [147]) that "if a potential resident is not accommodated by [YMCA], the relevant agency or local authority may be sourcing alternative accommodation in a hotel or a hostel for the homeless young person. Adopting a functional approach to the construction of Item 1(d) exclusion, and having regard to the economic reality in relation to the function of the [supply by YMCA], I conclude that Item 1(d) exclusion is applicable to the [supply by YMCA]".

65. Having analysed the question from a purposive and functional perspective, the Tribunal concluded that the supply of accommodation by YMCA fell within the exclusion in paragraph (d)

66. In *BLS1 Limited v Isle of Man Treasury* (TC/2020/00424 and TC/2020/02977) the Isle of Man VAT and Duties Tribunal (Judge Jonathan Cannan and Mr Laurence Vaughan-Williams) considered whether certain supplies fell within paragraph (d) (which applies to the provision in a hotel, inn, boarding house or similar establishment of sleeping accommodation) of Item 1, Group 1, Schedule 10 of the Isle of Man Value Added Tax Act 1996. The Isle of Man legislation contained a Note to Group 1 that was identical to Note 9 in the UK legislation (although, unhelpfully for us, numbered (10)).

67. BLS1 operated a building called The Quarters in Swiss Cottage. It comprised 81 furnished studios of varying sizes and grades. All had a king size bed, a living area including a sofa, a small desk, a kitchenette and a bathroom. The kitchenette was furnished with a microwave grill, a sink, a kettle, a Nespresso coffee machine and a small refrigerator with an icebox. There was a very small worktop with two kitchen cupboards. Basic crockery was provided. The studios had a smart TV and room safe but no kitchen hob, toaster or open flames. There were no laundry facilities in the studios. Every other floor of the building had a large communal kitchen. There was a weekly clean and change of linen and towels. There were house rules, which included a requirement for permission for overnight guests. A typical licence would be between 3 and 6 months. Taking into account renewals, the majority of occupiers would stay for 6 months or more. However, some stays were for less than 3 months. There was a restaurant on site (fitted out by BLS1, but leased to and operated by a related company) open from 12 noon until midnight every day.

68. The Tribunal first held that the supplies made by BLS1 were such that they did not fall within the land exemption (ignoring the exclusion in paragraph(d)). The rights to occupy were granted in the context of an establishment where occupiers would typically stay for at least 3 months and where the majority of occupiers stayed for more than 6 months. At [133] it commented:

> "Against that background, the restriction on overnight guests leads us to conclude that an occupier does not enjoy rights to use a studio as an owner. Someone who is living in a studio for those periods of time would expect, if occupying as owner, to be able to invite any guest to stay overnight. In contrast, a short stay guest at a hotel would not necessarily expect to be able to invite any guest to stay overnight without restriction."

69. In addition, the services provided by BLS1 in the context of the periods for which studios were occupied would alter the essential object of the supply if it would otherwise have been exempt. The services were weekly cleaning and housekeeping, in-house maintenance, 24 hour reception desk, superfast and secure wifi, a television service, a lounge area, bicycle shelter, post and parcel collection and underfloor heating. The appellant also engaged with Camden Council and satisfied the council tax liability of occupiers, which was included in the licence fee. Additional cleaning services, a linen service, an on-site gym and a restaurant were available for a charge. The Tribunal was satisfied that they involved considerable supervision and management on the part of BLS1. In their view, the services provided or available to occupiers were not plainly accessory to the supply of land.

70. The Tribunal then turned to the exclusion in paragraph(d). In relation to the general test for a similar establishment falling within paragraph (d), the Tribunal held (at [145]) that a similar establishment "will be marked by a supply of temporary accommodation, with an element of service, which is in competition with or potential competition with the hotel sector".

71. The Tribunal broke down Note 9 (in the UK VATA) as applying to premises which:

(1) provide sleeping accommodation, and either

(2) are used by visitors or travellers, or

(3) are held out as being suitable for use by visitors or travellers.

72. That led to a consideration of what makes someone a "visitor" or a "traveller". As far as visitors are concerned, the Tribunal said this (at [148]-[149]):

> "It is not always helpful to try and define terms which might be described as ordinary words of English. It is more helpful in the present context to identify the general characteristics of visitors and travellers. It seems to us that a visitor in the context of Note (10) is generally someone who is visiting an area for a particular reason and whose stay at the premises does not have sufficient degree of permanence to mark that person out as a resident. There are many reasons why someone might be a visitor, including work, study, leisure, or family reasons. On any view, it would not include someone who treats the premises as their home for the time being. It may be difficult in any particular case to draw a line between a visitor and someone whose intended stay has such a degree of permanence that they are not a visitor. The purpose for which an individual is staying may say something about the degree of permanence of the stay. It appears to us that the distinction is between a visitor and a resident, taking into account that an individual may intend to be resident for a relatively short period of time.
>
> A further point that arises is whether a visitor must intend to return home after the visit. Someone may be visiting having given up their home. They may be in search of a new home. In most cases, visitors will intend to return home or to establish a new home elsewhere following their visit. If not immediately, that same person might be regarded as a traveller and it may be that to some extent there is an overlap between those two types of occupiers."

73. At [151], dealing with travellers, the Tribunal said that "an individual might be a traveller for work, for leisure or for other reasons. Their stay at the premises will be intended as one stay amongst a number of stays in different places."

74. Turning to the question whether the premises were a similar establishment to a hotel, the Tribunal noted (at [161]) the comments of the Advocate General in *Blasi* that the provision of meals and drinks, cleaning of rooms and provision of bed linen were among the characteristic features of many establishments in the hotel sector. The Tribunal concluded that such services might also indicate that an establishment was suitable for use by visitors and travellers.

75. At [166] the Tribunal observed that it found it "notable that the PVD excludes from exemption the provision of accommodation in the hotel sector "or sectors with a similar function". This indicates that it is necessary to consider the function of hotels, which is generally to provide short term accommodation for visitors, travellers, and others who might require short term accommodation with associated services."

76. Their conclusion on these linked points was that BLS1 would satisfy the terms of the exclusion in paragraph (d):

> "186. There is grey area between what might be described as the hotel sector and the residential property sector. Serviced residential Apartments fall within that grey area. It seems to us that such premises may bear more similarities with either the hotel sector or the residential property sector depending on the particular facts.
>
> 187. It is difficult to say which side of the line The Quarters falls. It is a very marginal case. On balance, taking into account all the evidence, we are

> satisfied that The Quarters is likely to be used by some visitors and is held out for use by visitors. Whilst there is little evidence of who uses The Quarters, we infer from the way it is marketed and the nature of the rooms and facilities on offer that some visitors to London will use The Quarters as a base for their visit, as well as people who would be regarded as resident at The Quarters. We are also satisfied that The Quarters is held out for use by visitors, as well as residents. The evidence of holding out is essentially the marketing material, including the appellant's website and social media presence. Considering that evidence in the context of our findings of fact as a whole, we are satisfied that The Quarters is held out as being suitable for visitors."

77. Relevant factors here included:

(1) Most occupiers stayed more than 6 months. Some stayed less (as little as one month). Some licence agreements were for less than 6 months. Most occupiers did extend their licences so that their stay was more than 6 months. The Tribunal did not consider that the period of initial licence agreements itself indicated that The Quarters was used by visitors or travellers. It was, however, a factor to be taken into account in considering the evidence as a whole.

(2) The Quarters was marketed as providing both short term and long term "living experiences" and reflected an establishment that was similar to a residential block rather than a hotel. However, it included reference to short term lets, and in some of the material short term is defined as 1-3 months and long term as 3-12 months. Where premises are described as being available for a short term stay of 1-3 months, the Tribunal felt that was a factor which would make them suitable for at least some visitors and travellers. There were also references in the material to "guests" rather than residents, which suggested that The Quarters was suitable for visitors or travellers

(3) Overall, the nature of the agreements entered into by occupiers, the checking-in process and the taking of deposits indicated more permanent rental accommodation rather than a hotel.

(4) The studios themselves and the restriction on overnight guests suggested accommodation which had more in common with the hotel sector than the residential sector. Visitors would be less likely to be put off by such restrictions than people intending to make The Quarters their home.

(5) The Quarters had a restaurant on site, which was also open to the public. That is a common feature of many hotels and would be useful for visitors and travellers as well as residents.

(6) Cleaning and housekeeping services were provided and a private gym was available at an additional cost. There was a 24/7 reception desk and onsite maintenance. These are common features in both hotels and some serviced apartment blocks. Occupiers were charged separately for electricity which would be very unusual in the hotel sector

(7) The Quarters was treated as a block of individual dwellings for rating, council tax and insurance purposes. The fact occupiers were charged council tax suggested that they were not properly described as visitors. However, from the perspective of an occupier, council tax was included in the licence fee and they had no direct involvement with Camden Council. So, this was not determinative of whether The

Quarters was held out as suitable for visitors or travellers, or that it was not generally a similar establishment to a hotel.

78. Drawing these cases together:

(1) Supplies will not fall within the land exemption unless the 'essential object' of the transactions is 'the making available, in a passive manner, of premises or parts of buildings in exchange for a payment linked to the passage of time', rather than 'the provision of a service capable of being categorised in a different way'. There are two requirements here. First, to fall within the exemption, a level of exclusivity of occupation is required. Secondly, a supply of accommodation in a hotel or similar establishment coupled with additional services might be such that the overall provision is probably to be characterised as 'a more complicated service' than just a land supply. In such a case it will fall outside the exemption; *Fortyseven Park Street* and *BSLI*..

(2) Even if supplies have as their 'essential object' the making available of premises 'in a passive manner', they will be taken outside the exemption if they amount to 'the provision in an hotel … or similar establishment of sleeping accommodation'. The test of "similarity" is a broad one, as its purpose is to ensure that the provision of temporary accommodation like, and so in potential competition with, that provided in the hotel sector is subject to tax. Here there is an important distinction between long-term lettings of residential accommodation and short-term lettings of accommodation as in the hotel sector. The provision of meals and drinks, cleaning of rooms and provision of bed linen are among the characteristic features of many establishments in the hotel sector; *YMCA/Blasi*/*BLS1*.

(3) Premises will be taken to be an establishment similar to a hotel if they constitute premises in which furnished sleeping accommodation is provided and which (premises) are used by or held out as being suitable for use by visitors or travellers, even if they are also used by others (who are not visitors or travellers). A visitor is someone who is visiting an area for a particular reason and whose stay does not have sufficient degree of permanence to mark that person out as a resident. A traveller is an individual (who might be travelling for any reason) whose stay at the premises is intended as one stay amongst several stays in different places. *BLS1/ International Student House.*

79. There is clearly a not insignificant degree of overlap between some of these concepts. In particular, the provision of accommodation in a hotel would seem both to be capable of falling outside the land exemption on general principles and, if it fell within it, to be excluded by paragraph (d). Similarly, as we can see from the way the discussion in *BLS1* developed, the fact that hotels tend to be used for temporary accommodation by visitors and travellers (and indeed it is the provision of temporary accommodation which marks out a "similar" establishment) creates a significant overlap between Note 9 and the exclusion in paragraph(d) read on its own.

80. The position of hotels in the context of Item 1 is not the subject of any direct authority as far as we are aware. In *CCE v Sinclair Collis Limited*, [2001] UKHL 30, Lord Scott did make a reference to hotels, commenting as follows:

> "71. The exclusions from the article 13B(b) exemption show a clear and unequivocal intention on the part of the Council that transactions falling within an excluded category should fall outside the VAT exemption. But the exclusions cannot reasonably be supposed to indicate the opinion of the Council that every transaction falling within an exclusion would, had it not

> been for the exclusion, have fallen within the exemption. The exclusions certainly do show that transactions of the sort described are capable of falling within the exemption, and that it is the intention of the Council that they should not do so. So it is not necessary to ask whether a contract under which a person who takes a bedroom in a hotel is a contract of "letting of immovable property". It might or might not be. The answer would depend on the facts. A contract under which a room were taken for a week might well constitute a letting. A contract under which a room were taken for half an hour so that a man might consort with a lady would, I suggest, be very unlikely to be held to do so… In my opinion, the categories of exclusion in article 13B(b) and, for the same reasons, the categories of exclusion in paragraph 1 of Part II of Schedule 9 to the 1994 Act, do no more than indicate types of transaction capable of constituting a "letting" for the purposes of the Directive or of a "licence to occupy" for the purposes of the 1994 Act. Whether, in any particular case, the transaction would, had it not fallen within one of the excluded categories, have fallen within the exemption would have depended on the facts of the particular case."

81. In *BLS1* the Tribunal approached the question of exemption on the basis that supplies in the context of a hotel are capable of falling within the exemption in principle, albeit that they would then be excluded by paragraph (d). The practical relevance of this is that it would seem to be the case that only a supply which falls within the land exemption in principle but is excluded by paragraph (d) can benefit from paragraph 9 of Schedule 6 to VATA (which limits the amount on which VAT is chargeable after 28 days, but still allows full recovery of input tax). This is certainly what the Isle of Man Tribunal decided in *BLS1*. We are not sure that we would agree with them, but, fortunately, that is not an issue we need to address.

Paragraph 9 of Schedule 6 to VATA

82. Schedule 6 VATA contains special rules for calculating the value of supplies, which is the amount on which VAT is charged. Paragraph 9 of Schedule 6 provides as follows:

> "(1) This paragraph applies where a supply of services consists in the provision of accommodation falling within paragraph (d) of Item 1 of Group 1 in Schedule 9 and—
>
> (a) that provision is made to an individual for a period exceeding 4 weeks; and
>
> (b) throughout that period the accommodation is provided for the use of the individual either alone or together with one or more other persons who occupy the accommodation with him otherwise than at their own expense (whether incurred directly or indirectly).
>
> (2) Where this paragraph applies—
>
> (a) the value of so much of the supply as is in excess of 4 weeks shall be taken to be reduced to such part thereof as is attributable to facilities other than the right to occupy the accommodation; and
>
> (b) that part shall be taken to be not less than 20 per cent."

83. The rule in paragraph 9 is a derogation from the general rule that VAT is charged on the full amount of the consideration for a supply. As such, the UK required authorisation from the EC Commission to operate such a provision. Article 27 of the Sixth Directive provided a mechanism for approving derogations. In 1977 HM Customs and Excise wrote to the EC Commission listing the UK's special measures for derogation under Article 27 of the Sixth Directive and included the following:

> "(3) In order to reduce disparity of treatment between people who live residentially in hotels, etc., for long periods and those who occupy normal domestic accommodation, the 1972 Act also provides (in Sch. 3, para. 7 [now VATA 1994, Sch. 6, para. 9]) that where a stay in a hotel lasts more than four weeks, the value of the supply of accommodation and facilities, but not of meals and extras, is reduced for value added tax purposes for the period in excess of four weeks by excluding the value of the right to occupy the accommodation. The reduced value must not be less than 20% of the amount payable for the accommodation and facilities; if in particular cases the amount payable for facilities is higher than 20%, then tax is chargeable on that higher percentage.
>
> (4) This arrangement has enabled the United Kingdom to avoid the considerable legislative complications which would have arisen if it had been necessary to define the various types of accommodation for value added tax purposes. It has also avoided the necessity to treat as partly exempt traders those hoteliers who provide both short and long-term accommodation; and at the same time, it has reduced economic distortion and incentives to tax evasion. It is considered that the amount of input tax which would have been borne by the hotelier if exemption had applied is negligible.
>
> (5) All hoteliers using the provision are required to enter on their value added tax returns the full value of their supplies, irrespective of the status of the resident. Accordingly, the arrangements will have no effect on their own resources calculation.
>
> (6) The arrangements have proved simple to operate for both officials and traders alike, at virtually nil cost to the Revenue. It is the view of the United Kingdom that they conform with the requirements of para. 1 of art. 27 of the directive and may therefore continue to apply after 1 January 1978."

84. On 19 December 1986 the European Council authorised a modification of this derogation. The purpose of the UK measure continued to be "simplifying calculation of VAT in respect of long stays in hotels by assessing on a flat-rate basis the part of the service deemed to correspond to a letting of immovable property exempt under Article 13(B)(b)(1)". The change was that, going forward, the measure would only apply to hotel services provided to individuals themselves occupying the accommodation in question.

85. We do not have all the communications between the UK and EU authorities before us, but the materials we have seen make it very clear that, where paragraph 9 operates, there continues to be a single, taxable supply but (and this is the derogation) the amount on which VAT is charged is reduced from the full amount to the higher of the proportion of the total consideration "attributable to facilities other than the right to occupy the accommodation" or 20% of the total consideration. The UK rules (and the derogation) emphatically do not provide for any exemption of any supplies and paragraph (4) of the text at [83] above explains why (to avoid the complexities of partial exemption).

86. In *BLS1* the Isle of Man Tribunal considered (at [196]) that,

> "Schedule 7 [the IoM equivalent of paragraph 9, Schedule 6 VATA] has the intended effect of exempting a supply of the right to occupy a hotel room for stays of more than 28 days. It achieves that by providing that such a supply is to be valued by reference to the amount attributable to the facilities other than the right to occupy the accommodation".

For the reasons just explained, we would not agree with this observation, which is what seems to have influenced their conclusion that the IoM equivalent of paragraph 9 only operates

where a supply would be exempt in principle but is excluded from the exemption by paragraph (d).

Realreed's Submissions

87. Mr Beal places great store by the UK's derogation allowing what is now paragraph 9. He says that the intention of this was to allow a simplification measure, the effect of which is that the portion of long stays in hotels that is equated with the right to occupy the accommodation is deemed to be exempt. He says that this is very significant. As all the facilities and services are supplied by CCSL, not by Realreed, HMRC must necessarily recognise that stays in excess of 28 days should be deemed to be exempt supplies. Otherwise, he says, the derogation is not being correctly applied and the true nature of the exempt supply not recognised by national law.

88. HMRC have drawn a distinction in their assessment between supplies of Apartments made under AST terms or for more than six months on the one hand and those made on GRF terms for less than six months on the other. Mr Beal says that there is no logical reason for dividing the supplies made by Realreed up in this way. Given HMRC's acceptance that supplies on AST terms or for more than six months are exempt, the only logical conclusion must be that other supplies (leases on GRF terms for shorter periods) are exempt too.

89. As far as the basic exemption is concerned, Article 135(2) of the PVD provides an exclusion from exemption for the provision of accommodation in the "hotel sector or in sectors with a similar function" including holiday camps and campsites. He says that Realreed's property is clearly not a holiday camp or a campsite, nor does anyone suggest that it is a hotel. The only question is whether it is in a sector with a similar function as defined by UK law. He says that the questions of similar function and the interpretation of Note 9 cannot be approached too broadly. Otherwise, we would run the risk of running counter to the scope of the exemption and the limit of the exclusion. Most importantly he takes from Article 135(2) specifically including campsites and holiday camps the idea that, to have a similar function to a hotel, an establishment must operate in the holiday/leisure space.

90. In *Blasi* the CJEU considered letting arrangements treated as short term under German law, because German law set a specific time limit of six months. The CJEU held that exemptions were to be construed strictly and exclusions from exemptions were not to be. It was made clear, however, that the intention of the exclusion was to tax sectors in competition with the hotel sector, although Member States have some margin of discretion when distinguishing between letting of immovable property and provision of accommodation in hotel or similar sectors. The CJEU accepted the one possible basis for doing so was the duration of the stay, provided the approach was reasonable.

91. In *Temco* the CJEU held that the Sixth Directive contained autonomous provisions of EU law that were not dependent on terms of national law. The essence of the exemption was for the passive letting of property linked to the passage of time, rather than an activity of an industrial or commercial nature. Thus, the actual period of letting was not a decisive factor. Importantly, for us, the CJEU confirmed that it was not necessary for the duration of a stay to be fixed at the start of the contract.

92. In *International Student House*, the Tribunal equated the requirement of "similar" supply (to a hotel) with the provision of holiday accommodation.

93. In *Fortyseven Park Street*, the Court of Appeal concluded the taxpayer supplied a composite service and not simply a licence to occupy. Here, HMRC accept there is a letting of property but then contend that the terms of paragraph (d) is engaged. Their argument is different to that in *Fortyseven Park Street*. Mr Beal noted that the Court of Appeal did not

appear to have had the benefit of argument on the derogation in paragraph 9 when it reached its conclusion on paragraph (d).

94. One very important point for us is the answer to the question who supplies what to whom. Mr Beal says that the contractual analysis is clear. Chelsea Cloisters as a business (conceived of broadly) commits to provide serviced accommodation, but this is achieved by two distinct supplies from two different legal entities. CCSL supplies services directly to occupiers and Realreed lets the Apartments. All the evidence before the Tribunal points one way. Once this is accepted, then the two different supplies (by CCSL and Realreed) cannot be amalgamated to produce a composite whole; see *Telewest*. The importance of that for us is that the supplies made by CCSL must be ignored when determining the nature of the supplies made by Realreed. If we look only at the supplies made by Realreed (of accommodation alone), the element of service which is normally to be found in a hotel, is lacking and that determines the point of similarity against HMRC.

95. In *BLS1* the Tribunal defines similarity as "a supply of temporary accommodation, with an element of service, which is in competition or potential competition with the hotel sector". In addition, that definition must be interpreted with regard to the EU legal context, and thus a key aspect of "similarity" with a hotel is use predominantly for leisure or holidaymaking. Such use will not confer exclusive occupation on the occupant and the duration of a typical stay will be transient or temporary rather than approaching any degree of permanence.

96. So far as concerns the question of who a visitor or traveller is for the purposes of Note 9, Mr Beal says that Note 9 must be construed in the light of EU law. The concept of a visitor or traveller must therefore be construed as a visitor or traveller to a hotel or seeking accommodation in a similar sector. Such a visitor will typically be seeking leisure or holiday facilities, with a high degree of integrated services for a transient period. In contrast, someone who occupies residential accommodation, even if "visiting" the UK or someone who is required to "travel" to the accommodation to benefit from it is not a "visitor or traveller" for these purposes. Such a construction would go well beyond the scope of the exclusion from the exemption found in Article 135(2) of the PVD as construed by the CJEU. The point about why the UK has chosen to treat stays in excess of 28 days in a hotel as residential accommodation falling within the scope of the exemption is relevant here.

97. Dealing with how the business operates in practice, Chelsea Cloisters is held out as being serviced accommodation primarily for business professionals on relocation. Realreed has longstanding relationships with certain companies, some of which will book space for their staff direct. Others will find their own accommodation and in recent years Realreed has been using a variety of external websites and booking agencies, including websites specialising in serviced apartments as well as Booking.com and similar sites. Even where Chelsea Cloisters is listed on a site which markets hotels, searches for accommodation in Chelsea will generate hits for Chelsea Cloisters but not if hotels are filtered out of the search.

98. The move from AST's to GRFs does not alter the fundamental nature of the business. The offering is the same as it always has been. Dr Moran was clear that the sector in which Chelsea Cloisters operates is not in competition with hotels.

HMRC's Submissions

99. Dealing first with the use of AST terms, Ms McArdle says the supplies under AST's should fall within item 1(d) when they meet the requirements for it. However, typically they will not do so. This is because AST's give tenants a range of statutory rights which one would normally expect to see in a principal place of residence. Hotels and similar establishments do not normally make supplies on such terms given their formality and the statutory rights they confer. As such, HMRC have treated AST's as a proxy for the

distinction between a supply in a hotel or similar establishment on the one hand and an exempt supply of residential accommodation on the other. In many cases, they may also be a proxy for long term accommodation. HMRC's reference to lease/supplier terms in excess of six months is based on an understanding by the officer concerned that there were no supplies in excess of that period (at least at the outset). Nothing should be read into that approach.

100. Dealing with a contractual analysis, HMRC's case is that Realreed is the party with a contractual obligation to supply serviced Apartments. This is because it is Realreed which holds an interest in the land and contracts with the recipients of the supply to provide a single, composite supply of a licence to occupy the apartment and maid, towel and linen changing services. This Ms McArdle says is also the pleaded case of the appellant and in his judicial review witness statement (exhibited to his witness statement in these proceedings) Mr Reilly says that "Realreed is contractually obliged to provide serviced accommodation to its tenants".

101. As such, Ms McArdle says that there is no need to depart from the contractual terms given that there is no suggestion that those arrangements constitute a sham. Realreed's focus on the cashflow between the parties is beside the point. None of the documents we have seen suggest that two supplies are being made and Mr Beale is simply trying to rewrite the contractual arrangements.

102. As far as the reduced value rule is concerned, HMRC's position is that this has the effect of reducing the value of a supply of accommodation. The legislature provided (and consciously intended to provide) a rule focussing on valuation where supplies are made to individuals. The reduced value rule does not reduce the rate of taxation, which remains the standard rate, there are serious errors in Realreed's approach to the derogation the permitted derogation imposes a minimum 20% on the value of supply which is to be taxable. Any interpretation which permits a lower than 20% reduction in value is impermissible the purpose of the UK legislation was to reduce the taxable value to no less than 20%. It cannot be interpreted as having any other purpose. Ms McArdle accepts that this means that, if Realreed supplies services separately to and in parallel to CCSL, there is a minimum 20% value and we cannot go behind that. Mr Beale says that we should interpret the derogation in the light of its purpose, but the purpose we need to consider is the purpose of the UK legislature to the extent of the 20% and it was never the UK's purpose to allow a supply to be treated as being made with a value of zero.

103. So far as the definition of visitor or traveller is concerned, Ms McArdle points to *Acorn* and *BLS1*. A visitor is someone who is visiting an area for a particular reason and whose stay does not have a sufficient degree of permanence to mark them out as a resident. In *City YMCA* paragraph (d) was engaged where the length of stay of a resident varied from a week to two years with about 30% of the lets being less than six months. In *Namecourt Ltd v CCE*, (1983) LON/83/253 (discussed in *Acorn*) the Tribunal said that "it seems to us that this exception to item 1 is really directed to the sort of establishment which provides accommodation for a transient or floating, though not necessarily short stay, class of resident. It may be long-term or may be short-term, but it is accommodation which you go to with a view to moving on from in due course".

104. As far as similarity to a hotel is concerned, Ms McArdle noted that in *Blasi* the Advocate General said that the words "sectors with a similar function" should be given a broad construction, as their purpose is to ensure that the provision of temporary accommodation similar to, and hence in potential competition with, that provided in the hotel sector is subject to tax. He said that he it was appropriate to approach that distinction by

looking at the duration of a stay, since in general a stay in a hotel tends to be rather short and that in a rented flat fairly long.

Discussion

Who supplies what to whom?

105. We should deal first with the answer to the question who supplies what to whom. In the ordinary course, the starting point for any such analysis would be the relevant contracts in place between the parties involved (here, Realreed, CCSL and occupiers). However, as will already be clear, there are no documents in existence between Realreed and CCSL which set out the arrangements between them We have evidence of a course of dealing, reflected in the accounting entries for the transactions between them and the historic explanation for this in Mr Cutting's witness statement. Similarly, there is no evidence (apart from the reference to Realreed agreeing to provide services in the standard AST agreement we looked at) to indicate whether only one of the two companies, Realreed and CCSL, contracts with occupiers or whether both do or whether one contracts but partly as principal on its own account and partly as an undisclosed agent for the other.

106. CCSL invoices both supplies (occupation and services), but Realreed asserts that one of those invoices (for the occupation rights) is issued on its behalf. Given that Realreed (and not CCSL) has a land interest in Chelsea Cloisters, it is hard to see how CCSL could supply accommodation in the Apartments without some kind of agreement with Realreed entitling it to do so, and no evidence of any such agreement was produced to us. There is no evidence in anything we have seen to suggest that CCSL (which has no interest in the land) supplies occupation rights to anyone.

107. If we accept that Realreed supplies the rights to occupy the Apartments, there must nevertheless be some contractual arrangement with occupiers in relation to the ancillary services; they have been promised that certain services will be provided. It must be the case that either Realreed contracts with occupiers to provide the Apartments and to procure the provision of services (by it or someone else) or (which we consider to be a rather unrealistic analysis) Realreed and CCSL enter parallel promises with occupiers to provide accommodation (Realreed) and the ancillary services (CCSL).

108. It seems us to that the analysis which is most consistent with the fact that Realreed (and not CCSL) has a land interest in Chelsea Cloisters, and so is in a position to grant occupation rights, with Mr Cuttings' historical account and with the relationship between the parties so far (which is not very far at all) as it has been articulated or operated in practice, is that:

(1) Realreed supplies accommodation in the Apartments to occupiers;

(2) there is a promise or representation (based on the way the Apartments are marketed and consistent with the clear undertaking where ASTs are used) by Realreed that the ancillary services will be provided;

(3) CCSL provides those services and that is how Realreed discharges its promise to occupiers.

109. This, to our mind, is a straightforward analysis of the arrangements which is consistent with such evidence as there is (which is admittedly not very much) and the intention of the parties. In this context, we note that the expressed intention of the parties was taken to be relevant by Sir Christopher Staughton in *Telewest* (at [34]) when he was analysing the effect of arrangements which were not "crystal clear".

Does it matter?

110. Mr Beal's argument, given that CCSL is the company which provides all the ancillary services to occupiers, is that the services it supplies cannot be taken into account in determining the VAT liability of the services supplied by Realreed. In making this argument, he relies on the decision of the Court of Appeal in *Telewest* (discussed above). In that case, the Court of Appeal held that, where separate supplies are made by different suppliers (the provision of cable TV and the sale of TV guide), it is not possible to treat those supplies as being made by a single person and then, having done that, decide that one is ancillary to the other and determine their VAT liability on that composite basis. On that basis, the sale of the TV guide remained zero rated, because it was supplied by a separate company, when it would have been treated as ancillary to the provision of cable TV services (and therefore standard rated) had the TV services and the guide both been supplied by the same company. This was so even though it was not possible to but the cable TV services without also purchasing the TV guide.

111. The question we are addressing is, however, quite different from the question considered in *Telewest*. The question we are considering is whether Chelsea Cloisters is a "similar establishment" to a hotel. The focus of this question is on a place, not a person or an activity. To answer this question, we need to consider what is "on offer" at Chelsea Cloisters and then ask whether, in the light of that, Chelsea Cloisters is a "similar establishment" to a hotel. The answer to this question does not in any way turn on whether the person providing the sleeping accommodation (Realreed) is also providing the other services which (assuming this is the case) are needed to make Chelsea Cloisters into a hotel or similar establishment.

112. We accept entirely that Realreed is letting the Apartments and that this is all it is doing, but we do not accept that services supplied by a different person (CCSL) are to be left out of account, when deciding whether the place where Realreed makes those supplies is a similar establishment to a hotel, just because they are made by another person.

113. Assuming for the moment that some additional services (beyond Realreed's letting of Apartments) are required to be provided before Chelsea Cloisters can be a "similar establishment" to a hotel, we would accept that there must be a sufficient degree of permanence, scale and stability in the provision of those services before they can affect the description of Chelsea Cloisters. The same would be true if Realreed alone offered accommodation and services. Here the ancillary services have been provided by CCSL since a time before Chelsea Cloisters was acquired by the Chesterlodge Group, they are an integral feature of all lettings and the arrangements (between Realreed and CCSL) for the provision of those services are such that Realreed feels able to commit to occupiers that those services will be provided. Although delivered by CCSL, those services are a part of the "offering" at Chelsea Cloisters and, on our analysis of the contractual arrangements, something Realreed commits to. In our judgment, these factors demonstrate the required degree of permanence, scale and stability for us to take the services provided by CCSL into account in deciding whether Chelsea Cloisters is an establishment similar to a hotel.

114. Nothing in this conclusion runs counter to the decisions in *Telewest* or *Lower Mill*, both of which are (of course) binding on us. We have not run together the supplies made by CCSL and Realreed to decide what Realreed is doing or how to characterise its supplies for VAT purposes. We are proceeding on the basis that all Realreed does is let the Apartments and then, when it comes to deciding whether the place where it makes those supplies meets a particular description, not discounting the supplies made by another person just because they are made by someone else.

ASTs and lettings for more than 6 months

115. The next question we need to address is whether it makes any difference if the Apartments are made available on AST's rather than GRF terms and whether supplies where the initial term is six months or more should be treated automatically as not being within paragraph (d). As we have seen, HMRC have treated the provision of Apartments on AST's as falling outside paragraph (d). Similarly, in correspondence with Realreed, they indicated that lettings for more than six months (which we take to mean lettings for an initial term of more than six months) would also be treated as fully exempt from the outset.

116. As we have just discussed, the question the law asks is whether sleeping accommodation is being provided in an establishment which is similar to a hotel (and, where Note 9 is in point, asking the additional question whether the premises are used or held out as being suitable for use by visitors or travellers). The only question the law is posing is answered by looking at the premises in which the sleeping accommodation is provided, and the question whether Chelsea Cloisters is a similar establishment to a hotel is to be answered by looking at the premises as a whole.

117. If the answer to that question is that Chelsea Cloisters is an establishment similar to a hotel, the terms (AST or GRF) on which sleeping accommodation is provided do not make any difference when it comes to deciding whether the supply is excluded from the exemption by paragraph (d). As we saw in *Temco*, the CJEU has made it clear that the concepts used in the relevant provisions in the Directive are autonomous EU concepts, and the question whether a supply is in principle an exempt grant of a land interest is determined by asking whether the tenant has the required degree of exclusive occupation, not by focusing on the form of the land interest created by domestic law. The UK legislation makes it perfectly clear that both leases and licences to occupy are sufficient for this purpose. As we have seen, ASTs granted by Realreed tend to have break clauses in them and there was no suggestion before us that there is any real qualitative difference between the occupation of Apartments on ASTs or GRFs granted for the same period of time. Indeed, the general "direction of travel" since 2001 has been to replace ASTs with GRFs. Realreed may encounter some procedural difficulty in enforcing its rights with an AST rather than a GRF, but it was never suggested that this made any real difference to the analysis of what Realreed was supplying. We agree with Mr Beal that the choice between ASTs and GRFs is largely one of form and that distinction on its own is not a rational basis for deciding whether a letting falls within paragraph (d) or not; what matters is what Realreed supplies, not the precise legal analysis of the means by which it achieves that.

118. The question of the length of the arrangements is more difficult. In principle, one might expect the answer to be the same. If Chelsea Cloisters is an establishment similar to a hotel, then the provision of sleeping accommodation for <u>any</u> period would fall within the natural reading of paragraph (d). However, we know from *Blasi* that the purpose of this provision is to treat supplies made by establishments which are potentially in competition with a hotel in the same way as supplies by hotels. On that basis, if Realreed were to transact with an occupier on terms which are so far outside the spectrum of terms that might be expected to be found in a hotel that any element of <u>potential</u> competition is simply not present, then an interpretation of paragraph (d) should be found which conforms with the underlying purpose of the exclusion and preserves exemption for that supply. A route to this may be found in the interpretation of "sleeping accommodation" (which is the term the Directive leaves it to Member States to define), which we consider should be interpreted so as to exclude from paragraph (d) accommodation provided in an establishment similar to a hotel but which is provided on terms which would not be expected to be found in a hotel (so that there is no possibility of the establishment being in competition with any part of the hotel sector when it comes to that provision). Given the lengths of occupation periods which the

cases have accepted as being in potential competition with the hotel sector, we would expect this to include only accommodation with an ineluctable fixed initial term (so, with no break rights for either party) of at least six (possibly more) months. Ms McArdle says that there were no leases with an initial period of six months or more and so this point is academic, and on that basis it would not be appropriate to explore the point in abstract any further.

119. When considering the length of the letting, we should keep in mind that paragraph 9 will provide a very significant level of relief against the consequences of treating long leases of accommodation in hotels and similar establishments as standard rated; it will reduce the amount on which VAT is chargeable after 28 days to the amount (subject to a floor of 20%) which reflects the value of the ancillary (non-accommodation) services provided and yet fully preserve the supplier's ability to recover input tax.

120. To conclude on this point, if Chelsea Cloisters is an establishment similar to a hotel, the letting of Apartments should be treated in the same way, whether they are let on AST or GRF terms. A very long lease (whether on AST or GRF terms) of an Apartment might fall outside the definition of "sleeping accommodation" (read in the light of the purpose behind the EU provisions), but we understand that no Apartments were let for terms which make this point of practical relevance.

Is Chelsea Cloisters an establishment similar to a hotel?

121. No one has suggested that Chelsea Cloisters is a hotel, nor has there been any serious suggestion before us that the nature of the rights granted to occupiers do not confer the required degree of exclusivity needed for the land exemption to apply. Nor has anyone suggested that the land exemption does not apply because the complexity of the supplies made by Realreed means that the essential object of its supplies was not the provision of premises or parts of buildings in a passive manner, but rather the provision of a service capable of being characterised in a different way. If that were to be suggested, the fact that Realreed does no more than let the Apartments may be relevant. When looking at the supplies it makes, it is not possible to conclude that it is doing anything other than making premises available in a passive manner. The supplies that CCSL makes are not to be discounted in deciding whether Chelsea Cloisters is an establishment similar to a hotel, but Realreed cannot be treated as making CCSL's supplies for the purposes of deciding how to characterise what Realreed supplies. That much is abundantly clear from *Telewest* and *Lower Mill*.

122. Turning to the cases where the question of similarity has been discussed, we should start with the CJEU decision in *Blasi*. What we take from that case is that the question of similarity should be given a broad construction, as its purpose is to ensure that the provision of temporary accommodation, which the Advocate General considered to be similar to and hence in potential competition with that provided in the hotel sector, is subject to tax. German law, as interpreted by the German courts, used the length of the letting as the means of distinguishing between the two types of supply and the Court agreed that one of the important distinguishing features between accommodation in the hotel sector and the letting of dwelling accommodation is its duration. Given the margin of discretion the Directive gives to Member States to determine similarity, a rule which treated lettings for less than six months as taxable was not precluded. It is important not to place too much emphasis on the six-month letting period, because the discussion in *Blasi* was driven by the terms of the German law under consideration. However, we consider that we can fairly take from this case that the Court did not regard a six-month period as an unreasonable dividing line when it comes to deciding whether a letting is short or long-term. If it thought that, it would have said so given the terms of the German rules. We should also note the Advocate General's

comments that a person offering short-term lets fulfils essentially the same function as, and so is potentially in competition with, the hotel sector even where all of the additional supplies commonly seen in a hotel are not included. The essential distinction between hotel and similar lettings on the one hand and exempt lettings of residential property on the other is the temporary nature of the accommodation. That is likely to involve additional services, but the provision of those services was by no means an absolute requirement. In that case there was some element of service provision, but what level (if any) is required was not discussed.

123. In paragraph 19 of his opinion, the Advocate General referred to a person providing short-term holiday lets as someone who performs a function similar to that of a hotel. In his submissions, Mr Beal invited us to conclude that, given that the Directive refers to holiday sites, we should interpret the concept of a similar establishment to a hotel as one providing holiday or similar accommodation. We do not agree with this submission at all. Hotels accommodate a wide range of people for a wide range of purposes. Clearly, holiday accommodation, at the seaside or in other leisure destinations, is one important segment of the hotel sector. However, people stay in hotels for a wide range of reasons and for varying lengths of time. Mrs Blasi herself was providing accommodation for refugees in Munich; they were self-evidently not on holiday, nor were the young homeless people in *City YMCA*. If the Advocate General or the Court (which regularly reframes the questions posed to it) had considered that only premises providing holiday or leisure accommodation were similar to hotels, then they would have said so. The domestic (in which we include the Isle of Man) cases where premises were found to be similar to hotels, *Acorn Management Services*, *Fortyseven Park Street*, *City YMCA and BLS1*, did not involve (or were not decided on the basis that they involved) the provision of holiday or leisure accommodation. Nevertheless, the establishments were all found to be "similar" to hotels. More generally, we all know that people in business stay in hotels (which may host conferences or be situated near conference centres to encourage business visitors). Baroness Thatcher lived in the Ritz in the final months of her life when she could no longer cope in her home in Chester Square. John Mortimer wrote of a (fictional) barrister who lived in a hotel in Kensington[1]. At the other end of the time horizon we have Lord Scott's example of hotels being used for fleeting liaisons. The range of functions performed by hotels and the range of levels of accommodation and services offered raise issues when it comes to identifying the essential functions of the hotel sector, which is a necessary preliminary to deciding whether an establishment is "similar" to a hotel, and we will come back to this point later (at [132]).

124. Looking at factors which have been regarded as important in other cases, in *International Student House* the Tribunal focused on Note 9 as an aid to a description of the premises. The important distinction the Tribunal drew here was between a person whose presence in a place has a degree of permanence and someone who is temporarily visiting.

125. In *Acorn Management Services*, students staying on average of 15 weeks were considered to be visitors or travellers. They were present for a limited purpose and a relatively short stay. In *Fortyseven Park Street*, the special nature and long-term nature of the fractional interest was not sufficient to result in the premises not being similar to a hotel.

126. Relevant factors in deciding whether the premises in *City YMCA* were similar to a hotel included the distinction between long and short-term lettings. The Tribunal noted that short-term letting invariably involves additional services and greater supervision and management being provided. In that case, temporary accommodation was the essence of what the YMCA did. Residents stayed for periods between a week and two years with 30% of lets being for less than six months. Even though 70% of the lets were for more than six months, the

[1] John Mortimes "The Trials of Rumpole" (Penguin Books, 1979) p16

Tribunal thought that that did not change the short-term nature of the accommodation provided, especially given that no statutory rights were created, and YMCA could evict a resident for 24 hours' notice. Also, looking at matters from a functional perspective, the Tribunal asked, if an individual did not stay here, where else would they stay and thought that it was quite likely that an agency or local authority would accommodate them in a hotel.

127. *BLS1* is important, the Tribunal noted (at [161]) the Advocate General's comments in *Blasi* that the provision of meals and drink, cleaning of rooms and the provision of bedlinen were among the characteristics of features of establishments in the hotel sector. Given that the PVD excludes from exemption accommodation in sectors which are similar to hotels, the Tribunal considered that the function of hotels is generally to provide short-term accommodation with associated services.

128. If we look at the data for Chelsea Cloisters in the light of these observations, we see that nearly 2/3rds of stays in the period October 2007 to December 2008 were for 28 days or more and that figure decreased to 49.8% in 2014/15 and 38.5% in 2018/19. Whilst between one third and half of all stays were for more than 28 days, between a half and two-thirds were not. The average number of nights per stay was 16.66 in 2010/11, 15.39 in 2011/12, 10.92 in 2012/13, 9.25 in 2013/14, 11.55 in 2014/15 and 11.52 in 2015/16.

129. The data would suggest that Chelsea Cloisters is used by people who stay for relatively short periods, much more than was the case in *Blasi* or *YMCA* or *BLS1*. Accordingly, we see that core hallmark of a similar establishment (the provision of relatively short-term accommodation). We also see the provision in the premises of ancillary services. There is a daily maid service, linen is changed, and Apartments are cleaned at the end of a stay.

130. Although individual Apartments are treated separately for council tax purposes and utilities are metered separately, occupiers are presented with a single daily rate. They are not asked to pay council tax separately or for the utilities they consume. Although much was made of the possibility of occupiers having overnight visitors, we can see from the AST terms that there were limits on this; the terms seek to cap the number of people who can reside.

131. Whilst no catering services are supplied, there are restaurants on site. They serve local residents, but they are clearly available for occupiers and the earlier marketing materials draw attention to their availability. They are operated by third parties, but that was the case with the restaurants in *BLS1*. There are differences between Chelsea Cloisters and a typical hotel, of course, for example virtually no breakfast facilities are provided. Breakfast boxes have been available at least at intervals in the period in question, but the take-up has been very small. Where provisions such as soap and toilet rolls run out, occupiers need to buy replacements themselves.

132. In our judgment, even without taking Note 9 into account, Realreed is providing sleeping accommodation in an establishment which is similar to a hotel. The two hallmarks of short-term accommodation coupled with additional services (daily maid service, linen changing, cleaning at the end of a stay, residents bar, concierge – all provided by CCSL) mean that Chelsea Cloisters is an establishment in potential competition with the hotel sector, which also offers short-term accommodation with services. We have already identified (at [123]) the range of functions hotels perform and the different levels of accommodation and services on offer. One establishment is highly unlikely to be in competition with every part of the hotel sector, just as every hotel is not in competition with every other hotel. We mean no disrespect to Dr Moran and his colleagues when we say that our impression is that Chelsea Cloisters is probably not in competition with Claridge's. That diversity within the hotel sector may explain why these two hallmarks of hotels have been identified in the cases (with

no discussion of any required level or quality of accommodation or service provision), and why an establishment which to some extent displays these two hallmarks will be regarded as potentially being in competition with at least part of the hotel sector and thus a similar establishment. Chelsea Cloisters displays these two hallmarks and, in consequence, is an establishment similar to a hotel. We do not regard the physical appearance of the property (which, we are told, looks like a residential building), the absence of signage or the fact that a number of apartments (those on long lets) are effectively not owned by Realreed as being important.

133. Dr Moran in his evidence was clear that, in his view, Chelsea Cloisters did not set out to compete with hotels. We have seen how, depending on the filters used (especially if "hotel" is not used) Chelsea Cloisters is not identified in all searches on booking sites. That, however, is not the point. As the Advocate General made clear in *Blasi* (and the Tribunal picked up on in YMCA with its question, where else might those accommodated in the hostel go?) the question is whether there is potential competition between the establishment and the hotel sector, not whether the establishment has set out to lure guests away from hotels. All the cases make it clear that there is potential competition where an establishment offers short-term accommodation with additional services. Put another way, the test of potential competitiveness is an objective one, which requires us to identify the characteristics of an establishment in the hotel sector and then ask whether Chelsea Cloisters displays those characteristics. There is no subjective element. Whether those who operate Chelsea Cloisters actively set out to compete with businesses in the hotel sector is beside the point.

134. In case we are wrong on that point, we turn briefly to consider the impact of Note 9. This provides that premises are taken to be similar to a hotel if in those premises there is provided furnished sleeping accommodation used by or held out as being suitable for use by visitors or travellers. Clearly, Realreed is providing furnished sleeping accommodation, so the only remaining question is whether Chelsea Cloisters is used by or held out as being suitable for use by visitors or travellers.

135. In broad terms, we agree with Ms McArdle's summary of the approach taken in the cases. A visitor is the one who is visiting an area for a particular purpose and whose stay does not have a significant degree of permanence to mark them out as a resident. So far as the Apartments are concerned, we have already discussed the data on the length of stays. Clearly, the average length of visit (less than a fortnight) must mean that the Apartments are being made available to visitors or travellers. Occupiers are staying in Chelsea Cloisters for significantly shorter periods of time than was the case in *YMCA* and *BLS1*. They are clearly people who are staying in Chelsea Cloisters for limited periods and particular purposes. There is no degree of permanence in the average occupier's stay. Those stays may be longer than the average stays of visitors to London calculated in the GLA Working Paper, but nevertheless there is nothing in the nature of permanence about them.

136. Chelsea Cloisters is advertised on a wide range of booking sites. We accept Dr Moran's evidence that this is the result of changed booking methods generally and not an approach (particularly given the large amount of commission charged) he would choose for himself. Nevertheless, Chelsea Cloisters is marketed on sites used by people looking for short-term accommodation. Even though Chelsea Cloisters might not appear if "hotels" was removed from a search, they would nevertheless appear on a general search of sites such as Booking.com if a user was looking for accommodation in the area. Sites such as Booking.com, Hotels.com or Expedia.co.uk are not generally used by people looking to find a home. They are used by people travelling to or visiting a particular place to find short-term accommodation whilst they are there. It was never suggested to us that the Apartments are

advertised as being available for letting with Central London estate agents or traditional agencies dealing with residential rental properties.

137. In cross-examination, Ms McArdle pointed out to Dr Moran marketing materials prepared by Chelsea Cloisters which referred to the attractions of London "for leisure and business travellers" and concluded by observing that Chelsea Cloisters welcomes "thousands of professional and leisure travellers from around the world" every year. The website draws attention to travel times to airports.

138. Dr Moran's description of Chelsea Cloisters operating like a "home from home" is quite telling. Whilst accommodation in Chelsea Cloisters may have a different ambience to that in some hotels, a "home from home" is not someone's real home; it is where they stay while they are away from their "real" home for a particular or limited period or purpose.

139. Even some years ago, when booking sites were less prevalent and commercial customers bookings were handled centrally, it was still the case that the businesses at which Realreed targeted its offering were sending people to London for defined periods and purposes. There has been no suggestion that occupiers, with possibly one or two exceptions, have ever settled down and made an Apartment their home, certainly not for periods of more than a few months.

140. If we construe Note 9 in the light of the apparent purpose of the Directive (as derived from *Blasi*), we would interpret "visitor or traveller" as referring to a person who is present in a particular place without making it their home, i.e. they are not staying there with any degree of permanence, and who has come to a particular place in circumstances, or for a particular purpose, which means that they need relatively short-term (and therefore to some extent serviced) accommodation. To the extent there is any real difference between a visitor and a traveller, we consider that a visitor is a person who is present in a place impermanently, for a particular limited period or purpose, after which they will return home, and a traveller is a person who is moving between such places (i.e., they will be a visitor in more than one place before returning home). We know that it is the case that people in significant numbers stay in Chelsea Cloisters for periods of less than a fortnight. The only conclusion we can draw from the average length of stays and the way in which Chelsea Cloisters was marketed is that the Apartments were both used by visitors and travellers and held out as being suitable for such use.

Paragraph 9, Schedule 6, VATA

141. Mr Beal pressed very strongly on us his submission that the presence of paragraph 9 indicates that the provision of accommodation in the context of stays of over 28 days should be exempt. Despite the force of his submission, we are just not with him on this point at all. The whole point of paragraph 9 is to preserve standard rating, where (but only to the extent that) a single occupancy runs on beyond 28 days, so as to maximise input tax recovery for the supplier, whilst reducing the amount of VAT charged to the consumer. That, explicitly articulated, objective of the derogation would be thwarted if stays in excess of 28 days, otherwise covered by paragraph 9, were (either completely or to that extent) exempt. We agree absolutely that the UK clearly wanted to introduce (and did introduce) a special regime for stays in hotels and similar establishments which end up lasting for more than 28 days, but that special treatment was never exemption. The UK only obtained, and only sought, a derogation to reduce the taxable amount. The liability of a supply is unaffected. This is the plain and only possible reading of paragraph 9, and it is entirely consistent with the terms of the derogation. We have already accepted that the Isle of Man Tribunal does not seem to be with us on this point.

142. Where the length of a stay may be relevant is where its length (and possibly other terms) mean that the supply is never even potentially in competition with supplies made in the hotel sector. We discuss that point at [118]-[120] above, but that point operates entirely independently from paragraph 9 and, as we indicate, the length of stay contracted for will need to be very substantially longer than 28 days for this consideration to be in point.

143. The second issue which paragraph 9 raises, given our conclusions that the accommodation provided by Realreed falls within the exclusion in paragraph (d), is how paragraph 9 is to be applied to the services Realreed makes. In terms, paragraph 9 provides a measure of relief where a supply of services consists in the provision of accommodation falling within paragraph (d). It provides, where provision is made to the same individual for a period in excess of 4 weeks, that the value of the supply (which falls within paragraph (d)) is reduced to such part thereof as is attributable to facilities other than the accommodation, but subject to a minimum of 20% of the consideration.

144. At the beginning of the hearing, Mr Beal suggested that, if Realreed provides accommodation and CCSL provides ancillary services, the effect of paragraph 9 is to reduce to zero the value of Realreed's supplies (assuming they are not exempt, which is his primary argument). This is because, as it is not supplying anything other than accommodation, no "part" of the consideration it receives is attributable to anything other than accommodation and paragraph 9 only applies where part of the consideration a person receives is attributable to facilities other than accommodation. In broad terms, we should look at CCSL and Realreed providing accommodation and services and accept that CCSL's services being subject to VAT at the standard rate is sufficient to meet the policy objective of paragraph 9. Ms McArdle's point, on the other hand, is that, given the emphasis placed by Mr Beal on the fact that only Realreed is supplying the accommodation and that is all that Realreed is supplying, paragraph 9 operates with the 20% floor to the consideration charged by Realreed.

145. Paragraph 9 was clearly drafted in the expectation that the accommodation and other facilities would all be provided by the same person and that there would be a single supply of accommodation and facilities. Against that background, where it applies, paragraph 9 adjusts the value of "the supply" (the (assumed) single supply within paragraph (d)).

146. It is clear from *Telewest* and *Lower Mill* that there are two separate supplies here, one by Realreed (of accommodation) and another by CCSL (of ancillary services), that those supplies cannot be treated as made by the same person and that the composite supply rule cannot apply to the aggregate of supplies made by different suppliers. It follows from this that only Realreed is making a supply within paragraph (d) and that, for the purposes of paragraph 9, CCSL's supplies should be ignored.

147. Such a conclusion could give rise to an obvious unfairness. Suppose CCSL charged 20 for the services it supplies and Realreed charged 80, on a literal reading of paragraph 9, the total amount of VAT chargeable would be 7.2 (20% x (20 + (20% x 80))). On a purposive approach to paragraph 9, the amount of VAT that ought to be charged might be thought to be 4, being 20% of the higher of the 20 CCSL charges and 20% of the aggregate consideration charged by both companies (100).

148. That would be in line with the purpose of the derogation, as explained in HM Custom & Excise's comments to the Commission in 1977, that VAT should be charged on the higher of the amount payable for the facilities or 20% of the amount payable for the accommodation and facilities taken together. We might get to that result if we read "part" in paragraph 9(2) as only applying if there was a part of the consideration attributable to a supply within paragraph (d) that was attributable to supplies of facilities other than accommodation. If there is no such part, the floor in paragraph 9(2)(b) would consequently not apply.

149. The problem with such an approach, which might be thought to produce a "fair" answer if the consideration charged by a company in the position of CCSL is at least 20% of the consideration charged by the two suppliers taken together, is that it offers no protection if the consideration charged by such a company is less than 20% of the aggregate (or in the unlikely event that there was a single supply by a single supplier within paragraph (d) that contained no element of ancillary services). This is important because the derogation was "sold" to the EC Commission on the basis that the reduced value (on which VAT was charged) would never be less than 20% of the total consideration for the facilities and the accommodation taken together. Our "fair" interpretation would offer no protection in such a case and the UK would be operating an unapproved derogation.

150. This is not an academic point. We were shown three sets of (relatively recent – early 2019) sample invoices issued by CCSL in relation to accommodation (supplied by Realreed) and services (supplied by it). In two cases the services fee was 11.74% of the aggregate and in the third it was 10.94%.

151. In such a situation, to maintain our "fair" answer whilst being consistent with the approved derogation, we would need to read paragraph 9 as reducing the value of Realreed's supplies to the amount necessary to reflect the services supplied by CCSL (which would have no impact on the value of Realreed's taxable services if CCSL were charging a proper price for its services) or the 20% floor (applying to the aggregate consideration for both supplies). In our judgment, the words of paragraph 9, which assume a single composite supply, will not bear such an interpretation. In *Telewest* (at [68]) Arden LJ gave the absence of machinery in the VAT legislation to manage a situation where two supplies are treated as made by the same person as a reason why the two supplies should be analysed separately. Going down this route would not quite be introducing such a mechanism through our interpretation of paragraph 9, but we would be saying that the value of A's supply for VAT purposes depends on the value of B's and we would be departing from the *Telewest/Lower Mill* approach of treating supplies made by separate suppliers completely separately.

152. We do not consider that we should interpret paragraph 9 in a way which creates a risk of the provision operating in breach of the derogation authorising it. On that basis, and given the wording of paragraph 9 and authorities such as *Telewest* and *Lower Mill*, we consider that paragraph 9 should be interpreted, in accordance with its plain wording, as reducing the value of the supplies made by Realreed in respect of the excess period of a stay over 28 days to 20% of the value of such supplies. The VAT this gives rise to is in addition to, and to be calculated without reference to, the value of the (entirely separate) supplies made by CCSL.

153. We do not consider this analysis to operate harshly. It is the inevitable result of the arrangements put in place by CCSL and Realreed and their analysis of those arrangements (which we accepted), and it can, in any event, easily be avoided if CCSL stops supplying services itself and Realreed makes a single composite supply of both accommodation and services, which would be both a straightforward way of operating and one easily accommodated by paragraph 9. We should stress here that no one has suggested that the way CCSL and Realreed have divided up their respective functions at Chelsea Cloisters or approached the pricing split is in any way artificial or deliberately designed to create an abusive VAT advantage. Such considerations form no part of our analysis.

Conclusions on the Liability Appeal

154. Our conclusions on the issues raised by the Liability Appeal are:

> (1) Chelsea Cloisters is an establishment similar to a hotel, both on the ordinary meaning of that term and because Chelsea Cloisters falls within Note 9, as premises

where furnished sleeping accommodation is provided which is used by or held out as being suitable for use by visitors or travellers.

(2) Accordingly, the letting of the Apartments (whether on AST or GRF terms) is excluded from exemption by paragraph (d) of Item 1, Group 1, Schedule 9 VATA.

(3) Where paragraph 9, Schedule 6 VATA applies to the letting of an Apartment by Realreed, it operates to reduce the amount on which VAT is charged (at the standard rate) on that supply to 20% of the value of Realreed's supply, without reference to the value of CCSL's (entirely separate) supplies or any VAT chargeable on CCSL's supplies.

THE PENALTY APPEAL

155. We turn now to the Penalty Appeal. For reasons already explained, nothing in financial terms turns on our decision on the Penalty Appeal, because the penalty was suspended and the period of suspension has passed.

156. The penalty was imposed under paragraph 1 of Schedule 24 to the Finance Act 2007. There are two conditions for such a penalty. First, the document submitted to HMRC (here Realreed's VAT returns) contains an inaccuracy which leads to an understatement of a liability to tax. The second condition is that the inaccuracy was careless within the meaning of paragraph 3. Paragraph 3 provides that a document given to HMRC by a person is "careless" if the inaccuracy is due to failure by that person to take reasonable care.

157. Because of our decision on the Liability Appeal, the first condition is met.

158. Turning to the second condition, it is accepted that the test to be applied is to ask what a reasonable taxpayer, in the position of the taxpayer and exercising reasonable diligence in the completion and submission of the returns, would have done; see the decision of the Upper Tribunal in *Colin Moore v HMRC* [2011] UKUT 239 (TCC).

159. So far as Realreed's position is concerned, the supplies in question formed a very significant part of its business, the absolute amounts of VAT involved (as can be seen from the assessment figures) were substantial and the business was not operated in a straightforward way (the making of the supplies to occupiers of Apartments was split between CCSL and Realreed).

160. Briefly, Realreed's submission is that it acted reasonably and diligently and submitted its VAT returns consistently with what it believed to be the correct treatment, as endorsed by HMRC by their actions during previous inspections. HMRC did not challenge Realreed's treatment during previous visits, nor did it advise Realreed to seek specialist advice on the proper VAT treatment of its supplies. HMRC's dealings with Realreed included issuing a decision making corrections which can only be consistent with HMRC's acceptance of Realreed's approach to the VAT treatment of its supplies. Realreed says that it was reasonable for it to derive substantial comfort from the outcome of HMRC's inspections and it had no reason to think it had done anything wrong.

161. As we have already mentioned, one of Realreed's grounds of appeal was that HMRC's assessments and liability decisions infringed a legitimate expectation on its part. That aspect of its appeal is not before us, because it applied for judicial review of HMRC's decisions and Lavender J dismissed its application. In broad terms, he held that nothing that HMRC had done created a legitimate expectation on which Realreed could rely.

162. The evidence before us in relation to the Penalty Appeal came partly from Dr Moran. His evidence is that he left the detailed VAT affairs of Realreed to others. He was responsible for broader issues of group strategy. That position is entirely understandable, but

it does not help us to decide whether Realreed exercised reasonable care when it came to submitting the relevant VAT returns.

163. Mr Reilly, as finance director of Realreed, was responsible for its tax affairs. Mr Reilly's evidence was that, when he started to work for Realreed, Dr Moran and Mr Cutting explained to him that HMRC had always accepted that Realreed made both exempt and taxable supplies and that this was also evident from the records of previous inspections and other papers in Realreed's VAT files, which he reviewed. He started, therefore, with the benefit of those conversations and Realreed's historic VAT files. In cross-examination, Mr Reilly accepted that he had never looked at the legislation, HMRC guidance, or case law. He had simply relied on the very limited materials and discussions made available when he started at Realreed.

164. We were not shown any evidence about any advice which Realreed received, nor any internal notes or memos which may have been produced recording its analysis of the VAT position. The hearing bundle contained a heavily redacted note of a meeting with Touche Ross in 1991, during which the VAT position of various companies in the Chesterlodge Group was considered. The meeting appeared to proceed on the basis that the supplies made by Realreed were VAT exempt; there is no record in the note of meeting about why that conclusion had been reached or of any analysis.

165. Although HMRC did not challenge Realreed's position (at least until the inspection which gave rise,to this litigation took place), they equally never made a clear statement to Realreed that they agreed with its position. Realreed never asked HMRC for a formal ruling (e.g. through the non-statutory clearance mechanism) on is approach to the VAT treatment of its supplies.

166. There has been some discussion as to whether Realreed's business has evolved over the years. Dr Moran's evidence is that it is substantially the same. Certainly, its business has always been letting the Apartments, but it would seem clear from what we have been told that there clearly have been some changes. According to a fax dated 24 April 1990 (referred to by Lavender J at [32]) to someone in Argentina, who made an enquiry about accommodation, the writer said "our minimum letting period is four weeks and we let to companies only". From Mr Cutting's evidence, occupiers were required to sign ASTs. We now have lettings direct to individuals, occupation terms on average far shorter than 28 days, GRFs used far more than ASTs and direct marketing through booking sites etc.

167. In our judgment, whilst the business of Realreed has not fundamentally changed, there have been enough changes in the way it was carried on that a person taking reasonable care in relation to Realreed's VAT affairs might begin to wonder whether the VAT analysis (even if the assumed position in 1991was correct) had changed. Even a superficial reading of the legislation would make a reasonable, thoughtful person question whether Realreed's business was moving closer to that of a hotel or whether it was providing sleeping accommodation to visitors and travellers. As Ms McArdle said, none of these are particularly difficult or complicated words and, if nothing else, they would have put a reasonable, careful person on enquiry. Mr Beal submits that the questions in the Liability Appeal are difficult (they occupied the tribunal for four days), but that misses the point. The question in the Penalty Appeal is not how difficult the questions in the Liability Appeal are, but how much (if any) effort Realreed put into trying to find the answer. It does not matter if, despite trying, it got to the wrong answer to a difficult question, but it does matter if it put no effort into working out whether there was a question to answer or what the answer might be.

168. Even if the business had stayed exactly the same, the world (and tax law and practice) moves at a fast pace. It is wholly unreasonable to assume, without taking steps to check the

position, that the regime which operated in 1991 would be the same in the period to which the assessments relate.

169. The question whether Realreed has taken reasonable care is not the same as whether Realreed can rely on what it says is HMRC's effective approval of its approach to its VAT affairs. The question is: Did Realreed itself take reasonable care? The short answer to that question is "No". We have reached this conclusion because:

(1) There is no evidence of Realreed ever having taken considered professional advice about its VAT affairs.

(2) Even if there had been a fuller discussion of the VAT position in the meeting with Touche Ross in 1991 than the meeting note suggests, a reasonable person in Realreed's position would have refreshed that advice with Touche Ross (or another adviser) from time to time and there is no evidence that this was done.

(3) Realreed does not, of course, have to incur the costs of seeking external advice if it is happy with its own analysis of the position. There is, however, no evidence of the position having been analysed internally. Indeed, Mr Reilly's evidence is quite the opposite; he has never looked at any source materials to check whether the position as explained to him was correct. He betrayed absolutely no intellectual curiosity about Realreed's VAT affairs at all. He simply accepted what he was told and did nothing to validate his understanding.

(4) It is, of course, also possible to obtain reassurance from HMRC. They operate a non-statutory clearance service, and it may also be possible for a taxpayer, after a dialogue with HMRC, to feel confident that the VAT or other tax analysis they have adopted is correct (or at least is accepted by HMRC). There is, however, no evidence of Realreed having engaged in any discussion of this sort.

(5) To the extent it is relevant, Realreed was not entitled to rely on HMRC's dealings with it as creating a legitimate expectation so far as its VAT affairs were concerned. If it had planned to do so, it should have considered whether that was a justifiable thing to do. There is no evidence of its having taken any advice on this point at all.

Conclusions on the Penalty Appeal

170. For all these reasons, we have concluded that Realreed did not exercise the level of diligence and care in the submission of its VAT returns that a reasonable taxpayer in its position would have taken.

DISPOSITION

171. For the reasons set out above, the Liability Appeal and the Penalty Appeal are dismissed.

172. The VAT to be assessed on Realreed in consequence of the Liability Appeal failing is to be calculated on the basis set out in paragraph [154] above after giving Realreed appropriate credit for any input tax it did not claim in consequence of treating its supplies as exempt. If the parties cannot agree on the amounts, they may refer the issue back to the Tribunal.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

173. 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.

MARK BALDWIN
TRIBUNAL JUDGE

Release date: 15th DECEMBER 2023