GARDEN OR GROUNDS - THE SDLT DEFINITION OF RESIDENTIAL PROPERTY

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Introduction

Despite Stamp Duty Land Tax featuring as a topical issue due to Rishi Sunak's 'stamp duty holiday', it has also been playing out before both the First-tier and Upper Tribunals for another reason. As many will be aware, there are differences in the rate of SDLT dependent on whether a property is categorised as residential, or non-residential – the former rates being significantly higher. This categorisation turns on the meaning and effect of section 116 of the Finance Act 2003, which defines "residential property" for SDLT purposes. In the cases before the Tribunals, the taxpayer has sought to reduce their SDLT burden by arguing that the property in question was not wholly residential, usually because specific parts of the land were not "garden or grounds".

Legislation

The amount of tax due in relation to a chargeable transaction is contained within section 55 of the FA 2003. This section refers to two tables of rates for different parts of the total consideration for the transaction. Table A applies "*if the relevant land consists entirely of residential property*". Table B applies "*if the relevant land consists of or includes land that is not residential property*". In short, Table A rates are significantly higher than their equivalent counterparts in Table B. There are therefore noticeable differences in the amounts of SDLT payable dependent on its categorisation. As a rule of thumb, the difference is £60,000 – £70,000 per £1m in property value. It is noted that it is an 'all-or-nothing' test, so that if any part of a property is non-residential then the lower rates apply – there is no apportionment.

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The definition can be found in section 116(1) FA 2003 which provides:

> "(1) In this Part "*residential property"* means –
>
> (a) a building that is used or suitable for use as a dwelling, or is in the process of being constructed or adapted for such use, and
>
> (b) land this is or forms part of the garden or grounds of a building within paragraph (a) (including any building or structure on such land), or
>
> (c) an interest in or right over land that subsists for the benefit of a building within paragraph (a) or of land within paragraph (b);
>
> and "*non-residential property"* means any property that is not residential property…"

We note that "non-residential property" is defined 'negatively', i.e. as anything other than "residential property", rather than as land used for 'commercial' or 'agricultural' purposes, which is how the Revenue apply the definition for all intents and purposes.

Case law

It seems the Tribunals have largely adopted the Revenue's interpretation. The cases largely turned on the words "garden and grounds" in s 116(1)(b).

In *Hyman* [2019] SFTD 1277 the appellants argued that a barn, meadow and bridleway were not residential property due to their not forming part of the 'garden or grounds' of the house. The First Tier Tax Tribunal rejected that argument and stated that "*'grounds' has, and is intended to have, a wide meaning*", and further that "*its ordinary meaning is land attached to or surrounding a house which is occupied with the house and is available to the owners of the house for them to use*" (at [62]). 'Occupied' in this sense means that the land was available for the owners of the property to use "*as they wish*" – however, there is no requirement for such use. Grounds can also be "*allowed to grow wild*" and do not need to be separated by hedges or fences. Importantly – and this point was also dealt with in *Pensfold* [2020] UKFTT 116 – it is not fatal that other people have rights over the land. The fact that a farmer (*Pensfold*) or members of the public may enjoy the land and impinge on the owners' enjoyment of the grounds (and in some cases impose burdensome obligations on the owners) does not make the grounds any less the grounds of a residence. However, the conduct of a commercial activity on the grounds may render the land non-residential (also at [62] of *Hyman*).

The next case of note was *Goodfellow* [2019] UKFTT 750 where the Tribunal had to consider whether a room above a garage, and the paddocks, stables and stable yard formed part of the "grounds" of the property. In *Goodfellow*, the Tribunal introduced a new consideration – "*looking at the character of the property as a whole, the land surrounding the house is very much essential to its character, to protect its privacy, peace and sense of space, and to enable the enjoyment of typical country pursuits*" (at [17]). The Tribunal went on to state that no evidence was before it to show that a room above the garage was ever used for something more than residential purposes, that the office was nothing more than a study or dining room, and the paddocks (an adjunct to the stables) formed part of the grounds for recreational purposes ([18] *et seq.*).

In *The How Development 1 Limited* (TC/2019/00525, dated 15th January 2021), a woodland that was included in the conveyance was argued by the appellant's tax advisors not to form part of the 'garden or grounds'. The Tribunal found the woodland provided privacy and security and enhanced the residence's setting. Applying *Hyman* and *Goodfellow*, the Tribunal purported to give "garden or grounds" its ordinary meaning (at [77]). Going further than *Goodfellow*, the Tribunal found that in the case of grander properties an extensive wooded area would often be included. Distinct from the earlier case law, the woodland in *The How* was not readily accessible to the owners, nor was it clear it conveyed any real benefit on them as owners. However, this did not prevent the Tribunal from deeming it "*passively integral to The How's grounds*" (at [81]).

More recently, the Upper Tribunal has given its decision in the conjoined appeals of *Hyman, Goodfellow* and *Pensfold* [2021] STC 740. The taxpayers argued that land could only be part of the "garden or grounds" of a dwelling if the land was needed for the "*reasonable enjoyment of the house having regard to the size and nature of the house*". The Tribunal, acknowledging that "garden and grounds" are ordinary English words, avoided applying a literal interpretation. Giving the legislation a purposive interpretation, the legislature having included the word "of" was said to have intended there to be a connection between the garden or grounds on the one hand, and the dwelling on the other. However, the legislation is silent upon which test is to be applied when considering the aforementioned "*connection*". The Tribunal nonetheless stated that the purpose of section 116 is "*quite clear*" and there is no wording that imposes a requirement that the land should be needed for the reasonable enjoyment of the dwelling (at [38]).

Central to the appeal was the taxpayers' reliance on HMRC's Statements of Practice and Guidance. However, this case proved a salutary reminder that the courts or tribunals must decide the case by reference to the legislation, not the guidance - which may be wrong – as was indeed the case in respect of the old Revenue guidance (at [42]).

The Tribunal did, however, endorse some of the current Revenue guidance, but on an informative rather that authoritative basis. It agreed that whether land forms part of the garden or grounds requires consideration of a wide range of factors; with no single factor being determinative; not all being equal weight; and in some cases, a balancing exercise is necessary to consider whether the land in question constitutes "garden or grounds" (at [49]).

The most recent case in this area is *Brandbros* [2021] UKFTT 157. In that case, the taxpayer purchased a house with a garage. The garage was rented out under a commercial lease on the same day as the transaction completed. The questions included whether the transaction was residential or mixed-use, considering the commercial status of the garage (which went on to be used as a storage unit by a third-party business venture). The Tribunal held that the transaction was residential because the garage, being situated on the grounds of the property, was deemed to be residential under section 116(1)(b), regardless of its use.

Commentary

As stated above, in *Hyman* the Upper Tribunal decided that when determining what is, and what is not, grounds you look at a wide range of factors, e.g. 'use', 'layout of land and outbuildings', 'geographical factors', and 'legal factors and constraints'. Clearly, the test for determining whether something is in fact "grounds" is a vague one. Different judges will come to different views, meaning legal certainty is left questionable.

It is necessary to offer some criticism of the Tribunals' approach to section 116(1)(b). We limit the discussion to making a couple of points – much more could be said.

As was observed above, the definition of "residential property" is a 'inclusive' one, while "non-residential property" is defined by exclusion. It is not the case, in other words, that property, to be deemed 'non-residential', has to be positively shown to be commercial or agricultural. Yet this is precisely the approach the Tribunal has taken. For example, in the FTT decision in *Hyman* (quoted above), the Tribunal stated that:

> "*Land would not constitute grounds to the extent that it is used for a separate, e.g. commercial purpose*."

Although not explicitly stated, a similar approach is taken in most of the other cases. We consider this to be an incorrect application of the statutory definition. In *The How*, for example, even though the woodland is not "commercial" or "agricultural" in nature, it cannot, arguably, be said to be residential. This is because it is inaccessible from the property and does not convey any benefit on the proprietor *as proprietor*. We suggest, therefore, that there is a strong argument that *The How* was wrongly decided in spite of a lack of any commercial or agricultural use of the woodland.

Another example is the decision in *BrandBros*. In that case, the Tribunal decided the following:

> "*We are satisfied that the garage should be treated as a building or structure in the grounds or garden of the property. Therefore, as a matter of statutory interpretation, the garage is treated as residential property under section 116 regardless of the use to which it is put*."

The Tribunal then recognises that this is contrary to the dictum in the First Tier Tribunal decision in *Hyman* at [62], but nonetheless considers itself "fortified" in its conclusion by reference to a decision, heard on the paper, following an application for permission to appeal.

We consider it unfortunate that the Tribunal in *BrandBros* felt the need to go so far. The above-quoted part of the decision reads like the Tribunal didn't apply its critical faculties to the Revenue's arguments. This is because, if one applies the above reasoning to, say, a case where a factory or agricultural building is situated in the vicinity of a residential building – e.g. a cowshed in the vicinity of a farmhouse – the result would be that the cowshed, even if used for an agricultural purpose, would be considered 'residential'. Such a result would be absurd and clearly unintended by the wording of section 116(1)(b).

Be that as it may, the Upper Tribunal decision in *Hyman* could be seen as a positive one for taxpayers. This is because the decision clarifies somewhat the approach to take in these sorts of cases by endorsing the Revenue's multi-factorial approach. Given the vagueness of the approach, there will be many instances where there is an arguable case for the lower rates of SDLT. The first point of our conclusion is, therefore, that in spite of the apparent negative reception by the Tribunals of the arguments in the above cases, section 116 may yet prove a fertile ground for effective planning.

A second point to bear in mind is that any such planning should have "substance". It is possible the garage in *BrandBros* seemed a little too contrived for the Tribunal, and that *that* was the real reason for the Tribunal's dismissive determination. Perhaps the reception of an argument in a case where parts of the property genuinely appear non-residential might be different. An example of this, it is suggested, might be *The How*. In that case, the FTT did not apply the test suggested by the Upper Tribunal in *Hyman*. However, if that test were to be applied to the facts in *The How*, there is in our view a good case the woodland was not "residential property".

A final point is that planning should be done beforehand where possible. A case in point is *Pensfold* [2020] UKFTT 116. In that case, a farm was purchased and the lower rates were claimed on the basis that, at the time of purchase, the land was subject to a grazing agreement with a nearby farmer who had been using the land for grazing for some years. That claim was rejected by the FTT on the following basis:

> "*54. However, at the time of purchase, the land was not being grazed. The marketing brochure advertising the Farm for sale made no mention of the sale being subject to grazing rights, and the sale and purchase contract likewise made no mention of the property being subject to grazing rights. Indeed had the land, all 27 acres of it, been subject to grazing rights that would have made the plans to develop a rare breeds [sic] farm rather difficult to implement*. "

What would have been the position, one might ask, if the grazing agreement with the farmer, rather than being a "gentleman's agreement", had been formalised and referred to in the sales documents for the farm? It is possible that in such circumstances the farm would not have been "residential property" with the result that the taxpayer would have saved some £100,000 in SDLT on the purchase.