Neutral Citation Number: [2016] EWCA Civ 157

Case No: A3/2014/1326

IN THE COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)
THE HONOURABLE MRS JUSTICE ROSE
FTC/42/2013

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 17 March 2016

Before :
LADY JUSTICE SHARP
LORD JUSTICE SALES
and
LORD JUSTICE DAVID RICHARDS

- -

Between :

THE COMMISSIONERS FOR HM REVENUE & CUSTOMS	**Appellants**
- and -	
(1) APOLLO FUELS LIMITED & ORS	
(2) BRIAN EDWARDS & ORS	**Respondents**

- -

David Yates (instructed by **the General Counsel and Solicitor to HM Revenue and Customs**) for the **Appellants**
Rory Mullan and Oliver Marre (instructed by **Bury Walkers LLP**) for the **Respondents**

Hearing dates: 24 and 25 November 2015

- -

Approved Judgment

Lord Justice David Richards:

Introduction

1. The central issue on this appeal is whether an employee is liable to income tax in respect of a car leased to him by his employer on arm's length commercial terms, including lease charges at full market value. The Commissioners for HM Revenue & Customs (HMRC) contend that, although the employee does not derive any financial benefit from the lease and pays a full price by way of lease charges, he is nonetheless chargeable to income tax, by reason of Chapter 6 of Part 3 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA). The "cash equivalent" of the leased car, calculated in accordance with Chapter 6, is to be treated as part of the employee's earnings chargeable to income tax.

2. HMRC's case was rejected by the First-tier Tribunal (Judge David Demack and Ann Christian) and, on appeal, by the Upper Tribunal (Rose J). HMRC appeal to this court with the permission of the Upper Tribunal.

3. Income tax is a tax on income, or so it is generally understood. As Lord Macnaghten said in *London County Council v Attorney-General* [1901] AC 26 at 35:

> "Income tax, if I may be pardoned for saying so, is a tax on income. It is not meant to be a tax on anything else."

Income is not confined to salary, wages or other payments in money. Income may be received in other forms, such as benefits in kind. It is not surprising that the income tax legislation brings such benefits into charge, by ascribing a value to them and treating them as income. Goods or services supplied to an employee for full value would not ordinarily be regarded as conferring a benefit on the employee or as involving the receipt of income by him. A tax on the value of such goods or services would therefore be in the nature of a tax on consumption, rather than a tax on income. Of course, it is open to Parliament to deem the value of such goods or services, or indeed anything else, to be income, but one would expect Parliament to do so in clear terms. To borrow Lord Hodge's phrase in *Forde & McHugh Ltd v Revenue & Customs Commissioners* [2014] UKSC 14; [2014] 1 WLR 810 at [16], "the ordinary man on the underground would consider it to be counter-intuitive" that an employee should be subject to income tax on a supply for which he paid full value. Where that test was satisfied, Lord Hodge was "reluctant to attribute such a view to Parliament absent clear words or necessary implication."

The facts

4. The facts and procedural background are succinctly set out in paragraphs 2 to 11 of the Decision of the Upper Tribunal:

> "2. The corporate Respondents to this appeal are six companies in the Newell & Wright group. That group carries on a variety of trades and businesses including the distribution of fuel oils, transport contracting,

tanker manufacturing fabrication and sales, freight forwarding and haulage, and vehicle hire and sales. I shall refer to the corporate Respondents as 'the Group'.

3. The Group historically provided cars to salesmen and managers employed by its subsidiaries both as a perquisite of their employment and to enable them to carry out their duties. The cars were mainly second-hand and purchased at auction. The duties of the employees concerned included visiting new and existing customers and suppliers, delivering freight to customers, travelling between various company sites and visiting the companies' banks, accountants, etc. The annual business mileage of each of the employees concerned varied between 5,000 and 25,000 miles.

4. From 6 April 2002 there was a change in the law relating to the taxation of the provision of company cars to employees. Before that date, employees were charged to income tax as if a sum equal to 35 per cent of the value of the car when new was added to their income, but the charge was reduced to 25 per cent for employees who travelled more than 2,000 business miles in the year, and to 15 per cent for those who travelled more than 18,000 business miles. Further, if the car were four or more years old, the tax charge was reduced by one quarter.

5. Following the change, there was no longer any reduction in the charge to tax based on the extent of an employee's business travel or for the age of the car. Instead employees were charged to tax in the sum of 15 per cent (since reduced to 10 per cent) of the list price of the car if its CO_2 emissions were below a specified figure, with an addition of 1 per cent of the value charged for each 5g/km above that figure.

6. Following those changes, the Group decided it would move to an arrangement whereby it would lease the cars to the workforce for an arm's length hire rental. The original car provision scheme was ended in or about April 2003, and the new car leasing scheme implemented on its termination. All 26 employees who had previously been provided with a car agreed to the new arrangements and entered into car leases. Under the new arrangements, employees were told that they would be paid for business mileage at the same rate as other Group employees who used their own cars for business purposes. Sums due to the Employees as mileage allowance payments would be set off against

the rentals they owed to the Group under the car leases. 20 of the Group's employees are also Respondents to this appeal ('the Employees').

7. Each lease entered into by the Employees was a one-page document setting out the make and registration number of the car, the monthly rental and the VAT charged. The lease provides that amounts due in respect of mileage payments can be set off against the rental and that:

> "Should you give notice to leave the company you will have to
>
> A) Complete a standing order mandate for future rentals should you wish to continue hiring the vehicle, or
>
> B) Return the vehicle and any money owing will be settled on your last day."

8. The lease also provided that the Employee could cancel the agreement at any time, subject to 7 days notice or mutual agreement. The lease did not confer on the Group the right to cancel and did not restrict in any way the use that could be made of the car by the Employee.

9. It is accepted by HMRC that the rental paid by the Employees under the individual leases is an arm's length commercial rental as would be paid for the particular car if the Employee had hired it from a third party car hire company. The Tribunal heard evidence from the Group about how the rental charges had been calculated and made this finding of fact. It is not challenged by HMRC in this appeal. HMRC argue, however, that the car is still a benefit that falls to be taxed under Chapter 6 of Part 3 of the Income Tax (Earnings and Pensions) Act 2003 ('ITEPA') because the arrangements falls within section 114 of that Act. The Respondents say that Chapter 6 has no application in the circumstances of this case.

10. Because the Respondents had formed the view that the provision of the cars was not a taxable benefit, they did not deduct the tax now alleged to be due from the Employees' pay under the PAYE scheme or notify HMRC that cars were being provided to the Employees under the leases. HMRC, having concluded that the cars are subject to tax, served notices of assessment for that tax on the Employees

> rather than on the Group, under section 29 of the Taxes Management Act 1970. It was the Employees therefore who brought the appeal before the Tribunal in respect of the liability to tax on the car benefit. The Group's appeal related to HMRC's assertion that the Group was liable to pay NICs in respect of the use of the cars and in respect of the taxation and NIC liability for the mileage allowance payments.
>
> 11. The Tribunal found that no tax and no NICs were due to be paid in respect either of the cars or of the mileage allowance. HMRC do not challenge the finding that NIC contributions are not payable on the mileage allowance payments. Their appeal asserts that the Tribunal erred in finding that the Employees were not liable to pay tax on the cars and that the Group was not liable (i) to account for PAYE on the mileage allowance payments made to the Employees and (ii) to pay NICs on the cars under section 10 of the Social Security Contributions and Benefits Act 1992."

5. The principal issue before the Upper Tribunal and on this appeal is whether the arrangements for leasing the cars to the employees fall within Chapter 6 of Part 3 of ITEPA. If so, it is common ground that both income tax and National Insurance contributions are payable in respect of the cars. There is also an issue as to whether payments for mileage allowance, in respect of business use of the cars by the employees, are exempt from income tax as falling within the exemption provided by section 229 of ITEPA.

The relevant statutory provisions

6. This appeal, and the hearings below, have proceeded on the basis of the provisions of ITEPA in force in the 2009/10 tax year.

7. It is important to set the provisions of Chapter 6 of Part 3 of ITEPA in their statutory context. ITEPA imposes a charge to income tax on employment income, pension income and social security income: section 1(1). The provisions that define employment income, impose the charge to tax on it and set out exclusions and exemptions are contained in Parts 2 to 7, defined as the Employment Income Parts: see section 3.

8. The charge to tax on employment income under Part 2 is a charge to tax on "general earnings" and "specific employment income": section 6(1). Specific employment income is not in point, but "general earnings" means (a) earnings within Chapter 1 of Part 3 and (b) any amount treated as earnings under, among other provisions, Chapters 2 to 11 of Part 3: section 7(3) and (5).

9. Part 3 of ITEPA is headed "Employment Income: Earnings and Benefits etc Treated as Earnings".

10. Chapter 1 of Part 3 (section 62) defines "earnings" in relation to an employment to mean:

> "(a) any salary, wages or fee,
>
> (b) any gratuity or other profit or incidental benefit of any kind obtained by the employee if it is money or money's worth, or
>
> (c) anything else that constitutes an emolument of the employment."

11. For these purposes, "money's worth" means something that is either (a) of direct monetary value to the employee or (b) capable of being converted into money or something of direct monetary value to the employee: section 62(3).

12. Chapters 3-11 of Part 3 constitute "the benefits code": section 63(1). Chapters 3-7 deal with different subjects, viz. expenses payments; vouchers and credit-tokens; living accommodation; cars, vans and related benefits; and loans. There are no chapters 8 or 9. Chapter 10 provides for other benefits to be subject to a residual liability to charge and Chapter 11 excludes lower-paid employments from parts of the benefits code.

13. Section 64 in Chapter 2 of Part 3 deals with the relationship between earnings and the benefits code. Section 64(1) and (2) provide:

> "(1) This section applies if, apart from this section, the same benefit would give rise to two amounts ("A") and ("B") –
>
> (a) A being an amount of earnings as defined in Chapter 1 of this Part, and
>
> (b) B being an amount to be treated as earnings under the benefits code.
>
> (2) In such a case –
>
> (a) A constitutes earnings as defined in Chapter 1 of this Part, and
>
> (b) the amount (if any) by which B exceeds A is to be treated as earnings under the benefits code."

14. It is to be noted that the word "benefit" in the opening part of Section 64(1) is not defined.

15. Chapter 6 of Part 3 is headed "Taxable Benefits: Cars, Vans and Related Benefits". It comprises Sections 114-172. The provisions relevant to this appeal are as follows.

16. Section 114 defines the circumstances in which Chapter 6 applies and sub-sections (1)-(3) provide:

> "(1) This Chapter applies to a car or a van in relation to a particular tax year if in that year the car or van –
>
> (a) is made available (without any transfer of the property in it) to an employee or a member of the employee's family or household,
>
> (b) is so made available by reason of the employment (see section 117), and
>
> (c) is available for the employee's or member's private use (see section 118).
>
> (2) Where this Chapter applies to a car or van –
>
> (a) sections 120 to 148 provide for the cash equivalent of the benefit of the car to be treated as earnings,
>
> (b) sections 149 to 153 provide for the cash equivalent of the benefit of any fuel provided for the car to be treated as earnings,
>
> (c) sections 154 to 159 provide for the cash equivalent of the benefit of any fuel provided for the van to be treated as earnings; and
>
> (d) sections 160 to 164 provide for the cash equivalent of the benefit of any fuel provided for the van to be treated as earnings in certain circumstances.
>
> (3) This Chapter does not apply if an amount constitutes earnings from the employment in respect of the benefit of the car or van by virtue of any other provision (see section 119)."

17. It will be noted that section 114(2)(a) provides that where Chapter 6 applies to a car, sections 120-148 provide for the cash equivalent of "the benefit of the car" to be treated as earnings, and the remaining paragraphs make similar provision in respect of "the benefit" of a van or the provisions of fuel.

18. Section 117 is, to an extent, a deeming provision and provides that for the purposes of Chapter 6 a car or van made available by an employer to an employee or a member of the employee's family or household "is to be regarded" as made available by reason of the employment, subject to an exception not relevant to the facts of this case.

19. Section 118 provides that, for the purposes of Chapter 6, a car or van made available to an employee is to be treated as available for the employee's private use unless in the tax year in question the terms on which it is made available prohibits such use and it is not so used. Private use means any use other than for the employee's business travel.

20. Section 119 deals with the situation where an alternative to the benefit of a car is offered. Where a car is made available in the circumstances set out in section 114(1) and "an alternative to the benefit of the car" is offered, the offer of the alternative does not result in an amount "in respect of the benefit" constituting earnings under Chapter 1 of Part 6. As with the earlier sections, there is no definition of "benefit".

21. Section 120 is of central importance in this case:

> "(1) If this Chapter applies to a car in relation to a particular tax year, the cash equivalent of the benefit of the car is to be treated as earnings from the employment for that year.
>
> (2) In such a case the employee is referred to in this Chapter as being chargeable to tax in respect of the car in that year."

22. The method of calculating the cash equivalent of the benefit of a car is provided in section 121:

> "(1) The cash equivalent of the benefit of a car for a tax year is calculated as follows –
>
> *Step 1*
>
> Find the price of the car in accordance with sections 122 to 124A.
>
> *Step 2*
>
> Add the price of any accessories which fall to be taken into account in accordance with sections 125 to 131.
>
> *Step 3*
>
> Make any deduction under section 132 for capital contributions made by the employee to the cost of the car or accessories.
>
> *Step 4*
>
> If the amount carried forward from step 3 exceeds £80,000, the interim sum is £80,000.
>
> In any other case, the interim sum is the amount carried forward from step 3.
>
> *Step 5*
>
> Find the appropriate percentage for the car for the year in accordance with sections 133 to 142.

> *Step 6*
>
> Multiply the interim sum by the appropriate percentage for the car for the year.
>
> *Step 7*
>
> Make any deduction under section 143 for any periods when the car was unavailable.
>
> The resulting amount is the provisional sum.
>
> *Step 8*
>
> Make any deduction from the provisional sum under section 144 in respect of payments by the employee for the private use of the car.
>
> The result is the cash equivalent of the benefit of the car for the year."

23. Sections 122-124 define the price of a car for the purposes of calculating the cash equivalent. The price is calculated by reference to the price of a new car, rather than the market value of the car leased to the employee. A similar approach is adopted in relation to accessories, for which provision is made in sections 125-131.

24. Section 132 deals with the contributions by employees which fall to be deducted under step 3 of the calculation of the cash equivalent of the benefit of a car. The amount of the deduction allowed in any tax year is the lesser of (a) the total of the sums contributed by the employee in that year and any earlier years and (b) £5,000.

25. Sections 133-142 contain detailed provisions for determining the "appropriate percentage" for the purposes of steps 5 and 6 of the calculation of the cash equivalent of the benefit of the car. The appropriate percentage is for the most part determined by reference to the car's CO_2 emissions.

The issues

26. Before the Upper Tribunal, the principal issue, regarding the effect of Chapter 6 on car leases at full market value, was seen as giving rise to the following issues, as stated in its Decision at [20]:

> "a. Does the lease between the Group and its Employees involve a transfer of property in the car? If so, then the requirement in parentheses in subsection (1)(a) that the making available of the car has to be without any transfer of the property in it is not satisfied and the arrangements will fall outside Chapter 6. This raises two sub-issues:
>
> i. Do the leases transfer *any* property in the car to the Employees?

ii. If so, is the transfer of a partial interest in the car enough to preclude the application of the subsection (1)(a) and hence take the arrangements outside the scope of Chapter 6?

b. Is there another section of the ITEPA which treats an amount in respect of the cars here as earnings from the employment so that section 114(3) applies to take the arrangements outside Chapter 6? In particular, does section 62 apply even though it is accepted by the Respondents that the amount treated as earnings by section 62 would in the case of at least some of these Employees be nil?

c. Does the fact that, as HMRC accepts, the Employees paid the full market value for the cars mean that there is no 'benefit of the car' within the meaning of section 120 and hence nothing which can be liable to tax in this case?"

Transfer of property

27. The Upper Tribunal dealt with the first issue, whether the lease involved a transfer of property in the car, at [22] – [49]. At [39], the Upper Tribunal concluded that the First-tier Tribunal had been wrong to conclude that the car leases created property rights which were transferred to employees, for the purposes of section 114(1)(a), and therefore rejected the submission on behalf of employees on this point. In case she was wrong on that point, Rose J proceeded to consider at [40]-[49] HMRC's alternative submission that the words in parenthesis in section 114(1)(a) apply only where the entire ownership of the car is transferred to the employee, not where some partial right is transferred. Rose J concluded that, if she was wrong on the first point and the leases did transfer a proprietary interest in the cars to the employees, the scope of those interests was sufficient to mean that the condition in parenthesis in section 114(1)(a) was not satisfied, with the result that Chapter 6 would not apply to the car leases.

28. By a respondent's notice, the employees challenged the Upper Tribunal's decision on the first point, while HMRC challenged the decision on the alternative point.

29. The submissions of both parties before the First-tier Tribunal and the Upper Tribunal focussed on whether the car leases, as chattel leases, conferred a proprietary interest in the cars in favour of the employees. This involved a consideration of authorities such as *Bristol Airport plc v Powdrill* [1990] Ch 744, *On Demand Information plc v Michael Gerson (Finance) plc* [2000] 1 WLR 155 and *Celestial Aviation Trading 71 Ltd v Paramount Airways Private Ltd* [2010] EWHC 185 (Comm). This is a fertile area of academic debate.

30. It appeared to this court that the submissions on this point below, and repeated in the skeleton arguments for this appeal, and the decisions below proceeded on a wrong basis. Section 114(1)(a) does not refer to the creation or transfer of a proprietary interest in the car or van but to "any transfer of the property in it". "The property" in a chattel, such as a car, is a long established and well-understood concept connoting, in effect, legal title to the chattel. When the common law of the sale of

goods was codified by the Sale of Goods Act 1893, this was the phrase used to cover a transfer of title and it is repeated in the current legislation, the Sale of Goods Act 1979. Section 61(1) defines "property" as "the general property in goods, and not merely a special property". It means the absolute ownership interest in the goods: see *Bridge, Gullifer, McMeel & Worthington: The Law of Personal Property* (2013) at Chap 10. While the absolute ownership interest may be subject to other interests, for example a charge or mortgage, "the property" in a chattel is not constituted by an equitable or limited propriety interest. This point is clear from what Robert Walker LJ said in *On Demand* at 171B:

> "Contractual rights which entitle the hirer to indefinite possession of chattels so long as the hire payments are duly made, and which qualify and limit the owner's general property in the chattels, cannot aptly be described as purely contractual rights."

Such rights were more than "purely contractual", and may have created a proprietary interest in favour of the hirer, but they did not involve the transfer of the property in the chattels to the hirer but merely qualified and limited "the owner's general property in the chattels".

31. The Court put this point to Mr Mullan, counsel for the employees, at the end of the first day of the hearing and invited him, and counsel for HMRC, to make submissions on it the following day.

32. At the start of the hearing on the second day, Mr Mullan stated that, having considered the point, the employees were no longer pursuing their challenge to this part of the Upper Tribunal's decision.

33. The decision of the Upper Tribunal that there was no transfer of the property in the leased car and that Section 114(1)(a) is satisfied therefore stands, and we heard no further submissions on it. In my judgment, the decision of the Upper Tribunal on this point was right, but not for the reasons given. It was right because the car leases involved no transfer of the general property in the cars.

"Benefit of the car"

34. The next issue listed above is whether section 114(3) operates to exclude the application of Chapter 6 to the car leases. As section 114(3) applies only if an amount constitutes earnings from the employment "in respect of the benefit of the car" by virtue of any other provision, I consider it more logical to deal next with the third issue, viz. whether the fact that, as HMRC accept, the employees paid the full market value for the cars means that there was no "benefit of the car" within the meaning of section 120 and hence nothing that could be liable to tax in this case.

35. The Upper Tribunal, affirming the First-tier Tribunal, upheld the employees' submissions on this point. Rose J said at [64]:

> "I agree with the Respondents that the use of the word "benefit" in the benefits code is an indicator that what is intended to be caught is something which benefits the

> employee and that there is no such "benefit" if the employee has paid the market rate for the asset which is provided. It is true that the way that the benefit is calculated under the current provisions (taking into account the list price and the level of CO_2 emissions) reflects other policy considerations. But that cannot, in my judgment, affect the more fundamental point of whether there is a benefit to which those current provisions should be applied."

Rose J said that this textual indicator was strongly supported by two appellate decisions on which the employees relied, *Mairs (Inspector of Taxes) v Haughey* (1992) 66 TC 273 (Court of Appeal of Northern Ireland) and *Wilson (Inspector of Taxes) v Clayton* [2003] EWCA Civ 1657; [2005] STC 157. She also accepted the submission that "benefit" cannot mean something different in Sections 114 and 120 from its meaning in section 203 in Chapter 10 of Part 3, particularly in light of section 63.

36. Rose J stated her conclusion at [71]:

> "I therefore consider that *Mairs v Haughey* and *Wilson v Clayton* are authorities establishing that fair bargains are excluded from the regime for taxing benefits conferred on employees because there is no benefit which is properly subject to tax. Since HMRC accept that the leases between the Group and the Employees were at arm's length, there is no benefit here which is subject to tax under Chapter 6."

37. HMRC challenged this conclusion, and the Upper Tribunal's reasons for it, on a number of grounds.

38. First and foremost, HMRC submit that, provided the conditions in section 114(1) are satisfied, an employee receives "the benefit of the car" and it is simply a question of calculating the cash equivalent of that benefit in accordance with section 121, such sum being treated as earnings from his employment. Although "the benefit of the car" is not itself expressly defined, it does not import any requirement of a benefit in any ordinary sense of the word or any requirement to appraise whether the employee has paid full value for the lease of the car. As it was put by counsel for HMRC, the word "benefit" is merely shorthand for the circumstances identified by Parliament as engaging the provisions of Chapter 6.

39. HMRC submit that this is made clear by the deliberate policy choice by Parliament to use CO_2 emissions as the basis for calculating the amount to be treated as earnings. Counsel for HMRC stated in his skeleton argument that, while allowance is made for the deduction of any contributions made by the employee for the private use of the car:

> "It is an inherent feature of the scheme that such contributions, whilst possibly being regarded in the real world as fair value or market value, will in some circumstances be insufficient to prevent deemed income arising because of the fundamental mechanism of Chapter 6 which is to use the list price of a car as

> new and then to deem an annual benefit based on its CO_2 emissions".

40. Secondly, *Mairs v Haughey* and *Wilson v Clayton* were both decided under earlier and different legislation and in any event were not concerned with the provision of a car.

41. Thirdly, the Upper Tribunal's conclusion is inconsistent with the structure of the benefits code. HMRC does not dispute that fair bargains are excluded from the meaning of "employment-related benefit" in section 203 for the purposes of Chapter 10 of Part 3, dealing with benefits not covered by the specific earlier Chapters, but they say that that is not the case with all or most of the other Chapters.

42. In approaching the proper construction of Chapter 6, it is of course right to set it in its legislative context, which includes the other Chapters of the benefits code. But the overall context is the charging of the income and other benefits derived from employment to income tax. Since employees may be rewarded in many ways other than, or in addition to, the payment of salaries or wages, there need to be provisions which bring such other benefits into charge for income tax. Of course, as I earlier mentioned, Parliament may deem a provision or supply for which the employee has paid full value to be income for the purposes of income tax, but the taxpayer would expect Parliament to do so in clear terms. It is worth noting that the benefits code is one of the products of HMRC's Tax Law Rewrite Project, the aim of which was that direct tax legislation should be "rewritten in clearer, simpler language": see para 5 of the Explanatory Notes to ITEPA.

43. Parliament has used the phrase "the benefit of the car" in sections 114 (2) and 120(1) without defining it. Nonetheless, HMRC submits that it should be construed as no more than a drafting formula, describing the consequences of the application of section 114(1), rather than treating it as a meaningful phrase. On HMRC's case, Parliament could as well have used the phrase "the provision of the car". Indeed, in paragraph 2 of the skeleton argument of counsel for HMRC, the issue on the appeal is said to be whether an income tax charge arises in respect of "the provision" of cars.

44. It is true, as HMRC submit, that once Chapter 6 is engaged so that the need to calculate the cash equivalent of the benefit of a car arises, the calculation is linked not to the value of the provision of the car, as would for example be the case if the calculation started with the market rate at which the car would be leased, but is linked to the price of a new car and its CO_2 emissions. In my judgment, this does not mean that the word "benefit" is to be treated as carrying no meaning or significance. It means only that, if the employee receives a benefit as that word is normally understood, it is valued for tax purposes by reference to the price of a new car and its CO_2 emissions. HMRC's case suggests that the underlying policy rationale for Chapter 6 is to impose a tax on pollution but, if that were truly the policy, this is a very odd way of giving effect to it. Not only is it included in the statute imposing income tax on employment-related income, it is not carried out in any effective or consistent manner. HMRC accept that if an employer sold a car to an employee at full market price, no charge to income tax would arise, whatever the CO_2 emissions of the car.

45. These are all considerations which, in my judgment, show that the choice of the word "benefit", without any definition qualifying or altering its ordinary meaning, was

intended to show that, before a charge to income tax in these circumstances arises, there must be a benefit to the employee in the ordinary sense of that word. It is not a case of implying a requirement or condition into Chapter 6. It is simply a case of giving meaning and effect to its express terms.

46. As the Upper Tribunal's references to *Mairs v Haughey* and *Wilson v Clayton* make clear, neither was concerned with the particular provisions of Chapter 6 directly in point on this appeal. Both were concerned with section 154 of the Income and Corporation Taxes Act 1988, which in a general sense but not in its detailed provisions, was the predecessor to Chapter 10.

47. Section 154(1) provided that where, in the case of an employee:

> "(a) by reason of his employment there is provided for him … any benefit to which this section applies … ; and
>
> (b) the cost of providing the benefit is not (apart from this section) chargeable to tax as his income,
>
> there is to be treated as emoluments of the employment, and accordingly chargeable to income tax under Schedule E, an amount equal to whatever is the cash equivalent of the benefit."

Section 154(2) provided that the benefits to which the section applied were accommodation, entertainment, domestic or other services "and other benefits and facilities of whatsoever nature", with certain specified exceptions.

48. In *Mairs v Haughey*, the issue was whether payments made to compensate the workforce on the privatisation of the Belfast shipbuilders, Harland and Wolff, for the loss of contingent rights under a redundancy scheme was a "benefit" within the meaning of section 154. Hutton LCJ, sitting in the Court of Appeal of Northern Ireland, approved the following from the decision of the Special Commissioner:

> "Section 154 brings benefits into charge. All kinds of benefits are covered: but whatever they are, they must still be capable of being described as "benefits". The legislation is aimed at profits (in a broad sense) which escape taxation under the mainstream Sch E provisions for one reason or another. It is not aimed at receipts resulting from fair bargains."

49. Hutton LCJ continued (66 TC 273 at 314):

> "In my opinion, the decision of the Special Commissioner on this point was correct. The Respondent received the payment of £4,506 in return for surrendering his contingent right to receive a payment under the enhanced redundancy scheme, and the Special Commissioner held, at page 4D of his decision, that the payment did not overvalue that right. Therefore, I consider that the Respondent did not receive a "benefit" within the meaning of s.154 where the money received was paid to him, by way of fair valuation, in consideration of his surrender of a

> right to receive a larger sum in the event of the contingency of redundancy occurring."

50. The decision in *Mairs v Haughey* was considered and approved by the Court of Appeal in *Wilson v Clayton*. It concerned compensation payments made to employees following the compromise of their claims for unfair dismissal. The Crown accepted, as it had done in the Court of Appeal in *Mairs v Haughey* if not before the Special Commissioner, that section 154 did not operate to tax an employee in respect of a fair bargain. Peter Gibson LJ, with whom Clarke and Arden LJJ agreed, said ([2005] STC 157 at [50]) that the decision in *Mairs v Haughey* made "good sense". He continued:

> "The justice of excluding from the scope of s154 a payment made by an employer to an employee pursuant to a fair bargain seems to me self-evident, and, as Clarke LJ suggested in the course of the argument, it may explain why a payment made by the employer to an employee pursuant to an award of damages or to a settlement of a claim for such damages is, as the Crown accepts, not within s154. Where parties at arm's length arrive at a genuine compromise in settlement of hostile litigation, it would be an extremely difficult task for any tribunal or court to unpick the constituent parts of the bargain and to put a value on those parts. For my part, I would not rule out the possibility that it might be shown in some cases that the reason for the payment was to confer a gratuitous benefit within a compromise agreement so that to that extent s154 might apply. But there is no suggestion that there was any such reason in the present case."

51. The fact that HMRC did not contend that a fair bargain gave rise to a benefit under section 154 does not detract from the authority of these judicial statements as to the meaning, in a general sense, of "benefit" in these provisions. While it is true that both decisions were concerned only with section 154, the statements are applicable to the word "benefit" in other parts of the benefits code, unless by reason of a definition or context they are shown to be inapplicable. They were concerned with the meaning and significance of an ordinary word, not with a specialised use of it in a particular section. Clearly these decisions do not dictate that the same conclusion should be reached in respect of Chapter 6 but they provide significant support for that conclusion.

52. HMRC places reliance on the provisions of the other Chapters of the benefits code.

53. Chapter 3 is concerned with the payment of expenses. The scheme is to treat all sums paid to an employee in respect of expenses, or paid away by an employee in respect of expenses out of sums put at his disposal for that purpose, as taxable earnings but to permit the employee to make deductions allowed under identified sections in Chapter 2 of Part 5 (Deductions for Employee's Expenses). The effect is largely to produce a common code for the deductibility of expenses, whether paid by the employee out of his salary or out of funds provided to him for that purpose. HMRC submit that to introduce a test whether the payment of expenses was "beneficial" to the employee would make no sense when considered against the

statutory scheme. Indeed it would not, but Chapter 3 makes no reference, defined or undefined, to "benefit" or any similar term. It is a longstanding and self-contained code on expenses which can shed no light on the very different provisions of Chapter 6.

54. HMRC submit that throughout Chapters 4 to 7 there are multiple indications that the draftsman is not concerned with whether the relevant provision is, on the particular facts of an employee, beneficial or provided at arm's length or under a fair bargain.

55. Chapter 4 deals with cash and non-cash vouchers and credit cards, debit cards and other "credit-tokens" provided to an employee by reason of his employment. In each case "the cash equivalent of the benefit" of the voucher or token is treated as earnings. The "cash equivalent" of the benefit of a cash voucher is the sum of money for which the voucher can be exchanged: section 81. The "cash equivalent" of the benefit of a non-cash voucher and of a credit-token is the difference between the cost of provision and any part of that cost made good by the employee: sections 87(2) and 94. There are certain exceptions, including where the expenditure by the employee would be deductible as an expense.

56. In all the instances covered by Chapter 4, the employee has been provided with a benefit in the ordinary sense of the word. I find it difficult to see how Chapter 4 can do other than assist the employees' case on Chapter 6.

57. Chapter 5 provides that if living accommodation is provided for an employee by reason of the employment, "the cash equivalent of the benefit of the accommodation" is treated as taxable earnings: section 102. There are exceptions for necessary or customary accommodation in section 99. The method of calculating the cost equivalent of the benefit depends on whether the cost of providing the accommodation (as defined in section 104) exceeds £75,000. In each case the cash equivalent is calculated in a way which gives credit for payments made by the employee. Again Chapter 5 supports the employees' position on Chapter 6.

58. HMRC place particular reliance on section 98 in Chapter 5, concerning accommodation provided by a local authority. It provides:

> "This Chapter does not apply to living accommodation provided for an employee if –
>
> (a) the employer is a local authority,
>
> (b) it is provided for the employee by the authority, and
>
> (c) the terms on which it is provided are no more favourable than those on which similar accommodation is provided by the authority for persons who are not their employees but whose circumstances are otherwise similar to those of the employee."

59. The reason for this exception is obvious. It has long been one of the functions of local authorities to provide social housing, often at less than its full market value.

Without this exception, the employees of local authorities would be placed at a disadvantage compared with other people in a similar position. It clearly does not assist HMRC's case.

60. Chapter 7 is said by HMRC to be perhaps the clearest indication that Parliament is not concerned with whether there is a benefit in the sense of something that is actually beneficial to the employee. Chapter 7 deals with employment-related loans, defined to include any sort of credit. Section 175(1) provides:

> "The cash equivalent of the benefit of an employee-related loan is to be treated as earnings from the employee's employment for a tax year if the loan is a taxable cheap loan in relation to that year."

61. Broadly stated, a taxable cheap loan is one where no interest is paid on the loan in a year when the employee holds the employment or the amount of interest paid on it for that year is less than the interest that would have been paid "at the official rate". The cash equivalent of the benefit of an employment-related loan is the difference between the amount of interest that would have been payable on the loan for that year at the official rate and the amount of interest (if any) actually paid on the loan for that year.

62. In broad terms, it can readily be seen that Chapter 7 is concerned with loans made on terms that are beneficial to the employee. HMRC nonetheless submit that benefit to the employee is irrelevant to the application of Chapter 7 because the mechanism of judging whether a loan is a taxable cheap loan is by reference to the official rate of interest, as opposed to a market rate judged by the individual circumstances of the borrower, and even if the rate is above the official rate of interest, it is still caught if interest is rolled up as opposed to being paid.

63. HMRC relied on the decision at first instance of Peter Gibson J in *Williams (Inspector of Taxes) v Todd* [1988] STC 676. In that case a district inspector of taxes was charged to income tax on the benefit of a loan provided to him by the Inland Revenue. The taxpayer was instructed to take up duties in London and, to assist him in his move from Wigan, he was paid an advance of salary which, although repayable on demand, would be recovered by deductions from his salary by equal instalments over a ten-year period with no interest payable or recoverable from him in respect of the advance. He was charged to tax on the cash equivalent of the benefit of the loan under section 66 of the Finance Act 1976. He appealed, contending that the advance was not a loan for the purposes of section 66 and, even if it were, he had not received any benefit to which the section could apply.

64. Reversing the general commissioners, Peter Gibson J held that the advance was a loan and that he had received the "benefit" of it for the purposes of section 66. Peter Gibson J reached the second decision on two, alternative grounds. One ground was that, as the taxpayer had the advantage of the loan interest-free, "it is plain and obvious that it is right to describe him as having the benefit of the loan" (p.682). The other ground was that it was not in any event necessary to conclude that the loan in fact provided a benefit to the borrower in order for section 66 to apply. Section 66(1) applied where there was outstanding for the whole or part of a year a loan to an employee or a relative "of which the benefit is obtained by reason of his employment" and either no interest is paid on the loan or the amount of interest is less than interest

at the official rate. Peter Gibson J observed at page 681 that the words referring to "benefit" did not look like a condition: "it does not say that the loan must be beneficial to the employee." Section 66(3) charged to income tax the release or writing off of the whole or part of a loan "the benefit of which was obtained by reason of his employment". Even a loan at interest greater than the official rate is:

> "one as to which it is sensible to say that 'the benefit of which was obtained by reason of his employment'. The sub-section is quite plainly applicable to all loans obtained by reason of employment even if a loan is for a full commercial rate of interest".

65. Peter Gibson J concluded that:

> "It is apparent that it is not necessary for there to be a benefit, in the terms of something advantageous to the employee, found for section 66 to apply. The reference in the heading to the chapter to "Benefits" does not to my mind compel any different conclusion. Such a heading is in general terms applicable to a whole group of sections."

66. I do not consider that the terms of Chapter 7 or *Williams v Todd* assist HMRC's case.

67. In *Williams v Todd*, Peter Gibson J was concerned to construe the word "benefit" in the expression "a loan … of which the benefit is obtained by reason of his employment" in section 66(1) of the Finance Act 1976 and, in the same sub-section, the word "benefit" in the expression "an amount equal to whatever is the cash equivalent of the benefit of the loan for that year". It is a perfectly ordinary use of language to speak of a borrower receiving the benefit of a loan, even if it is at a full commercial rate, and this was the submission of counsel for HMRC as recorded by the judge at p.680:

> "… he submitted that for the purposes of s66 it is not necessary to find as a fact that a benefit accrued to the employee from the loan. He submitted that s66(1), and indeed other sub-sections, simply assumed that it was appropriate to refer to a borrower as having the benefit of a loan in the same way as it is common enough in ordinary parlance to ask the question, "did you receive the benefit of the loan?" without going into the question whether in fact the loan provided a benefit for the borrower."

68. That reading of sub-section (1) was underlined by the terms of sub-section (3) which the judge at p.681 held to be quite plainly applicable to all loans obtained by reason of employment even if it was for a full commercial rate of interest. Further, sub-section (4) was otiose if "benefit" in sub-section (1) did not apply in the case of a loan at a full commercial rate of interest.

69. Chapter 7 is a sophisticated set of provisions designed to deal with a number of situations. The main thrust of the Chapter is to bring into charge to income tax loans to employees which are beneficial to them in the ordinary sense of the word. Employment-related loans are chargeable to tax if they are "taxable cheap loans". A

loan will be a taxable cheap loan if either no interest is paid on it for the relevant year – an obvious case of benefit in the ordinary sense of the word – or if the interest paid on it is less than interest "at the official rate". The "official rate" is fixed from time to time by regulation and it is apparent from looking at those regulations that the rate is changed to meet changes in commercial lending rates. Nonetheless, because it is at any time a fixed rate, there will be occasions on which an employment-related loan is at a full commercial rate that is below the official rate at that time. Where that occurs, such loan is in effect deemed to be a cheap loan, even though it is not cheap by reference to prevailing commercial interest rates. This deeming effect can, of course, work both ways. Because new official rates tend to lag behind changes in commercial rates, there will be periods when the official rate is less than prevailing commercial rates. It is simply a by-product of having a fixed rate that some loans on full commercial terms will nevertheless be subject to tax.

70. It seems clear from the legislation that the purpose of applying "the official rate" is to avoid arguments as to what an appropriate commercial rate for a loan by an employer to an employee would be in circumstances where there is no objective yardstick. This is shown by section 176 which applies a different regime to "loans on ordinary commercial terms" made to an employee by a person in the ordinary course of a business that includes the lending of money or the supplying of goods or services on credit. Provided the terms of the employment-related loan are the same as comparable loans made generally to members of the public at or about the same time or, where the terms differ, the difference arises in the ordinary course of the lender's business, the loan is not a taxable cheap loan. In the case of such loans, there is a readily available objective yardstick by which to determine whether the loan was on ordinary commercial terms and hence not a cheap loan. Likewise, a loan at a fixed rate of interest will not be a cheap loan provided that the interest payable for the tax year in which the loan was made was no less than interest at the official rate for that year. The fact that subsequently the official rate is increased to a level greater than the fixed rate of interest under the loan will not make it a cheap loan.

71. In my judgment, the use and meaning of the word "benefit" in relation to loans under Chapter 7 does not shed light on the meaning of "benefit" in Chapter 6.

72. HMRC accept that the word "benefit" in Chapter 10 carries its ordinary meaning.

73. For all these reasons, I conclude that the Upper Tribunal and the First Tier Tribunal were right to decide that a charge to income tax arises under Chapter 6 only if the terms on which a car is leased to an employee confer a benefit on the employee in the ordinary sense of that word. The employees in this case received no such benefit.

Section 114(3)

74. By reason of my decision on the meaning of "benefit" for the purposes of Chapter 6, it is not strictly necessary to consider whether, in any event, the effect of section 114(3) would be to prevent a charge to tax arising in this case under Chapter 6. However, it was fully argued and it was the first basis on which the Upper Tribunal held that no charge to tax arose under Chapter 6.

75. Section 114(3) provides:

> "This Chapter does not apply if an amount constitutes earnings from the employment in respect of the benefit of the car or van by virtue of any other provision (see section 119)."

It is common ground that the reference to section 119 is not in point in this case.

76. The purpose of this provision is clear enough. If an amount constitutes earnings under a different provision, it will be chargeable to income tax as such, it would involve a charge to double taxation if it were also to be chargeable to income tax under Chapter 6.

77. It was common ground that the provision most obviously in point was section 62 and the submissions of the parties focussed on that provision.

78. Section 62, as stated in sub-section (1) "explains what is meant by "earnings" in the employment income Parts." For present purposes, the relevant head of "earnings" is that set out in section 62(2)(b): "any gratuity or other profit or incidental benefit of any kind obtained by the employee if it is money or money's worth". Section 62(3), codifying earlier judicial decisions, defines "money's worth" as:

> "something that is –
>
> (a) of direct monetary value to the employee, or
>
> (b) capable of being converted into money or something of direct monetary value to the employee."

79. The car leases in the present case did not contain any prohibition on the employee sub-hiring the car. If, therefore, the car was leased to an employee at less than the market rate, the employee could derive a benefit by sub-hiring the car at a full market rate and this would constitute "money's worth" as defined.

80. In the present case, however, the cars were leased to the employees at full market value and therefore no charge to income tax would arise in consequence of section 62. The employees submitted, and the Upper Tribunal accepted, that a nil amount arising under section 62 was nonetheless "an amount constitut[ing] earnings from the employment in respect of the benefit of the car … by virtue of any other provision" (being section 62). Rose J said at [57]:

> "I hold that on the proper construction of section 114(3), if the arrangement falls to be considered under section 62 ITEPA because the car is money or money's worth then it falls outside section 114. That is the case even if, because of the payments made by the employee in return for receiving the asset that constitutes 'money's worth', the amount of the earnings that falls to be taxed under section 62 is in fact nil in a particular case. Section 114(3) is intended to settle the interrelationship between Chapter 6 and section 62 and that does not depend on the happenstance of whether in a particular case there is a small excess of the money's worth."

81. In [55] and [56], Rose J summarised the submissions of the employees. First, "there is nothing incongruous about treating nil as an "amount" for this purpose". They pointed to the fact that HMRC did the same thing in a different context, section 236, which I will deal with later. The employees submitted that HMRC's construction led to an absurdity in the relationship between section 62 and section 114:

> "If the Employees had paid less than full market value for the lease of the cars then HMRC accept that there would be something that falls to be taxed as earnings under section 62 and section 114(3) would apply to take the car provision outside Chapter 6 – a situation which is greatly preferable from the Respondents' point of view. It is only because HMRC acknowledges that the Employees have paid full market value for the car rental that the earnings are nil and the question of the application of Chapter 6 arises."

82. I do not accept the decision of the Upper Tribunal on this point. Nil is not a number or an amount, but the absence of a number or an amount. It is a cipher of no value. There may, of course, be circumstances where the context in which the word "amount" is used indicates that it is to include nil. But, the ordinary meaning of the phrase "an amount constitutes earnings from the employment" connotes a positive number, in other words an amount. There is nothing, in my judgment, in the context which dictates a different approach. In particular, the submission of the employees based on an absurdity in the relationship between section 62 and section 114 is not well-based if, as I and the Upper Tribunal have held, "benefit" carries its ordinary meaning. The purpose of section 114(3) is, as I have mentioned, to avoid a charge to double taxation. A charge to double taxation cannot arise if the amount said to constitute earnings by virtue of another provision is nil.

Mileage allowance

83. A similar point arose in relation to the subsidiary issue in this appeal, on the application of the mileage allowance exemption in section 229. Rose J adopted the same approach, but interestingly the submissions of HMRC and the employees were, in effect, the reverse of their submissions on section 114(3).

84. As Rose J explained at [75], employees who use their own private cars for business journeys can usually claim a mileage allowance from their employer to reimburse them for the fuel they use and a contribution to the other costs of running their cars. Provided that the mileage allowance does not exceed an amount specified in the legislation, the employee does not have to pay tax on it. This exemption is contained in section 229. Section 229(1) provides that no liability to income tax arises in respect of approved mileage allowance payments for a vehicle to which Chapter 2 of Part 4 applies. So far as relevant to the present case, section 229(1) does not apply if "the vehicle is a company vehicle": see section 229(4)(b). HMRC accepts that, if the cars leased to the employees are not "company vehicles" within the meaning of section 236(2), mileage allowance payments would be exempt from income tax pursuant to section 229.

85. So far as relevant, a vehicle is defined as a "company vehicle" by section 236(2) if in a tax year:

> "(b) the cash equivalent of the benefit of the vehicle is to be treated as the employee's earnings for the tax year by virtue of –
>
> (i) section 120 (benefit of car treated as earnings),
>
> (ii) … or
>
> (iii) section 203 (residual liability to charge: benefit treated as earnings), …"

86. Rose J had held that section 120 did not apply to treat the cash equivalent of the benefit of the car as earnings. If she was wrong on that point, she went on to consider whether section 236(2)(b) applied if the cash equivalent was nil because the car leases were on full market terms.

87. This issue would arise in circumstances where, carrying out the calculation required by section 121 and deducting in accordance with section 144 any payment made by the employee, the cash equivalent of the benefit would be nil. Section 144(2) in terms provides that where the amount paid by the employee equals or exceeds the provisional sum resulting from the calculation, "the provisional sum is reduced so that the cash equivalent of the benefit of the car for that year is nil". Rose J observed that this provision contemplated that a nil amount could still be a "cash equivalent" within the meaning of section 120. She held that if the cash equivalent was nil, it was still to be treated as earnings under section 120 for the purposes of section 236(2)(b). She said at [84]:

> "I agree with HMRC that the subsection is concerned with identifying vehicles which fall within the scope either of Chapter 6 or of Chapter 10 as opposed to whether an actual tax liability arises for the employee. It is intended to have the effect that if the car or van is within Chapter 6 or within the residual charge in Chapter 10, it is treated as a company car and different rules apply to any payments made for mileage from the rules which apply when an employee uses his own car. This does not depend on whether the cash equivalent is a positive value or nil."

88. As Chapter 6 does not apply to the car leases in this case, the subsidiary issue concerning the mileage allowance did not arise for decision before the Upper Tribunal or in this court. But, as Rose J quite properly came to a view on the point, I will express my own view.

89. I do not agree with Rose J on this point. The test laid down in section 236(2)(b) is not whether the cash equivalent of the benefit of the car was nil but whether that cash equivalent was "to be treated as the employee's earnings" for the relevant tax year. If the cash equivalent is nil, it forms no part of the employee's earnings nor, in my judgment, is the effect of these provisions to deem an absence of earnings in respect of the car to be earnings. I do not accept that the sub-section is intended in those circumstances to have the effect that, if the car is within Chapter 6 (or within the residual charge in Chapter 10), it is to be treated as a company car. If that were the

intention, I cannot see why the section does not simply say so. Standing back from the detail of the language, it is not easy to see why an approved mileage allowance paid to an employee who uses his own private car for business journeys should be exempt from income tax, while such an allowance provided to an employee who pays full value for the lease of a car to him should not be exempt.

Conclusion

90. For the reasons given in this judgment I would dismiss the appeal. Like the Upper Tribunal, I express no view on the issue which would have arisen if the appeal were allowed, namely whether HMRC were entitled to assess the employees for the tax on the cars under the Taxes Management Act 1970.

Lord Justice Sales:

91. I agree.

Lady Justice Sharp:

92. I also agree.