International Association of Assessing Officers
IAAO Research Exchange

2018 AVLR by Year

3-7-2018

Iceland Foods Ltd v Berry

Supreme Court of the United Kingdom

Follow this and additional works at: https://researchexchange.iaao.org/avlr-year-2018

Citation
[2018] UKSC 15

This Book is brought to you for free and open access by the AVLR by Year at IAAO Research Exchange. It has been accepted for inclusion in 2018 by an authorized administrator of IAAO Research Exchange. For more information, please contact researchexchange@iaao.org.

Hilary Term
[2018] UKSC 15
On appeal from: [2016] EWCA Civ 1150

JUDGMENT

Iceland Foods Ltd (Appellant) *v* Berry (Valuation Officer) (Respondent)

before

Lord Kerr
Lord Reed
Lord Carnwath
Lord Hughes
Lady Black

JUDGMENT GIVEN ON

7 March 2018

Heard on 25 January 2018

Appellant
Daniel Kolinsky QC
Luke Wilcox
(Instructed by TLT LLP)

Respondent
Tim Morshead QC
Zack Simons
(Instructed by HMRC Solicitors Office)

LORD CARNWATH: (with whom Lord Kerr, Lord Reed, Lord Hughes and Lady Black agree)

1. The court is asked to decide whether the services provided by a specialised air handling system, used in connection with refrigerated merchandise in the appellant's retail store, are "manufacturing operations or trade processes" for rating purposes. This turns on the construction of the Valuation for Rating (Plant and Machinery) (England) Regulations 2000 (SI 2000/540) (the "2000 Regulations"). If they are, then the air handling system falls to be ignored in calculating the rateable value of the premises. The Valuation Tribunal decided this issue in favour of the appellants. That finding was reversed by the Upper Tribunal ([2015] UKUT 0014 (LC)), whose decision was upheld by the Court of Appeal ([2016] EWCA Civ 1150; [2017] Bus LR 766).

Facts

2. The facts (as found by the Upper Tribunal) were set out in full in the judgment of the Chancellor (with whom Gloster and Sharp LJJ agreed) in the Court of Appeal. It is sufficient here to note the main points. Iceland is a well-known supermarket operator specialising in the sale of refrigerated foods, with more than 800 stores in the UK and Ireland. The appeal property, at 4 Penketh Drive, Liverpool, is typical. It is a small retail warehouse forming part of a larger retail development known as the Speke Centre. Iceland took occupation in May 2007. The property was let in a shell condition, and the air-handling system was installed by Iceland. Its business is mainly focused on the sale of refrigerated products, which represent roughly 80% of its sales by value, divided evenly between chilled and frozen lines. At the Penketh store, frozen and chilled products are stored and displayed in about 80 refrigerated cabinets, arranged around the perimeter of the sales floor and in four aisles running from front to rear.

3. All but one of the cabinets at the Penketh store are "integral" rather than "remote" units. The Upper Tribunal explained the difference:

> "18. … The object of any refrigerator is to maintain the internal temperature (and thus that of the goods stored in it) at the desired level by absorbing heat from within the cabinet and expelling it outside the cabinet by means of a condenser. Integral cabinets achieve this using refrigeration equipment and condensers installed within the body of the cabinet itself, and by expelling heat to the environment immediately

> surrounding the cabinet. Remote cabinets, in contrast, employ refrigeration equipment at a distance from the cabinets; heat is absorbed by a liquid refrigerant which is conveyed to the cabinet through pipes permanently installed in the store and is expelled remotely through condensers located outside the building.
>
> …
>
> 20. As integral cabinets are designed to operate below a particular ambient temperature (25ºC in the case of Iceland's … cabinets) the heat generated by the cabinets themselves must be controlled to ensure that they perform as intended and do not malfunction. Where a large number of integral cabinets is present in a confined space, it is necessary to provide an air handling system with a correspondingly large cooling capacity. If the design parameters of the cabinets are exceeded the permitted product storage temperature within the cabinets may be breached causing a deterioration in the quality of the products stored or displayed in them."

The advantages for Iceland of integral cabinets include flexibility, independence of operation, and lower capital cost. It is common ground that the value of the cabinets themselves is to be left out of account for rating purposes.

4. The air handling system was described by the Upper Tribunal as follows:

> "12. The air handling system provides a ventilating, heating and cooling service to the appeal property, and comprises three main elements. A large air handling unit with a mechanical cooling capacity of approximately 85 kW is located outside and to the rear of the building; this unit serves a network of ducts by which warm or cold air is supplied to and extracted from the retail area through an array of ceiling mounted diffusers and grilles. On our inspection we were able to observe the air handling unit and to contrast it with the very much smaller units on the rear walls of adjoining stores - one of which is considerably larger than the [premises]. Iceland's equipment occupies its own fenced compound and in size and shape resembles a very large refuse skip (4.5 metres by 2.35 metres in area) from which rise two vertical supply and return air ducts, each a metre square, which enter the rear wall of the

> building 4 metres above the ground. A separate but linked mechanical extract system is located at the rear of the retail area, furthest from the entrance, to deal with the removal of excess heat in that area. Finally, the whole system is controlled by means of a computerised control unit located adjacent to the air handling unit. …"

5. The air handling system functions at all times, day and night. It is designed and programmed to maintain the store temperature during trading hours at an acceptable level for both the functioning of the refrigerated cabinets and the comfort of staff and customers. To achieve the acceptable temperature range during trading periods, Iceland's control strategy targets a temperature within the store of 21ºC which is in the middle of the recommended range of comfortable temperatures for staff and customers. For the majority of the time an acceptable temperature is maintained on the sales floor without the use of mechanical cooling, but at 21ºC mechanical cooling commences. The aim is to ensure that the maximum temperature at which the cabinets are designed to function is not exceeded. Although a substantial proportion of the heat load is generated by other sources, the cabinets are by far the largest single contributor. Without the integral cabinets, the heavy-duty air handling system installed in the store would not be required and a very much smaller system would be sufficient.

The statutory provisions

6. Schedule 6 to the Local Government Finance Act 1988 is headed "Non-Domestic rating: Valuation". Paragraph 2(1) provides that the rateable value of a non-domestic hereditament is taken to be "an amount equal to the rent at which it is estimated the hereditament might reasonably be expected to let from year to year" on certain specified assumptions (none of which is now in issue). By paragraph 2(8), the Secretary of State is authorised to make regulations providing that in applying the preceding paragraphs, in relation to a hereditament of a prescribed class, "prescribed assumptions (as to the hereditament or otherwise) are to be made". The 2000 Regulations were made under that provision.

7. The present form and content of the regulations are derived from a report by an Expert Advisory Committee under the chairmanship of Mr Derek Wood QC, Rating of Plant and Machinery (Cm 2170) ("the Wood Report"), published in March 1993. The committee was established to review the law and practice relating to the rating of plant and machinery, with a view to updating and harmonising it throughout the United Kingdom. The report was followed by the Valuation for Rating (Plant and Machinery) Regulations 1994 (SI 1994/2680), which replaced the previous law. They were in turn replaced by the 2000 Regulations (applying to England only, following devolution), but without any change to the provisions

material to this appeal. As indicated in the explanatory notes to both sets of regulations, they "reflected" the recommendations of the Wood Report. (Equivalent Regulations, also said to reflect the Wood recommendations, have been made by the relevant legislatures in Scotland, Wales, and Northern Ireland.) It will be necessary to refer in more detail later to parts of the Wood Report, which is clearly an appropriate aid to construction of the Regulations (see *Bennion on Statutory Interpretation* 7th ed (2017), para 24.9).

8. Paragraph 2 of the 2000 Regulations is headed "Prescribed assumptions as to plant and machinery". It provides:

> "2. For the purpose of determining the rateable value of a hereditament for any day on or after 1 April 2000, in applying the provisions of sub-paragraphs (1) to (7) of paragraph 2 of Schedule 6 to the Local Government Finance Act 1988 -
>
> > (a) in relation to a hereditament in or on which there is plant or machinery which belongs to any of the classes set out in the Schedule to these Regulations, the prescribed assumptions are that:
> >
> > > (i) any such plant or machinery is part of the hereditament; and
> > >
> > > (ii) the value of any other plant and machinery has no effect on the rent to be estimated as required by paragraph 2(1); and
> >
> > (b) in relation to any other hereditament, the prescribed assumption is that the value of any plant or machinery has no effect on the rent to be so estimated."

It is important to emphasise the significance in the valuation of the Classes set out in the Schedule. Those Classes are the only categories of plant and machinery which are brought into account for valuation purposes. They are in effect exceptions to the general rule (embodied in sub-paragraphs (a)(ii) and (b)) that the value of plant and machinery has no effect on the estimation of value of the hereditament for rating purposes.

9. The Schedule sets out the classes of plant "to be assumed to be part of the hereditament" (in the words of the title). In broad terms, Class 1 covers plant and machinery used for generation, storage or transmission of power on the hereditament. Class 2 (relevant in this case) covers plant and machinery used in connection with heating, cooling and other services to the hereditament. Class 3 covers such items as railway lines, lifts, cables and other items used for transmission of electricity or communications, pipe-lines and drain or sewers. Class 4 covers a number of bulky items of plant and machinery (listed in Tables 3 and 4) such as blast furnaces, fixed cranes, and turbines and generators, but excludes smaller movable items (not exceeding 400 cubic metres) and those that are not "in the nature of a building or structure".

10. Class 2 provides:

> "Plant and machinery specified in Table 2 below … which is used or intended to be used in connection with services to the hereditament or part of it, *other than any such plant or machinery which is in or on the hereditament and is used or intended to be used in connection with services mainly or exclusively as part of manufacturing operations or trade processes*." (emphasis added)

"Services" are defined as meaning -

> "heating, cooling, ventilating, lighting, draining or supplying of water and protection from trespass, criminal damage, theft, fire or other hazard."

The plant and machinery specified in Table 2 includes (under the heading "Heating, Cooling and Ventilating") ten items of equipment (such as water heaters, and refrigerating machines) and associated "accessories". It is not in issue that the disputed air handling system is covered by the Table, nor that it is used "in connection with services to the hereditament" within the meaning of Class 2. The only issue is whether it is excluded by the italicised words quoted above. For simplicity in this judgment (following earlier usage - see below), I shall refer to those words as the "Class 2 proviso" or the "proviso". References in the judgment to the word "plant" should be read (where appropriate) as including reference also to "machinery".

Legislative history

11. In this court, as in the Court of Appeal, both parties sought to draw assistance from the background history of these provisions, dating back to the latter part of the 19th century, and including reports by a number of expert committees. The history is of some value in explaining the genesis of Class 2, and more particularly the background of the law and practice as understood at the time that the Wood Committee made its recommendations.

12. The main problem has been to draw a defensible line between, on the one hand, plant properly treated as part of the hereditament for the purpose of assessing its hypothetical letting value, and plant more fairly attributable to the tenant's business within it ("the tools of the trade"), having regard also to the need to keep up with changes in technology. The search for a coherent legislative solution can be traced back to the much-criticised decision of the House of Lords in *Kirby v Hunslet Union Assessment Committee* [1906] AC 43. The House there disapproved a distinction based on whether the plant was a fixture, in the traditional land law sense, but failed (so it was said) to put in place a workable alternative.

13. The resulting uncertainty led in due course to the establishment of an inter-departmental committee ("the Shortt Committee"), to inquire into the law and practice regarding the rating of plant in both England and Scotland. The committee reported in February 1925: *Report of the Inter-Departmental Committee on the Rating of Machinery and Plant in England and Wales* (Cmd 2340). Its recommendations led in turn to the enactment of the Rating and Valuation Act 1925. Section 24 of that Act, taken with the Third Schedule, can be seen as setting the pattern, albeit in simpler form, for subsequent enactments including the 2000 Regulations. It established the general principle that value of plant on the hereditament was to be left out of account for rating purposes, save for the classes specified in the Schedule, which were "deemed to be a part of the hereditament".

14. There is a helpful description of the general effect of the Third Schedule in the judgment of Lord Hewart CJ in *Townley Mill Co (1919) Ltd v Oldham Assessment Committee* [1936] 1 KB 585 (DC), although the facts (relating to plant in a disused mill) are too different from the present to make it of any direct assistance. In particular he drew a distinction (as had the Shortt Committee, para 15) between "motive" and "process" plant, only the former being taken into account for rating purposes. He said:

> "When one turns to the Third Schedule of the Act, it is apparent that it enumerates that type of machinery and plant which is conveniently described in the case as motive machinery; it is

> the machinery without which the mill could not begin to work, as, for example, the generation of power, heating and cooling, lifts and elevators, railways, tramlines and tracks, and other things, the foundation of that which was to become the work of the mill. When the machinery and plant referred to in the Third Schedule are eliminated, what is left is the kind of machinery which is concisely described in this case as process plant and machinery, operative plant and machinery, working and manufacturing plant and machinery. By section 24(1)(b), no account is to be taken of the value of any plant or machinery of that kind …" (p 598)

He noted that under the previous law the value of plant in a mill, though not rated as such, was taken into account as "enhancing the value of the hereditament to be rated" (p 599). The effect of the Act, intended as "beneficial to those interested in the carrying on of industry", was "to get rid of all the doctrine of enhanced value", and to lay it down that "process" plant must henceforth be disregarded when ascertaining the rateable value of the hereditament (pp 602-603). The decision was upheld by the House of Lords, where can be found statements to similar effect (see [1937] AC 419, pp 428-429 per Lord Russell of Killowen).

15. Turning to the detail of the Third Schedule, Class 1(b) can be seen as the precursor of Class 2 of the current regulations. It covered plant used -

> "… mainly or exclusively in connection with -
>
> (a) …
>
> (b) the heating, cooling, ventilating, lighting, draining, or supplying of water to the land or buildings of which the hereditament consists, or the protecting of the hereditament from fire:
>
> Provided that, in the case of machinery or plant which is in or on the hereditament *for the purpose of manufacturing operations or trade processes*, the fact that it is used in connection with those operations or processes for the purpose of heating, cooling, ventilating, lighting, supplying water, or protecting from fire shall not cause it to be treated as falling within the classes of

> machinery or plant specified in this Schedule." (emphasis added)

The other classes were (in very broad terms) similar in scope to what became the classes in the 2000 Regulations (see para 9 above).

16. The italicised words in the proviso to Class 1 seem to have been the first appearance in this context of the expression "manufacturing operations or trade processes". The circumstances in which the proviso came to be included are of some historical curiosity, since it was proposed by Mr Neville Chamberlain MP, as the responsible Minister (Hansard Standing Committee A, 4 August 1925, col 1093). He explained the purpose as being to exclude "such processes as really belong to the precise work which is being carried on in the shops" rather than "the general heating or ventilating of the plant". He gave an example:

> "where, for instance, a man is polishing at a buff, and there is a fan drawing off the dust so that it shall not go down his throat, that is to be treated as part of the machinery, and not as part of the heating or ventilating plant which is run."

It is unnecessary to decide whether those observations are admissible under the principle in *Pepper v Hart* [1993] AC 593 (see *Bennion op cit* para 24.11). The general purpose is clear enough from the wording of the proviso itself, and the example is so far from the present facts as to be of no practical assistance in this appeal.

17. Returning to the 1925 Act itself, section 24(3)-(6) enacted a procedure to provide more precise information about the contents of the specified classes. A special committee was to be established to prepare a statement "setting out in detail all the machinery and plant [appearing] to fall within any of the classes specified in the Schedule". The statement (modified if necessary following consultation) was to be embodied in a Ministerial order having effect as though substituted for the Third Schedule. Provision was also made for its subsequent revision at intervals as directed by the Minister.

18. The first such order was made in 1927 (The Plant and Machinery (Valuation for Rating) Order 1927 (SR & O 1927/480)). No further change was made until the setting up of the Ritson Committee, which reported in 1959: Report of the Committee on the Rating of Plant and Machinery. Its report included a revised statement under section 24(4), leading to the Plant and Machinery (Rating) Order 1960 (SI 1960/122). Between 1987 and 1990, section 24 was replaced in similar

terms by section 21 of the General Rate Act 1967, which preserved the 1960 regulations (section 117(3)). The first regulations made under the 1988 Act (The Valuation for Rating (Plant and Machinery) Regulations 1989 (SI 1989/441)) were in similar form. There was no material change to the substance of Class 1(b) (or 1B as it became) over this period.

19. Meanwhile, as explained by the Wood Report (chapter 4), the law in Scotland had developed separately. The general rule was established by section 42 of the Lands Valuation Act (Scotland) Act 1854 (17 & 18 Vict, c 91), which included within the definition of lands and heritages subject to rates "all machinery fixed or attached to any lands or heritages". The perceived burden was partially relieved by the Lands Valuation (Scotland) Amendment Act 1902 section 1, which added a proviso to section 42, limited to any building occupied "for any trade, business or manufacturing process". More recently, in response in part to unfavourable comparisons with the position in England, the Local Government and Planning (Scotland) Act 1982 section 4 gave the Secretary of State power to amend the proviso to section 42. That was done by the Valuation (Plant and Machinery) (Scotland) Order 1983 (SI 1983/120). It included (inter alia) an exception for certain categories of plant "used in an industrial or trade process", if located "wholly or mainly outwith" any building (regulation 3(2)).

The Wood Report

20. As already noted, the 2000 Regulations were designed to reflect the recommendations of the Wood Report. The committee included representatives of the professions, and the private sector, and of the Valuation Offices of the three jurisdictions The report itself contains a valuable survey of the development of the law, in the different parts of the United Kingdom, and discussion of its difficulties and inconsistencies.

21. Chapter 8, headed "The new scheme - competing principles", outlined the committee's general approach. In particular they accepted the validity "up to a point" of a "tools of the trade" exemption, but considered that it must be subject to qualification in the interests of fairness as between ratepayers (paras 8.6-7). They commented on the problems of dealing with plant used to provide services to a building but also having a trade purpose. Since this passage is relied on by Mr Morshead QC for the respondent, it is right to quote it in full:

> "8.8 What we have said so far relates to plant and machinery which is used for the purpose of a trade or industrial process. There is also the problem of plant and machinery which is introduced for the purpose of providing services for the

premises, or which forms part of its infrastructure. This type of equipment has never given rise to any difficulty as a matter of principle. In the letting market landlords typically provide the services and infrastructure, and it has been taken for granted that such items should always be deemed to form part of the hereditament, even in the case of property which is not normally found in that market.

8.9 The difficulty arises in the practical application of the principle, again as our predecessors have found, because it is extremely unusual, in the case of large-scale industrial property, to find plant and machinery which is installed exclusively for the purpose of providing general services, such as light, heat and ventilation, and is not also closely bound up with the trade process. In the existing regulations in each of the countries of the United Kingdom it has therefore proved necessary to draw some fairly arbitrary line in order to indicate the point up to which such plant and equipment can fairly be rated, by analogy with commercial hereditaments generally, and beyond which rateability should cease, because at that stage it is impossible in practical terms to disentangle the service from the process function. We have looked at the boundaries which have been drawn in the past, and have re-drawn them in order to simplify the task of valuers, assessors and agents and to reflect some of the technical changes which have taken place in industry since they were last reviewed."

22. The committee concluded, at para 8.10, that the "underlying conceptual approach" of the existing regulations in each part of the UK was "soundly based". They then summarised the principles on which future regulations should be based:

"Rateability should continue, in our opinion, to be determined in accordance with the following rules:

(1) that the land and everything which forms part of it and is attached to it should be assessed;

(2) that process plant and machinery which can fairly be described as 'tools of the trade' should be exempt within certain limits;

(3) that process plant or machinery (in certain cases exceeding a stated size) which is or is in the nature of a building or structure or performs the function of a building or structure should, however, be deemed to be part of the hereditament or subject;

(4) that service plant and machinery, and items forming part of the infrastructure of the property should be rated; and

(5) that, in the case of plant and machinery which performs both a service and a process function sensible lines have to be drawn which will indicate exactly how much falls to be rated and how much does not."

23. In chapter 9, the committee commented specifically on Class 1B of the English regulations (paras 9.11-12). They noted the distinction between plant and machinery which "services property", and that provided for use "in connection with the trade process being undertaken", adding:

> "But many services in non-domestic property, which might be found whatever the use of the property, are also used incidentally for manufacturing operations in some instances."

The definition in Class 1B was "not … free from ambiguity" and had given rise to disputes as to when plant should be treated as falling within it. As an example of the problem, they referred to the treatment of an air-conditioning plant, which may have been installed "to facilitate a particular process - for instance computer suites or clean rooms", or to "enhance the working conditions of employees", but it was impossible to distinguish between the two purposes. They concluded:

> "9.14 We have considered whether the current definition should be amended or dropped altogether. For example, we discussed whether it might be preferable to exclude from rateability only that service plant which 'solely' supports a process function. However to treat plant as process plant only if it was wholly for process purposes would increase the rateability of this type of plant and machinery. Such plant is rarely met in practice. As an alternative, we considered whether it would be possible to apportion the value of the plant between

> Classes 1B and 4 reflecting the relative use for service and process activity. But this would run contrary to our desire for cost-effectiveness of valuation effort and could create new opportunities for dispute.
>
> 9.15 We therefore conclude that notwithstanding the difficulties which have been encountered in deciding the degree to which plant is used for process purposes the law as we understand it in both England and Scotland should remain unaltered but that the draftsmanship should be improved to eliminate the difficulties inherent in the English Regulations."

Although the committee did not include their own draft, these paragraphs can be taken as a useful indication of the thinking behind the Class 2 proviso in its current form.

24. Annex L to the report contained a "Summary of worked examples with Wood Committee recommendations". This listed some "typical items of plant and machinery", for different categories of "Industry", with an indication of their rateability respectively in England (including Wales, and Northern Ireland), Scotland, and under the Wood recommendations. One category, headed "Industry - (e) Retail distribution", included the example of "refrigeration plant", and gave the answers as no, yes, no; so indicating that, at least in the perception of the Committee, such refrigeration plant was currently exempted from rateability and should continue to be so under their recommendations. It is also of interest that the Committee received written evidence from the Cold Storage and Distribution Federation, and the National Association of Warehousekeepers, and paid a visit to the Safeway Main Distribution Centre.

25. Finally, in anticipation of a submission of Mr Morshead, I should note one feature of the Scottish system on which the Wood Committee commented unfavourably. This was the distinction drawn by the 1902 Act between, on the one hand, premises "occupied for any trade, business or manufacturing process", and other types of premises, for example, "institutional premises such as hospitals, schools, colleges and universities …". They recommended against the perpetuation of this distinction in the harmonised system (paras 5.2(1), 8.21, 13.19).

The decisions below and the submissions in the appeal

The decisions

26. The Upper Tribunal (paras 64-66) found difficulty in finding "a satisfactory line to distinguish between uses which amount to trade processes and those which do not". They thought that "the conjunction of the expression with manufacturing operations", and the fact that it was "an exception to a general rule", pointed to "a less expansive approach to the scope of trade processes". They saw force in Mr Morshead's submission that -

> "… the common defining characteristic of manufacturing operations and trade processes is activity bringing about a transition from one state or condition to another, including by the creation, completion, repair or improvement of the subject matter of that activity."

They did not think that the display or storage of goods in itself, nor the creation of an environment conducive to the display or storage of goods, could properly be regarded as involving a trade process. The requirement of a particular retailer for more substantial or powerful equipment than is normally found in retail premises did not create a relevant distinction. They added:

> "66. All retail warehouses require heating, cooling and ventilation to a greater or lesser extent. We do not consider that the plant and machinery installed to provide those services can properly be regarded as being used or intended to be used as part of manufacturing operations or trade processes. We appreciate that the scale of Iceland's particular air handling system is dictated by the presence in its store of substantial numbers of integral cabinets, each of which creates heat, and which collectively are essential to Iceland's preferred style of trading. A serious malfunction of the air handling system would therefore put its stock at risk. That feature distinguishes Iceland's air handling needs from those of other retailers, but we do not regard that difference as critical. Although the particular needs of Iceland create a greater need for those services than the norm, we do not agree that they make its air handling system an exception to the general rule that such plant and machinery is to be assumed to be part of the hereditament and therefore to be rateable."

The tribunal went on to consider whether, assuming the air handling system was used as part of a trade process, it was "mainly" so used. They would have answered this question in favour of Iceland. They accepted Iceland's evidence that "the main technical and operational reason for Iceland's selection of this air handling system is its suitability for the maintenance of an environment in which integral cabinets can operate successfully" (para 78). This part of their decision has not been challenged.

27. In the Court of Appeal, the Chancellor (paras 40-46), having found little help in the authorities cited or the legislative history, relied on "the usual principles of construction". He agreed substantially with the reasoning of the Upper Tribunal. He thought that, normally at least, manufacturing operations and trade processes would be activities that "bring about a transition from one state or condition to another", and would "include the creation, completion, repair or improvement of the subject matter of that activity" (para 41). He noted also that the relevant sub-clause was "an exception, not a proviso", and should be construed "quite narrowly" (para 42). He thought the display of goods for retail sale was "the antithesis of a trade process". He accepted that "the process of freezing chickens" would probably be a trade process, but not "just keeping them frozen to be offered for sale". He also agreed with the tribunal that the fact that the environment appropriate for the methods of a particular retailer requires more substantial and complex equipment than normal does not mean that it is used for "a trade process" (para 45).

The submissions

28. In this court, Mr Kolinsky QC for Iceland submitted that the Court of Appeal misunderstood the underlying purpose of the legislation, as disclosed by a study of the legislative history, and adopted an unduly restrictive reading of the provision. He identified Iceland's trade process as "the continuous freezing or refrigeration of goods to preserve them in an artificial condition without which they would be worthless". Neither the ordinary use of language nor the case law justified the view that a transition was required from one state to another.

29. He relied (as he did in the Court of Appeal) on three authorities which supported a wider approach:

> i) *Union Cold Storage Co Ltd v Southwark Assessment Committee* (1932) 16 R & IT 160, relating to the application of the precursor of Class 4 of the 2000 Regulations to cooling chambers in a warehouse used for storing food. The case proceeded on the basis (recorded at p 164) that the chambers were "admittedly plant on the hereditament for the purpose of manufacturing operations or trade processes".

ii) *Union Cold Storage Co Ltd v Bancroft* [1931] AC 446, where the issue was whether, for the purposes of industrial derating, certain refrigeration equipment was for storage purposes or for the purposes of altering or adapting goods for sale. Viscount Dunedin described the plant as used as part of an "elaborate process involving the use of machinery … for the preservation of goods during storage" (pp 492-493).

iii) *Assessor for Lothian Region v BP Oil Grangemouth Refinery Ltd* (1985) SLT 453, where the Lands Valuation Appeal Court proceeded on the basis that a marine terminal at a petrochemical works, used solely for the purpose of loading refined oil, was premises "used in an industrial or trade process" (p 459, per Lord Ross).

30. As a further illustration of the practice of the Valuation Office at the time of the Wood Report, he referred to *Hays Business Services Ltd v Raley (Valuation Officer)* [1986] 1 EGLR 226 (LT) (Emlyn Jones FRICS). That concerned a warehouse used for the storage of archival materials including documents, films and audio-magnetic tapes. For some items of a sensitive nature, there had been installed specialist items of plant, including heating plant, humidifiers, and fire-protection equipment which utilised Halon gas so as to extinguish fires without damaging the stored items. The tribunal recorded that the Solicitor for the Inland Revenue, for the Valuation Officer, had conceded that the specialist heating and humidification equipment were non-rateable (p 227J). The tribunal reached the same conclusion in respect of the fire protection plant, which was not rateable because it was "on the hereditament primarily to protect the material that is stored there". It added:

> "Even if it were to be found that this could only be done by the protection of the building and therefore that that was the main use of the equipment, it would nevertheless not be included within the schedule because it was there expressly for the purpose of the trade process being carried on." (p 228E)

To similar effect, Mr Kolinsky relied also on the Wood Report, which proceeded on the assumption that an air-conditioning plant installed "to facilitate a particular process" such as a computer suite, was excepted from rating (see the passage quoted at para 23 above).

31. He found more recent support for the same broad approach in *Leda Properties Ltd v Howells (Valuation Officer)* [2009] RA 165 (LT George Bartlett QC President). Although no issue arose under the proviso as such, it was common ground that the sophisticated air handling system of a computer hall, described in the decision (para 3) as "provid[ing] the temperature and humidity control necessary

for process purposes", was to be left out of account under the regulations (paras 3, 34). Mr Kolinsky (who coincidentally appeared on that occasion for the respondent Valuation Officer) asked us to note that the Valuation Officer, Mr Howells, was described as having had since 1996 "a lead role" in the valuation of "specialist classes of property, including computer centres" (para 32). We were asked to infer that the common ground reflected the Valuation Office's considered and established position at the time.

32. For the Valuation Officer, Mr Morshead supported the reasoning of the Upper Tribunal and the Court of Appeal. Like them he submitted that the Class 2 proviso constitutes an exception to the general principle of rateability, and should be narrowly construed. The composite phrase "manufacturing operations or trade processes" must be read as a whole. It was not enough that the ratepayer's activity could be labelled as a "trade" and that one or more of its activities could be labelled as a "process". This was the error made by the tribunal in the *Hays* case, the reasoning of which was "plainly misconceived". The *Union Cold Storage* cases, to the extent that the statutory context was the same, were not necessarily comparable on the facts. In so far as they involved the application of a reduction in temperature to turn fresh goods into frozen or chilled ones, it would be uncontentious to describe that activity as a "manufacturing operation or trade process". He referred also by way of analogy to the Capital Allowances Act 1968 section 7, which defines "industrial building" as including (inter alia) a building in use for the purposes of "a trade which consists in … the subjection of goods … to any process" (section 7(1)(e)). In *Bestway (Holdings) Ltd v Luff* [1998] STC 357, 381, Lightman J had summarised, under heads (1) to (7), the effect of the authorities on the meaning of the expression "subjection to process" (notably *Kilmarnock Equitable Co-operative Society Ltd v Inland Revenue Comrs* (1966) 42 TC 675, 1966 SLT 224):

> "(3) Subjection to a process means a treatment (or course of operations) involving the application of a method of manufacture or adaptation of goods or materials towards a particular use, purpose or end …"

This showed that "process" implied some form of adaptation of the goods, not simply their storage in a constant state as in this case.

33. Mr Morshead also went further than the Court of Appeal. He submitted that Iceland's retail activities were wholly outside the scope of the Class 2 proviso, which was directed towards plant serving productive activities in industry, rather than commercial activities more generally. He supported that submission by reference to the history, including the reports summarised above, and specifically to the Wood Report (in particular paras 8.8-9 quoted above). He read the report as recognising a wide-ranging general rule applicable to "commercial hereditaments generally",

distinguished from the activities of industry; and as proposing for the latter (in his words) "an exemption only in the narrow case of plant which serves a 'process function' in industry".

Discussion

34. It is appropriate to begin by addressing Mr Morshead's broader submission, not in terms adopted by the Upper Tribunal or the Court of Appeal: that is, that the Class 2 proviso was concerned with productive activities in industry and not with other forms of commercial activity, such as the retail activities of Iceland. With respect to him, and to those instructing, I find this an impossible contention, both on the wording of the Regulations and against the background of the Wood Report. As to the first, if the draftsman had wished to limit the proviso to industrial activities, it would have been easy to say so. The inclusion of "trade processes", as an alternative to "manufacturing operations" can only be read as designed to widen the scope of the proviso to include other forms of trade and their processes. Trade is a familiar word which naturally extends to Iceland's retail activities. Subject to the interpretation of the word "process", there is nothing in the proviso or in its context to justify a narrower approach.

35. Further, far from gaining support from the Wood Report, the submission seems to me wholly inconsistent with it. It is true that there were some references in chapter 8 to particular issues affecting industry, but I cannot read those as intended to limit the scope of the recommendations more generally. On the contrary, the emphasis was on "the principle of fairness between ratepayers", which was regarded as "of paramount importance" for the political credibility of the "business rating system" (para 8.6). Nor was there any such limitation in the general rules proposed at paragraph 8.10, or the specific discussion of Class 2 (paras 9.14-15) (see above). Rule (2) proposed exemption for plant and machinery that can fairly described as "the tools of the trade", without any limitation of the nature of the trade. Similarly rule (5) which dealt with the need to draw lines between the "service" and "process" functions was expressed in general terms.

36. The submission is even less easy to reconcile with the Scottish legislation, which referred to "any trade, business or manufacturing process". As noted above, the report criticised that, not for extending its scope too far, but for not going far enough. Finally, Mr Morshead was unable to explain why, if his submission were correct, the worked examples extended to "retail distribution"; nor why from 1986 until as recently as 2009 the practice of the Valuation Office had apparently taken a wider view, so as for example to treat air conditioning plant for a computer centre as within the scope of the proviso. The *Hays* case (1986) is of course not binding on this court, nor indeed on the Valuation Office. It is unnecessary to decide whether on its facts it was correctly decided. However, if it had been thought in any way

controversial at the time of the Wood Report, it would be very surprising for it not to have been addressed.

37. Turning to the reasoning below, the Court of Appeal and the Upper Tribunal both saw the proviso as an "exception to a general rule", to be construed narrowly; and as naturally referring to a process designed to bring about a "transition" from one state to another. The Court of Appeal even saw some significance in the change (between 1925 and 1994) from a "proviso" to an "exception": para 42. In my view this approach pays insufficient regard to the place of the proviso in the scheme of the Regulations as a whole. Whatever word has been used at different times, it is and always was an exception to an exception. As already explained, the classes are themselves exceptions to the general rule of non-rateability; the relevant proviso (or exception) brings items of plant back into the scope of the general rule. The rationale is that, although they may provide a service to the building, they also provide a service to the activities of the trader within it, and the latter is their main or exclusive function. They are therefore more fairly considered for rating purposes as "tools of the trade" (in the words of the Wood Report) within the general rule of non-rateability.

38. There is certainly nothing in the Wood Report to suggest that the use of the word "except" or the other changes of language were intended to signal a substantive change. On the contrary, the passages quoted above show that the intention was to retain the law substantially without alteration, while improving the draftsmanship. How this was done (reflecting the language of Wood Report paras 9.11-12) is apparent from a comparison of the wording of the 2000 Regulations with that of its predecessors. An important change was the introduction of the expression "services …" to distinguish the functions of different categories of plant. Thus, it is recognised that plant which is used in connection with "services to the hereditament" may also be used in connection with "services … as part of manufacturing operations or trade processes …". Viewed in this way, the key distinction lies in the main use to which the services are put: in connection with the hereditament, or with the processes within it.

39. In my view, there is nothing in the word "process" itself which implies a transition or change. The cases under the Capital Allowances Act 1968 were no doubt coloured by the context, related to "industrial" buildings, and the need for goods to be "subjected" to a process. This is apparent in particular from the opinion of Lord Guthrie in the *Kilmarnock* case (42 TC 675, 681, 1966 SLT 224, 228). He recognised "process" as a word with "various meanings some wider than others", including "the widest significance of 'anything done to the goods or materials'"; but in conjunction with the word "subjection" a narrower reading was appropriate. I agree respectfully with that view of the wider meaning of the word "process", which is also consistent with the standard dictionary definitions. A "trade process" is simply a process (in that wide sense) carried on for the purposes of a trade.

40. Mr Kolinsky submits that, in the context of Iceland's trade, the word is apt to cover "the continuous freezing or refrigeration of goods to preserve them in an artificial condition". I agree. Since the services provided by the relevant plant have been held to be used "mainly or exclusively" as part of that trade process, they should be left out of account for rating purposes.

41. For these reasons, I would allow the appeal, and, on this issue, restore the decision of the Valuation Tribunal.