VAT AND ALTERATIONS TO LISTED BUILDINGS – THE *ZIELINSKI BAKER* APPEAL

John Walters Q.C.[1]

Zero-rating for VAT is available under Group 6 of Schedule 8 to the VAT Act 1994 for the first grant of a major interest in a substantially reconstructed "protected building" by the person carrying out the substantial reconstruction (item 1). It is also available for the supply of construction services and building materials made in the course of an approved alteration of a "protected building" (items 2 and 3).

The *Zielinsky Baker*[2] appeal, in which the House of Lords gave judgment on 26th February, was about whether an approved alteration of an outbuilding within the curtilage of a dwelling house, which was a listed building, was eligible to be zero-rated. The alteration in question was the conversion of the outbuilding to provide games and changing facilities and the construction of an adjoining indoor swimming pool. This conversion required listed buildings consent (which was duly obtained) because it was an "approved alteration" to the listed building.

The VAT Tribunal's decision[3] was to allow zero-rating of the construction services. This was reversed in the High Court by Etherton J[4]. His decision was, in turn, reversed by the Court of Appeal[5] in a 2:1 majority decision. The House of Lords by four to one have reversed the Court of Appeal's decision and refused zero-rating.

In the course of the appeal process a number of problems with the drafting of Group 6 have been encountered. It has been difficult to ascertain what precisely was (or is) the legislative purpose behind Group 6, in particular, whether Parliament's purpose in providing for the zero-rating is to assist housing or to assist the nation's heritage. And at least one problem area remains, which has not been dealt with by the House of Lords' decision. Practitioners will need further guidance from Customs and Excise on what their policy will be as a result of the decision.

To begin with a bit of history that will be familiar to many readers: from the introduction of VAT in 1973, repairs and maintenance of all buildings have been taxable at the standard rate. The position was different for construction and alterations. These were all zero-rated from 1973 to 1984. This lead to a lot of litigation on the question of whether particular works were repairs or alterations, culminating in the *Viva Gas*[6] case in 1983 which left the category of (zero-rated) alterations so wide that in the next year's Budget the Government announced that it would put an end to the importance of the distinction by standard-rating all alterations. It was as a result of a political concession during the course of the 1984 Finance Bill that zero-rating was in the end retained for substantial reconstructions and "approved alterations" of "protected buildings". This was achieved by the insertion into the zero-rating schedule of the VAT Act 1983 of a new Group 8A entitled "Protected Buildings".

There was, of course, a definition of "protected building", which was simply a building which was a listed building within the meaning of the relevant planning Act dealing with listed buildings or a building which was a scheduled monument within the meaning of the relevant Act dealing with ancient monuments. "Approved alteration" was defined (by Note (3) of Group 8A) as meaning, chiefly, an alteration requiring authorisation under the relevant planning or ancient monuments Act.

From 1984 to 1989 all "approved alterations" of "protected buildings" were zero-rated, but by the Finance Act 1989 a residential condition was imposed in line with the general recasting of the VAT law on supplies of property following the ECJ's decision in *EC v UK*[7]. This was done, not by completely recasting Group 8A (as was done in the case of Group 8, renamed "Construction of Dwellings, etc."), but by inserting a residential requirement into the definition of "protected building". On consolidation in 1994, Group 8A so amended was re-enacted as Group 6 of Schedule 8 to the VAT Act 1994. Thus the current (post-1989) definition of "protected building" is as follows:

> '"Protected building" means a building which is designed to remain as or become a dwelling or number of dwellings (as defined …) or is intended for use solely for a relevant residential purpose or a relevant charitable purpose after the

> reconstruction or alteration and which, in either case is–
>
> (a) a listed building, within the meaning of– [the relevant planning legislation] or
>
> (b) a scheduled monument, within the meaning of– [the relevant ancient monuments legislation]'

Zielinsky Baker was, of course, a case about a listed building, not a scheduled monument, and so the meaning of "listed building" in the Planning (Listed Buildings and Conservation Areas) Act 1990 was directly in point.

That meaning is found in section 1(5) of the 1990 Act and is as follows:

> 'In this Act "listed building" means a building which is for the time being included in a list compiled or approved by the Secretary of State under this section; and for the purposes of this Act–
>
> (a) any object or structure fixed to the building;
>
> (b) any object or structure within the curtilage of the building which, although not fixed to the building,

> forms part of the land and has done so since before 1st July 1948,
>
> shall be treated as part of the building.'

The taxpayer's argument in the Tribunal and the High Court focussed on the illogicality (as a matter of policy, and, therefore, of construction) of confining zero-rating to a single structure, the main dwelling house, when the approved alteration is made to another structure within the curtilage of the main dwelling house, which is used (together with the main dwelling house) as a single dwelling. This argument encountered difficulties in the Tribunal (which found for the taxpayer on the different, technical, ground, which was pursued in the Court of Appeal and the House of Lords), and was dealt a fatal blow by Etherton J., who held that "building" in the definition of "protected building" could not be read as including two or more buildings. Ironically, Lord Nicholls, who dissented in the House of Lords, was attracted by this argument, which in his view dealt with the absurd consequences of Customs' position in accepting that zero-rating applied to an alteration to the physical structure of the main dwelling house, but not to an alteration of a similar residential nature to an outbuilding within the curtilage.

As a result of the House of Lords' decision, zero-rating will continue to be available for all approved alterations to the fabric of the listed building itself – *i.e.* the building on the list maintained by the Secretary of State – provided that the listed building fulfils the residential conditions laid down in Group 6. Approved

alterations to certain (but not all) garages will also qualify. Thus, alterations consisting purely of architectural ornamentation will be zero-rated (as well as alterations to the accommodation), provided that the building being altered is the listed building itself, which is also a dwelling or used for a relevant residential or charitable purpose. But alterations, however domestic or residential in nature, will not qualify for zero-rating if what is being done is to convert an outbuilding into an adjunct of the listed building itself.

The technical ground, which appealed to the Tribunal and was pursued successfully in the Court of Appeal, but rejected by the House of Lords, relied on the definition of "listed building" in the 1990 planning Act. By that definition the outbuilding was treated as part of the main dwelling house, which was the listed building in question, and, indeed, as Rix L.J. pointed out in the Court of Appeal, the "approved alteration", which was in fact carried out to the outbuilding, was technically (as a matter of planning and even VAT law) an alteration to the main dwelling house which required, and received, approval or authorisation under the 1990 planning Act. The approach of treating the outbuilding as part of the main dwelling house – which, of course, itself satisfied the residential condition imposed by Group 6 – was carried through, on the taxpayer's argument, to illuminate the definition of "protected building" itself. Thus the "building" in that definition, which is required to be both a dwelling and a listed building or an ancient monument, was to be taken to be the artificial construct indicated by the definition of "listed building" in section

1(5) of the 1990 Act, and on that basis, of course, an approved alteration which was physically carried out to the outbuilding was to be taken to be an alteration of a the "listed building", which was a dwelling.

There were a number of indications that this was the right approach, in particular Note (10) to Group 6, which was introduced in 1989 at the same time as the residential condition which caused all the trouble, and which specifically provided that the construction of a building within the curtilage of a protected building does not constitute an alteration of the protected building. The taxpayer argued that this was a clear indication that the draftsman of the 1989 Act thought that the alteration of a building within the curtilage of a protected building *would* constitute an alteration of the protected building. This argument was dismissed by Lord Walker, giving the leading speech in the House of Lords, as an "uncertain straw in the wind" and Note (10) itself was disregarded, as being "unfathomable".

In the result, the House of Lords accepted Customs' case that it was wrong to use the definition of listed building in the 1990 planning Act to determined which building was to be taken to be the "protected building". This involved reading the definition of "protected building" as requiring that a "protected building" should be a residential building and *also* a listed building, though of course the word "also" is not found in the legislation. A more fundamental objection to the taxpayer's case was that it worked where the protected building was a listed building, but not – or not

in the same way – where the protected building was an ancient monument. This is the gist of the reasoning of Lord Hope of Craighead.

And what of the problem area not dealt with by the House of Lords? The main difficulty is the mismatch between the definition of "listed building" and the definition of "protected building" which results from the decision. In particular, "parts" of a listed building within the definition, sit in a kind of VAT limbo. A building within the curtilage of a listed building, which has been there since 1948, is not itself a listed building, although the listed building controls apply to it. It is "part" of a listed building and therefore *cannot*, strictly speaking, be a "protected building" for zero-rating purposes. This means that alterations (or sales after "substantial reconstruction") of a barn or other outhouse within the curtilage of a listed building, *even though* the barn or outhouse is a self-contained dwelling, do *not* qualify for zero-rating – unless Customs decide to allow zero-rating by concession. This is the position whether the main "listed" building is itself residential or not. Lord Walker, by words in parenthesis, indicated that an alteration to a detached potting shed would obtain zero-rating if it qualified as a separate dwelling with self-contained living accommodation. Unfortunately, the precise terms of the legislation do not give this result and Customs should be invited to give an assurance that this will be the position in practice.

[1] Counsel for the taxpayers, Zielinski Baker & Partners, in the Court of Appeal and the House of Lords.

[2] *Commissioners of Customs and Excise v Zielinski Baker & Partners Limited* [2004] UKHL 7, on appeal from [2002] EWCA Civ 692.
[3] (2000) VAT Decision 16722
[4] [2001] STC 585
[5] [2002] STC 829
[6] [1983] STC 819
[7] [1988] ECR 3127