Appeal number:TC/2016/3270

CORPORATION TAX – computation of profits – deductions for replacement of tools – implements, utensils, articles – s 68 CTA 2009 and s 74(1)(d) TA88; mistake claim -para 51A Sch 18 FA 98 whether generally prevailing practice.

FIRST-TIER TRIBUNAL
TAX CHAMBER

TURNERS (SOHAM) LIMITED **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE CHARLES HELLIER

Sitting in public at Taylor House London on 26 to 29 November 2018

Julian Hickey instructed by Qubic Tax for the Appellant

Rupert Baldry QC and Ben Elliott, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. This appeal raises two issues. The first is the correct construction of section 68 CTA 2009 and its forebear section 74(1)(d) TA 1988. These provisions concerned the deductibility of expenditure on “implements, utensils and articles”. The second is the application in the facts of the case to Case G of para 51A Sch 18 FA 1998 which removes HMRC’s liability to make repayment on a claim based upon a mistake if the mistake was based on generally prevailing practice.

2. In its corporation tax computations for the years ending 31 December 2009, 2010 and 2013[1] the Appellant ("Turners" or "the company") deducted the expenditure it had incurred on the replacement of tractor units and trailers used in its haulage trade. It claimed the deductions were authorised by section 68 CTA. HMRC considered that those sections did not authorise such deductions and on that basis issued closure notices denying the deductions. The company appeals against those notices.

3. In its original corporation tax return for the period ending 31 December 2008, the company claimed capital allowances for the costs of replacement tractor and trailer units, but in 2011 made a "mistake claim” in relation to that year, disclaiming capital allowance expenditure and claiming a deduction for the costs of replacements under section 74(1)(d). HMRC refused that claim both on the basis that section 74(1)(d) did not authorise a deduction and on the basis that if it did the claim was prevented by para 51A as the treatment originally adopted for that year was in accordance with generally prevailing practice and therefore excluded by case G of that section. The company appeals against those conclusions.

4. In the first part of this decision, after making some initial findings of fact, I shall discuss the arguments in relation to the deductibility of the costs of the replacement trailer and tractor units. In the second part I shall address the arguments in relation to para 51A.

The Evidence and Findings of Fact

5. There was a Statement of Agreed to Facts and Issues. I heard oral evidence from Graham Miller the company’s chief financial officer and Mr Rakeel Hussain of HMRC and had a bundles of various copy documents.

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[1] For the years 2011 and 2012 it appears that the company adopted the same practice but HMRC did not open an enquiry into the relevant returns.

6. Turners carry on the business of a road haulage trade which includes the distribution of food, fuel, building products, and containers.

7. In the years 2008, 2009, 2010, and 2011 it purchased trailer units, tractors and tank units for use in its trade and as replacements for items previously used. In all it purchased 615 such replacement items in these years and incurred a total cost of some £33 million. The 615 items have been divided into seven categories (although I refer to them collectively in this decision as tractor and trailer units):

(1) 398 tractor units

(2) 31 curtain sided trailers

(3) 12 Skelly trailers

(4) 128 refrigerated or temperature controlled trailers

(5) 19 fuel tankers

(6) 18 cement tankers

(7) 9 food tankers.

8. Each of the units in each category was for the purposes of this decision of the same nature as the example of that category provided in Mr Miller's evidence. They were of the following descriptions:

(1) Tractor Units were the front ends of articulated lorries. They pulled trailers and tankers. They had three sets of axles and were some 5.3m (18ft) long. 342 of them could be used for any haulage purpose other than the transport of hazardous materials and 56 were adapted to pull food and hazardous material.

(2) Curtain sided trailers were trailers with flexible curtains along both sides. They were used for the transport of goods requiring protection form the elements. They were 13.6, (43ft) long.

(3) Skelly trailers had no sides and were used to transport containers. They were 12m (40ft) long.

(4) Refrigerated and temperature controlled trailers were about the same size as curtain sided trailers but had solid sides and refrigeration equipment.

(5) Fuel tankers were 12.3m (41ft)long; food tankers 11.5m (38ft)long and cement tankers were some 10m (33ft)long

9. The company's statutory accounts for each of the periods were prepared in accordance with generally accepted accountancy practice ("GAAP"). Turners treated the cost of replacement tractor and trailer units as the costs of tangible fixed assets. They were capitalised at acquisition cost in the balance sheet and depreciated over their useful economic life, recognising debits in the computation of the Profit and Loss account for the depreciation charge each year. No debit was recognised in any year in the computation of the profit and loss account for the full cost in that year of any of the items.

10. For the year ending 31 December 2008 the company initially claimed capital allowances in its tax return for the expenditure on the replacement items purchased in those years.

11. On 21 December 2011 the company amended its tax return for the 2008 year replacing the claim to expenditure qualifying for capital allowances for that year by a deduction from its trading profits of the amount expended on those items in that year. On the same date it made an overpayment claim under section 51 Sch 18 FA 89 for the year ending 31 December 2008 claiming relief (and disclaiming capital allowance expenditure) on the same basis as for the year to 31 December 2009.

12. In its tax return for the years ending 31 December 2010 and 2013 the company made no claims to capital allowances for the purchases of the items but deducted their cost in completing its taxable profits.

13. HMRC opened enquiries into the returns for 2009, 2010 and 2013 which they concluded by refusing the deductions claimed for the expenditure on the trailer and tractor units. They also refused the overpayment relief claim.

14. Turners appeal against the closure notices and the refusal.

15. I make further findings of fact in relation to the para 51A matters later in this decision.

<u>PART 1: The deductibility of expenditure on implements, utensils and articles.</u>

16. The statutory provisions potentially relevant to the deductibility of expenditure on such items changed over the course of the accounting periods under consideration and fell into two groups with potentially different effects:

(1) for the period ending 31 December 2008 the statutory provisions relevant to the argument were section 74 TA 88 and sections 42 and 48 FA 98.

(2) for the remaining periods the relevant provisions were in CTA 2009 (enacted as part of the Tax Rewrite Project) and in particular sections 46, 48, 51, 53 and 68 of that Act.

17. In the remainder of this Part I shall consider first the arguments in relation to deductibility for the period ending 31 December 2008 and then those relating to the other periods.

<u>(1) The period ending 31 December 2008</u>

18. Section 42 FA 1998 provided:

> "(1) For the purposes of Case I or II of schedule D the profits of a trade, profession or vocation must be computed on an accounting basis which gives a true and fair view, subject to any adjustment required or authorised by law in computing profits for those purposes. ..."
>
> I shall refer to the accounts prepared on such a basis as "commercial accounts"

19. Section 46 FA 98 provided:

> "(1) In provisions of the Corporation Tax Acts relating to the computation of the profits of a trade, profession or vocation references to receipts and expenses are (except where otherwise expressly provided) to any items brought into account as credits or debits in computing such profits.
>
> There is no implication that an amount has been actually received or expended.
>
> ..."

20. Section 74 (1) TA 88 provided:

> "(1) Subject to the provisions of the Corporation Tax Acts, in computing the amount of profit to be charged under Case I or II of schedule D no sum shall be deducted in respect of
>
> > ... (d) any sum expended for repairs of premises occupied, or for the supply, repairs or alterations of any implements, utensils or articles employed for the purposes of the trade or profession beyond the sun actually expended for those purposes;
> >
> > ...
> >
> > (f) any capital withdrawn from, or any sum unemployed or intended to be employed in the trade profession or vocation…"

21. I understood that it was common ground that "supply" was used in its archaic sense of "replacement" – as in "supply teacher". The issue did not arise for consideration because the units were supplied in the more modern sense as well as being, as a matter of fact, replacements.

22. In relation to these periods and these provisions the company argues that: (1) the cost of replacement of the tractor units and trailers was a sum expended on their "supply" (and was, and did not exceed, the sum actually expended) and that the decisions of the Courts show that section 74(1)(d) and its predecessors is to be construed as authorising the deduction of such expenditure even if capital in nature; and (2) that those decisions show that "implements, utensils or articles" was a phrase capable of encompassing such items as tractor units and trailers.

23. HMRC argue: (1) that subparagraph (d) is merely prohibitive: it prevents the deduction of amounts which might otherwise be deductible in computing profits and does not authorise the deduction of any sum proscribed by other provisions or which had not been deducted in computing commercial profits; and (2) that the trailers and tractor units were not "implements, utensils or articles".

24. I was referred to a number of authorities in which the tools repair rule had played some part. Some of these cases were decided against the background of three other regimes for deductions relating to items such as tools and plant and machinery. Before turning to those authorities I shall give a brief account of those regimes.

"Renewals Allowances".

25. The company's skeleton argument describes the deduction it seeks as a "Renewals Allowance constituted by section 68 and its predecessor section 74(1)(d)". I have not adopted this terminology because at relevant times before the advent of the capital allowance regime there were four different sets of rules which related to the obtaining of deductions in relation to tools or plant and machinery. They were:

> (1) what I shall call the "tools rule" as it applied to replacements (without any presumption that it is limited to things which may be called tools) in section 74(1)(d) and its predecessors;
>
> (2) the wear and tear provisions originally enacted in section 12 FA 1878;
>
> (3) the obsolescence rules;
>
> (4) the renewals practice.

26. Relevantly at all times the Acts also contained the provision in section 74(1)(f) TA 88 (which first appeared in Rule 3 of the schedule D Rules in Income Tax Act 1842) which prohibited a deduction in computing profits "on account of capital withdrawn from or any capital sum employed or intended to be employed as capital in [the trade]".

(1) The tools rule

27. This first appeared in the Income Tax Act 1842 but in a form which meshed with the rule which then applied which taxed in each year the average of the profits of the previous three years. It provided that no deduction should be made:

> "for any sum expended for the supply or repair or alteration of any implements, utensils or articles employed for [the trade]…beyond the sum usually expended for such purposes according to the average of three years preceding the [year of assessment]".

28. The same rule appeared as Rule 3(d) in the Income Tax Act 1918. In 1927 there was a change: taxable profits were no longer computed on a three-year average and the word "usually" and the reference to the 3 year average were omitted from the provision in consequence. These provisions were then repeated in the same form in the Income Tax Act 1952, then in section 130 TA 1970 and later in section 74 TA 88.

(2) The wear and tear provisions

29. These first appeared in section 12 Customs & Revenue Act 1878, and provided for a deduction for wear and tear. They required the Commissioners in assessing any trades to "allow such deduction as they may think just and reasonable as representing the diminished value by reason of wear and tear during the year of any machinery or plant used for the purposes of the concern".

30. This allowance became Rule 6 of the schedule DI rules in the Income Tax Act 1918. By contrast with the tools rule which appeared among the prohibitions in Rule 3, this provision authorised a deduction from profits free from the prohibition on the deduction of capital items.

31. This provision remained in force in this form until the advent of the capital allowances regime in 1945.

(3) the obsolescence provisions

32. Rule 7 of the schedule DI Rules in Income Tax Act 1918 provided for a deduction for the cost of replacing and plant and machinery which had become obsolete. The deductible amount was the cost of the replacement less the aggregate of prior wear and tear allowances.

33. Like the wear and tear allowance this was a deduction from profits determined outside any prohibition of the deduction of capital items.

34. I believe this provision remained in force until the advent of the capital allowances regime.

(4) The Renewals Practice.

35. This was first authoritatively set out in a Command Paper "on the subject of allowances for depreciation and obsolescence" produced to Parliament in 1918. The paper describes the section 12 wear and tear provisions and the obsolescence provisions but also described an allowance for which no statutory authority was claimed and which operated as an alternative to the wear and tear and obsolescence allowances. This alternative permitted the costs of *renewing* plant and machinery to be claimed as a deduction. The deductible amount was the cost of the replacement less the scrap or sale vale of the plant and machinery replaced.

36. There is some question as to whether this Practice was a free standing concession or represented a very generous interpretation of the tools rule – extending it to all plant and machinery and providing for a degree of carry forward of unused deductions (although requiring reduction of the scrap value of the replaced asset). It might even be characterised as a concession which extended the strict operation of the tools rule. What is clear however is that the Practice authorised a deduction for the capital cost of renewed plant and machinery.

Judicial consideration of the deduction of expenses in relation to "implements, utensils or articles ".

37. I now turn to the five cases to which I was referred in which the tools repair rule played some part, and in which comment had been made as to the operation of section 74(1)(d) (or its predecessors) and the indications or otherwise in those cases that section 74(1)(d) or its predecessors authorised deduction and of the meaning of “implements, utensils or articles”

38. *Caledonian Railway Co v Banks* (1880) 1 TC 487 concerned the application of the wear and tear provisions of section 12 Customs & Revenue Act 1878 and their interaction with the tools rule. The company sought a deduction under section 12 for wear and tear on account of the depreciation of its rolling stock and machinery. This had been refused by the Revenue.

39. In calculating its chargeable profits the company had made in its accounts, and had been allowed, deductions for the "renewal and repairs of locomotive power, carriages, at wagons etc". That included the cost of the substitution of new locomotives carriages and wagons for those which were worn out. The company sought an additional deduction for wear and tear under section 12. The Revenue's decision not to allow that further deduction was upheld by the Special Commissioners on the basis that "any diminution in value by reason of wear and tear ... has been met by the [renewals and repairs deductions so that it was] not just and reasonable that any further deduction should be allowed [under section 12]."

40. The Court of Session confirmed the decision of the Special Commissioners. It held that because the amount allows as renewals and repairs represented the cost of maintaining the value of the company's rolling stock to the extent of, or in relation to, its usefulness for earning profit, it was not just and reasonable to allow a further deduction under section 12 for depreciation: the company could not “get a deduction for deterioration twice over”.

41. Of relevance to the present appeals are the comments made as to the basis on which the deduction for repairs and renewals had been made. The Lord Justice Clerk started by recognising that in determining the amount of profit, the outgoings necessary to attain that profit must be deducted and that the case related entirely to the mode of estimating that deduction. He said at 494:

> "This was originally regulated by the Rules of schedule D of the 1842 Act which provided what deductions were, and what were not, to be allowed in the case of expenditure on plant””

and quoted the provisions of Rule 3 of schedule D of the 1842 Act. He did not consider the provisions relating to the prohibition of deduction for capital items. He continued, "That substantially is the principle upon which from 1842 down to 1878 this calculation was made".

42. The Revenue’s calculation, he said, showed the process by which it had "endeavoured practically to apply the statutory provisions", and had "allowed deductions for repairs and renewal".

43. Lord Gifford concurred with the Lord Justice Clerk. He made no reference to Rule 3 of schedule D and said (at p499)

> “... The Special Commissioners ... have fixed the deduction for wear and tear on a different principle altogether from that contemplated by [section 12]. Instead of attempting to fix "diminished value by reason of wear and tear during the year" they have allowed the Company deductions of the actual sums expended by them for repairs and renewals, and, ... this sum can fairly be taken as making up the whole deterioration which the wear and tear of the year has occasioned. ... Instead of the Commissioners guessing that possible deterioration ... they have taken ... the actual sums expended in repairing and renewing the plant ... This is perfectly fair..."

44. The company, he said (at p500) could not get a deduction for deterioration twice over: once "for the actual expenses and then by deducting an additional sum for the same things".

45. Mr Hickey suggests that the failure of the court to comment upon whether the tools repair rule was applicable to larger capital items such as locomotives is indicative of the fact that it was accepted that the Rule should be construed as an express or implied authority for the deduction of the expense of renewal of such items.

46. I do not regard the judgement in this case as authority for the proposition that Rule 3 authorised a deduction for repairs and renewals of items such as railway stock. That is for the following reasons:

(1) the Lord Justice Clerk does not refer to the prohibition on capital items;

(2) he describes the deduction which was allowed as made pursuant to an endeavour to apply the statutory provisions practically: that indicates to my mind a suggestion that the deduction allowed by the Revenue was not in accordance with a strict construction of the tools rule;

(3) the issue as to whether Rule 3 authorised deduction (rather than merely prohibiting deduction in excess of actual expenditure) was not discussed. The basis on which the deductions had been given was not questioned. There was no consideration of whether or not Rule 3 applied to items such as rolling stock;

47. *Hyam v CIR* (1929) 14 TC 479 was heard against the background of Rule 3(d) Income Tax Act 1918 (which repeated the provisions of Rule 3 ITA 1842) . It was not argued before the Court of Session that a Rule 7 deduction for wear and tear of plant and machinery should be allowed. The case involved the reconstruction of a shop. The reconstruction involved the provision of new shop fittings. On appeal to the Court of Session the question was whether the net cost of that provision was deductible

48. Before the General Commissioners the Revenue had agreed that the fittings were "implements, utensils or articles" employed for the trade within the meaning of Rule 3(d). The Lord President (Clyde) found some difficulty in treating the shop fittings is falling within as falling within that phrase - a phrase which he said suggested what are "ordinarily known as loose tools". (Later also giving the example of expenditure on crockery, pots and pans by a hotel as an expense which would be a proper deduction from gross profits in the terms of Rule 3 (d) [at 486]). He proceeded however on the basis of the agreement by the revenue that the fittings were such implements etc. and said that it was against Rule 3(d) that the company’s claim should be judged. Lord Blackburn expressly reserved his opinion on this matter. Lord Sands and Lord Morison made no comment on the issue.

49. The General Commissioners had held that the cost of the fittings was capital and so not deductible. The Lord President Clyde did not conclude that this was correct, whilst the cost of “such supply was a proper charge against revenue in the books and a proper deduction from gross profits in the terms of [Rule 3(d)]”, he held that the expense incurred in the reconstruction was not "usually expended" and

therefore deduction was prohibited by Rule 3(d), saying: “The Rule only permits deduction of items “expended” for the supply repairs, or alteration of any implement, utensil or article to the extent of the sum actually expended”. In context I do not regard his use of “permits” to mean “authorises”.

50. Lord Sands considered Rule 3(d) and the prohibition on capital items in Rule 3(f). In relation to Rule 3(d) he said:

> "Now I think that Rule recognises that the repair of premises and the supply and repairs of implements etc are legitimate deductions from annual revenue, subject to this - and this seems to me and this seems to be what clause is specially designed to secure - that the allowance shall be no more than the average of the three preceding years."

51. But he said that one must view the provision as "subject to the usual distinction between capital and revenue expenditure". He did not think that it had been shown that the General Commissioners erred in holding that the expenditure was capital.

52. Lord Blackburn upheld the Commissioners decision on the basis that the expenditure was capital in nature. Lord Morison thought that the Commissioners were entitled to find the expenditure disallowed as capital and thought no question arose under Rule 3(d):

> "I think that the provision prohibition enjoined under section (d) is not against any deduction for recurring expenditure on repairs on and renewals, but is directed only against the deduction of a larger sum than is ascertained on a three year's average of such expenditure."

53. I do not regard the Court of Session’s reluctant acceptance of the concession that the shopfittings should be treated as implements, utensils or articles as authority that that phrase embraced items of that nature. Rather the Lord President's use of the phrase "loose tools" is to my mind indicative of his view of the nature of such items.

54. The quotation from Lord Sands might suggest that he viewed the Rule as authorising a deduction rather than merely prohibiting a deduction over and above actual (average) expenditure. But his later finding that the deduction was not available because the expenditure was capital indicates to my mind that he viewed the Rules as cumulative proscriptions on deduction rather than as authority for deduction..

55. The only clear relevant findings I am able to take from the judgement in this case are: (1) that capital expenditure, even if actually expended was not a permitted deduction, and (2) that such that items such as shop fittings were doubted as falling within "implements, utensils or articles".

56. *CIR v Great Wigston Gas Co* (1946) 29 TC 197 concerned deductions claimed for wear and tear and under the Renewals Practice in the context of Excess Profits Tax. Wear and Tear deductions had been claimed for gas holders, meters, cookers and gas fires but expenditure on the rest of the company’s plant and machinery was allowed under the Renewals Practice.

57. Somervell LJ, who gave the judgement of the Court, explained [at p206] that under the income tax code and Revenue practice the taxpayer had an option in relation to the cost of repairing and replacing plant and machinery: he could claim wear and tear deductions under Rule 6 (which replicated section 12 Customs & Revenue Act 1878) and if applicable obsolescence allowance under Rule 7 (replicating section 24 FA 18), or, as an alternative, claim the cost of renewals on the basis set out in the 1918 Command Paper. He then said [p 206/7] that there had been argument as to whether the Renewals Practice was an extra statutory concession or allowed under Rule 3(a) as money wholly and exclusively laid out or expended for the purposes of the trade or under Rule 3(d), although saying that it seemed clear that many renewals of plant and machinery would be claimable under Rule 3(d). Those statements indicate that he regarded both Rule 3(a) and Rule 3(d) as authorising deduction - or at least assumed that such was the case.

58. *Caledonian Railway* was cited to the court as an example of a wide construction of Rule 3(d). Somervell LJ suggested that by allowing the Renewals Practice the Inland Revenue were giving Rule 3(d) "a somewhat wider construction than it would otherwise bear". But he concluded:

> "on the view ... which we take, a substantial proportion of the deductions allowed for renewals are undoubtedly authorised by statute".

59. Those words may suggest that he considered that as regards the plant and machinery which was not gas holders etc the tools rule was a rule authorising a deduction rather than merely prohibiting certain deductions or that the deductions were permitted by the wear and tear rule. But there is no indication in this judgement as to how, or on what basis (wholly and exclusively, wear and tear or 3(d)) the "substantial proportion" was calculated or to which items it related, or whether or not those items were or not capital, or had been deducted in the commercial accounts.

60. Whilst Somervell LJ’s findings are dependent upon a conclusion that most of the expenditure was deductible under the statute, the reasoning for that conclusion (which reaches no set view on the extent of the tools rule) does not to my mind indicate that the Court considered: (1) that items such as gas holders fell within "implements, utensils or articles"; (2) that Rule 3(d) authorised a deduction rather than merely limiting any deduction to actual expenditure; or (3) that the Renewals Practice was a legitimate interpretation of Rule 3(d).

61. *Hinton v Madden* 1959 1 WLR 875 (1959) concerned the treatment of knives and lasts used by a shoe manufacturer. At this time capital allowances were available under sections 279 et seq ITA 1952.

62. Section 137 (d) and (f) ITA 1952 tracked the words of Rules 3 (d) and (f) of the 1918 Act. Section 16 FA 1954 permitted an additional allowance for capital expenditure on new plant and machinery. Section 16(1)(c) provided that expenditure would be treated as capital for the purposes of section 16 even if it had been allowed in computing taxable profit if it would be so treated for the purposes of the capital allowance provisions. The issues in the case were: (i) whether the knives and lasts

were plant and machinery – it was held that they were, and (ii) whether the expenditure was capital.

63. The majority, Lords Reid, Tucker and Jenkins, considered that the additional allowance under section 16 was available. Lords Tucker and Jenkins held that the expenditure was capital and addressed no argument to section 137(d), Lord Tucker saying that the question as to capital or revenue was to be judged "free from any consideration of how it has or should be dealt with" under section 137(d).

64. Lord Reid concluded that the expense was capital but said that this case was complicated by the fact that deductions "ha[d] been made under section 137(d)" [p886]. But although he thought that section 137(d) applied primarily to revenue expenditure he did not think that obtaining such a deduction was conclusive that the expenditure was not capital because: (1) section 137(f) was unhappily worded and the history of its application showed that it had been the custom to allow capital expenditure: it was "not at all clear that [section 137(d)] was intended only to be available in the case of revenue expenditure"; (2) section 16(3)(c) countenanced the possibility that it was nevertheless capital, and (3) there was doubt as to whether section 137 (d) had been properly applied.

65. Lords Keith and Denning in the minority said that the expenditure was revenue in nature: Lord Keith noting that it would be perfectly proper to describe the knives and lasts as implements utensils or articles, the expenditure on which could properly be charged as a deduction ([894]), and that section 137(d) "recognised" that the cost of repairs to machinery was a charge against revenue; and Lord Denning saying that the sum actually expended could be deducted because it fell within section 137(d).

66. Lord Reid was dealing with a case in which the expenditure had been allowed by the Revenue, not one in which the issue was whether it should have been allowed or was authorised by section 137(d) Whilst he may have assumed that such was the effect of section 137(d), he did not hold that it was. I do not see Lord Keith's statement that section 130(d) "recognised" a charge against income as being inconsistent with its being a prohibitive provision, and Lord Denning's view of the authority of section 137(d) was not necessary for his conclusion. Overall it does not seem to me that the speeches in this case compel the conclusion that section 137(d) authorised a deduction.

67. In *Brown v Burnley Football and Athletic Co Ltd* 1980 STC 45 Vinelott J considered the deductibility of the cost of the replacement of a stand at a football pitch. It was argued that the cost fell within section 130(d) TA 1970 (the successor of section 137(d)) and was revenue not capital. Vinelott J quoted section 130(d) and said:

> "These restrictions operate negatively: that is to say they are restrictions on an implicit right to deduct sums expended for repairs being of course sums which were wholly and exclusively laid out for the purposes of the trade... the effect of the words ... is to limit the deduction to sums actually expended during the relevant year of account ...".

He then proceeded to find that the replacement was not a "repair" and therefore not deductible. Having done so there was no need to consider whether the expense was capital or revenue.

68. It is not wholly clear whether Vinelott J considered that the “implicit right to deduct” arose: (i) from the fact that the expenditure was wholly and exclusively incurred for the purpose of the trade – and thus outside the restriction in section 130(a) – or (ii) because it was a repair within section 130(d), or (iii) because it was a sum which had been deducted in computing accounting profits or because repairs were naturally properly deductible as revenue items.

69. But if section 130(d) merely acts negatively, a finding that an expense is not a repair merely leaves at large whether it is a deductible expense on general principles. It thus appears that Vinelott J regarded section 130(d) as the only gateway to a deduction for the expense, and accordingly as the creator of the “implicit right to deduct”. But his recognition that the question of whether the expense was capital or not was potentially relevant indicated that he considered that if it were capital it would not be deductible despite the implicit authority of section 130(d): in other words that any implicit right drawn by implication from section 130(d) could be negated by other provisions.

70. As a result I am not able to draw from this case the proposition either that section 130(d) was merely prohibitory, or that it authorised a deduction. What is clear is that he considered that any right arising under section 130(d) was subject to the restriction on the deduction of capital expenses.

71. In *Jenners Princes Street Edinburgh Ltd v IRC* 1998 STC (SCD) 196, the Special Commissioners held that "actually expended" in section 74(1)(d) (the identically worded successor to section 130(d) meant truly expended in an accounting sense rather than on a cash basis.

Discussion

72. I deal first (a) with the question of whether or not section 74(1)(d) *authorises* a deduction and then (b) with the implements, utensils or articles question

(a) Does section 74(1)(d) authorise a Deduction?

73. The company argues that section 74(1)(d) authorises deduction of the costs of replacement of implements, utensils and articles. It says: (i) that such authorisation is in the words of the provision, (ii) that the authorities noted above indicate that such is the case, (iii) that such is its (implicit) effect notwithstanding that no expense appears for the cost in the commercial accounts and (iv) such is its effect whether or not those costs are capital in nature.

(i) The words of section 74(1)(d)

74. To my mind the words of this provision do not *authorise* the deduction of the costs of replacement of implements, utensils and articles. Paragraph (1)(d) is prefaced

by "no sum shall be deductible in respect of" and preceded and followed by a list of proscribed items. The tenor of the provisions is, as Vinelott J said in *Burnley*, to operate negatively to limit deduction rather than to provide for a deduction. The words admit the possibility that something outside the prohibition may be deductible but do more no more than that.

75. What is not prohibited by particular subparagraph of subsection (1) may be deductible, but is not made deductible by falling outside the prohibited description: it is deductible only if it is not proscribed by other provisions and is otherwise properly deductible. Thus for example an expense laid out wholly and exclusively for the purposes of trade which falls outside the prohibition in subparagraph (a) is not deductible merely because it falls outside that prohibition, and can notwithstanding that escape be not deductible - for example if it is a royalty within subpara (p). Paragraph (d) is no different in its effect.

(ii) The Authorities

76. I accept that in some of the judgements in the cases cited above there are suggestions that section 74(1)(d) or its predecessors authorised a deduction for expenses outside the prohibition. But in none of these cases was the question of whether or not section 74 actually authorised deduction at issue. Further in two of the cases the deduction being claimed appeared in the commercial accounts of the taxpayer (see *Caledonian* at 500 and *Hinton* at 880; the other reports are silent as to this issue); at best the cases provided acknowledgement that if an amount has been deducted for the actual cost of repairs etc section 74 does not require it to be disallowed. Nor is it clear to me that Vinelott J’s remark in *Burnley* suggested that a right is implicit in the section rather than in the overall scheme of the tax. And, on the other hand in the quotation from *Odeon* below Pennycuick J speaks of section 137 as an overlaying set of prohibitions on deductions already in the accounts.

77. I am therefore not persuaded that those cases compel a different conclusion from that I reach in (ii) above.

(iii) Deduction despite no expense in the commercial profit and loss account

78. Prior to the enactment of section 42 FA 89 Sir Thomas Bingham MR in *Gallaher v Jones* 1993 STC 537 quoted (at p 554) with approval the words of Pennycuick VC in *Odeon Associated Theatres Ltd v Jones1973 48 TC 257* when he said:

> "... first one must ascertain the profits of the trade in accordance with ordinary principles of commercial accountancy. That, of course involves bringing in as items of expenditure such items as would be treated as proper items of expenditure in a revenue account made out in accordance with the ordinary principles of commercial accountancy. Secondly, one must adjust to this account by reference to the express prohibitions contained in the relevant statute, those now being contained in section 137 of Income Tax Acts 1952.” (later recognising any other “express statutory adjustment”).

79. That principle seems to me to have been given statutory form by section 42 FA 89 which is set out above.

80. Thus if one wishes to deduct a particular item the first step is to see if it is deducted in the commercial accounts of the trade; if it has been, the second step is to see if its deduction is prohibited and the third step, if the first two do not result in a deduction, is to see if there is any express provision under which deduction is required.

81. The expenses of the replacement of the trailers and tractor units were not deductions in the commercial profit and loss account of the Appellant. As a result it is only if there is some express or implied provision which requires their deduction that they may be deducted. The only provision upon which the Appellant relies on is section 74. The company notes that Bingham MR in *Gallagher* described (at 555j-h) the adjustments to be made to the commercial accounts as flowing from any express or implied statutory rule and asserts that section 74(1)(d) provides an implied rule that renewals expenditure is deductible. It so argues for the following reasons.

82. (1) That the effect of the provisions in CTA 2009 is expressly to allow such deduction and since CTA 2009 was intended merely to restate the law, section 74 must have the same effect.

83. I do not accept the premise of this argument for reasons I shall turn to shortly. Nor do I accept the logic: it seems to me that even if CTA 2009 has the effect for which the Appellant contends that may be evidence of what its creators thought was the previous law, but is not relevant to the proper construction of the prior law.

84. (2) That by denying a deduction for amounts beyond those actually expended, the section implicitly permits deduction for expenditure up to that point.

85. In my view the provision recognises that such amounts may be deductible but does not authorise the deduction of sums which are not deducted in the commercial accounts.

86. (3) That if a deduction for replacement cost is available only when such amounts have been deducted in the commercial profit and loss account, section 74(1)(d) would be otiose because: (1) any amounts treated as revenue in the commercial accounts would be deductible anyway, and (2) amounts treated as capital for accounting purposes (and therefore left out of the computation of revenue profits) would never be deductible. In this connection they say that section 74(1)(d) must be interpreted as authorising deduction for capital expenditure because: that was HMRC's practice; that is how it is restated in section 68 CTA 2009, and that is how the courts applied it. If section 74(1)(d) could not provide a deduction for items which were not treated as revenue in the accounts it became redundant.

87. On the view I take of the proper construction of section 74(1)(d) it is merely prohibitive. If there are items in the commercial accounts which for some reason exceed the sum actually expended their deduction is disallowed by it: it is not redundant. The fact that HMRC may have allowed - either under the Renewals

Practice or by reference to some generous interpretation of section 74(1)(d) – the deduction of capital expenses is irrelevant. The view taken by Parliament in 2009 is not conclusive as to the meaning of the provision, particularly given the differences between section 68 CTA 2009 and 74(1)(d). And in my judgement that is not how section 74(1)(d) was *applied* by the Courts.

(iv) Deductible even though capital in nature

88. It was common ground that the company's expenditure on the tractor units and trailers was capital in nature. But HMRC did not argue that a deduction for the expenditure was proscribed by section 74(1)(f). Indeed they appeared to me to assert that section 68 – which authorised a deduction for and only for capital expenditure had not marked a change in the law. In my view if that was their assertion, it was wrong.

89. I am not persuaded by the authorities that section 74(1)(d) authorises the deduction of capital expenditure. There is nothing in it which indicates that it overrides 74(1)(f). That it did not so authorise such a deduction was the ground of the decision of three of the four judges is the Court of Session in *Hyam*; and for the reasons set out above it does not seem to me that the speeches in *Hinton* or the judgement in a *Wigram* indicate that section 137(d) authorised the deduction of capital sums. Whilst the cost of trains and wagons in *Caledonian Railway* seems fairly clear to be capital in nature, there was no discussion in that case of the restriction on deduction of items of capital nature.

90. Neither am I persuaded that the view taken by Parliament in enacting section 68 CTA 2009 - namely that the provision applied to give relief in relation to items of a capital nature - and only of a capital nature - is relevant to the construction of section 74 before 2009. It seems to be quite possible that the enactment of section 68 reflected the long established practice of HMRC in giving section 74 "a wider interpretation than it would otherwise bear".

Conclusion – section 74(1)(d)

91. I find that for the accounting period ending 31 December 2008 no deduction for the costs of the tractors and trailers was authorised by section 74(1)(d) and none is available since no deduction for those costs appeared in the commercial accounts of the trade. Further I find that the costs are not deductible as they are capital in nature.

(b) Implements, utensils or articles

92. If I am wrong and section 74(1)(d) authorises a deduction for expenditure on implements, utensils and articles even if that expenditure is not a deducted in computing the commercial accounts profit, or it is capital in nature, the question arises as to whether the tractor and trailer were implements, utensils or articles.

93. The company argues that the tractor and trailer units were implements, utensils or articles within section 74(1)(d). It says that:

(1) whether or not an item falls within these words is not limited by any condition as to size or standard;

(2) neither is there any limitation by reference to cost or frequency of replacement;

(3) the use in the statute of "any" before "implements, utensils or articles" is significant: it indicates an unrestricted meaning;

(4) the Shorter Oxford English dictionary definition of “implement” includes “a piece of equipment” and that of "article" a "particular thing"; those definitions clearly encompass tractor and trailer units;

(5) in particular the Shorter Oxford English dictionary defines "implement" as a thing used to apply manual force to an object or designed for some particular mechanical function in a manual activity. Those words clearly encompass the use of the units in the transportation of goods;

(6) the purpose of the provision is to afford relief for a wide range of trades and the words should be construed with that purpose in mind;

(7) items within “implements, utensils or articles, must include those capable of "alteration": that indicates items of a complex nature and not limited to items such as spanners or beer glasses. Otherwise "alteration" would be redundant";

(8) the object of section 74 is to give relief to capital items - items of enduring benefit – “implements, utensils and articles” should be construed widely so as to permit such relief;

(9) The fact that *Caledonian* accepts that trains and coaches could be "implements, utensils or articles" that indicates the breadth of the words; and

(10) section 41 TCGA contains no suggestion that the assets to which section 74 applies be small and relatively inexpensive.

94. HMRC argue:

(1) that the words, which have a degree of overlap, suggest items which might be used manually or as part of some mechanical process;

(2) the authorities suggested items such as loose tools (*Hyam*), knives, lasts (*Hinton*), not items such as lorries or machines with a long life; or other larger items shop fittings are not implements, utensils or articles;

(3) "articles" suggests something which is part of a set as in an “article of furniture”; and

(4) the words carry a sense of small degree or scale.

Discussion.

95. For the reasons which follow I consider that the tractor and trailer units were no implements, utensils or articles..

96. The authorities give little assistance. I do not consider that *Caledonian* provides guidance that items such as engines and carriages can fall within the statutory words.

The dicta in *Hyam* indicate what may clearly fall within the statutory words - loose tools, beer glasses etc - but gives no clear indication of what does not.

97. The Shorter Oxford English dictionary gives the following meanings:

> "implement" as "a tool, instrument, or utensil, employed in a particular trade, activity etc";
>
> "utensil" as "an implement, vessel, or article"
>
> "article" as a particular item ... a particular thing (the specified class); a commodity; a piece of goods or property.

98. That dictionary defines "tool" (which appears in its definition of "implement") as

> 1. A thing used to apply manual force to an object or material, especially a device designed for some particular mechanical function in a manual activity, as a hammer, a saw, a fork; an implement. Now also, a powered machine used for a similar purpose
>
> 2. A thing ... used in the carrying out of some activity, occupation or pursuit; a means of effecting a purpose of facilitating an activity."

99. As can be seen there is a degree of circularity in these definitions. I do not find them peculiarly helpful.

100. To my mind as a matter of ordinary English usage the trailers and tractor units (of all the 7 descriptions in this case) do not fall within these words. I do not intend to provide a definition of the words or to set out precise limitations on their ambit. I consider their meaning is illustrated (but not defined) by considering the use and qualities of things which clearly fall within the envelope of the words and recognising that something else will generally also fall within them if it shares sufficient of the characteristics of the things which are clearly within the words, and that generally it will fall out if it does not. The following (a non exhaustive list) fall clearly to my mind within the words:

> hammers, screwdrivers, nail clippers, hairbrushes, cheese graters
>
> > - all portable items by which manual force is transmitted to some substance to change it or its state;
>
> pens and paint brushes
>
> > - portable items used to create or change the state of something (such as paper or ink)
>
> measuring cylinders, rulers and electric meters
>
> > - all portable items used to measure something
>
> drills and drilling machines, sanding machines, lathes
>
> > - larger machines which do or aid a task which generally could be done manually

clothing

- movable items which cover or insulate

spades, forks, brushes, chisels

- portable items which are used in making or preparing things

Glasses. Plates, table linen

-portable items used to contain or cover something.

101. It seems to me that the trailer and tractor units do not share sufficient features these items to suggest that they fall within the words. There are large. They do not measure. They do not transmit manual force to a substance or assist in its transmission. They do not perform a function in the making of a product. They do not cover or insulate. They are not portable. Their function is to transport, not to make or alter. I would not describe them as designed for a function in a manual activity.

102. I do not agree that "any" requires an extended meaning of the words. I accept that the words can apply in any trade, but that does not require an extended meaning, merely a search in the activity of the trade for such items as are used within it. Some of the articles which will fall within the words will be alterable – for example clothing – others will not; the ability to be altered does not require a complex nature. Since I do not consider the purpose of section 74(1)(d) to be to give relief for capital expenditure I do not consider these words should be construed so as to encompass items of enduring benefit to the trade. For the reasons I set out below, I do not find the provisions of TCGA instructive.

103. I accept that some things may lie on the edge of the compass of these words: there are some items in relation to which one may hesitate before saying they fall or do not fall within it. But it seems to me that the items in this case fall clearly outside that compass and that anxious consideration is not needed.

104. As a result I find that a deduction is not available in respect of the items even if section 74(1)(d) authorises a deduction for items the expense of which is not included in the calculation of commercial profit and loss or which is capital in nature.

(2) The remaining periods: those ending 31 December 2009, 2010 and 2013

105. The remaining periods were governed by CTA 2009. The following statutory provisions were relevant to the arguments advanced in relation to the disputed expenditure in these periods:

106. Section 46

> "(1) The profits of a trade must be calculated in accordance with generally accepted accounting practice, subject to any adjustment required or authorised by law in calculating profits for corporation tax purposes..."

I shall refer to profits so calculated as "GAAP profits"

107. Section 48 - Receipts and expenses

(1) In the Corporation Tax Acts, in the context of the calculation of the profits of a trade, references to receipts and expenses are to any items brought into account as credits or debits in calculating the profits.

(2) It follows that references in that context to receipts or expenses do not imply that an amount has actually been received or paid.

(3) This section is subject to any express provision to the contrary.

108. Section 51 - Relationship between rules prohibiting and allowing deductions

(1) Any relevant permissive rule in this Part -

(a) has priority over any relevant prohibitive rule but

(b) is subject to [certain presently irrelevant sections]

(2) In this section any "any relevant permissive rule in this Part" means any provision of -

(a) Chapter 5 [which includes section 68] ... which allows a deduction in calculating the profits of the trade…

(3) In this section "any relevant prohibitive rule", in relation to any deduction means any provision of this Part ... which might otherwise be read as

(a) prohibiting or deferring the deduction, or

(b) restricting the amount of the deduction.

109. Section 53 - Capital expenditure

(1) In calculating the profits of a trade, no deduction is allowed for items of a capital nature.

(2) Subsection (1) is subject to provision to the contrary in the Corporation Tax Acts.

110. Section 68 - Replacement and alteration of trade tools

(1) This section applies if -

(a) expenses are incurred on replacing or altering any tool used for the purposes of a trade, and

(b) a deduction for the expenses would not otherwise be allowable in calculating the profits of the trade because (and only because) they are items of a capital nature.

(2) In calculating the profits of the trade, a deduction is allowed for the expenses.

(3) In this section "tool" means any implement, utensil or article."

<u>The parties' arguments.</u>

111. In outline the company argues that the cost of replacing the tractor units and trailers were "expenses incurred" within section 68(1)(a), and that the only reason

such expenses would not be not otherwise deductible was that they were of a capital nature. Thus section 68 authorises their deduction. It says that, having regard in particular to the decisions of the Courts in relation to the predecessors of section 68, the tractor units and trailers were tools of the trade.

112. HMRC argue:

(1) that the cost of the tractor and trailer units was not taken into account in computing the GAAP profit;

(2) accordingly, there was no debit in respect of the expenditure in the computation of the profit in those accounts (I shall call such a debit a "GAAP Profits debit");

(3) as a result of section 48 that meant that for the purposes of the Corporation Tax Acts there was no "expense" in respect of the expenditure; and

(4) as a result section 68 could not authorise a deduction because there was no "expense" incurred on replacing tools; and

(5) further, as they said in relation to section 74(1)(d), the trailer and tractor units were not "tools", as defined.

113. I note that in relation to the section 74 period HMRC did not base their argument on the absence of a debit despite the provisions of section 46 FA 98 which, like section 48 identifies expenses with debits in computing the profit. That, as I understand the argument, was because section 74 related to "expenditure incurred" whereas section 68 speaks of "expenses" having been incurred.

114. The company says that HMRC's submissions that "credits" and "debits" in section 48 are restricted to those which appeared in calculating the GAAP profit, and that "expense" is restricted to such a debit are wrong for the following reasons:

(1) section 48 speaks of credits and debits being "brought into account", not brought into <u>the</u> account<u>s</u>". The section does not say that the references to expenses are items brought into account as accounting debits;.

(2) section 48 relates to the "calculation of the profits of the trade": those are the profits on which corporation tax is born (section 35 CTA). By section 46 they are the profits after any adjustment authorised by law, not the GAAP profits; the debits and credits referred to in section 48 are therefore "tax debits" - those brought into account in calculating taxable profits (and so after the operation of section 68). Thus an "expense" for the purposes of section 68 includes the deduction mandated by section 68. As a result the deduction is available;

(3) elsewhere in the Corporation Tax Acts there are provisions which expressly define debits and credits or refer to tax debits and credits, and provisions which would be otiose if credits and debits meant GAAP accounts credits and debits;

(4) section 48(3) provides that subsection (1) is subject to any express provision to the contrary. Section 68 is such;

(5) section 68 does not refer simply to "expenses" but "expenses incurred". That indicates that what is referred to actual costs not GAAP accounts debits;

(6) when section 68 was repealed by section 72 FA 2016 transitional rules included in section 72(4) provided that the repeal of section 68 had effect in relation to -

"expenditure incurred" after 1 April 2016;

“expenditure incurred” must be synonymous with "expenses incurred” in section 68: that indicates that section 68 is concerned with actual expense not accounting debits;

(7) section 48 originated with section 46 FA 1998 which was headed "minor and consequential provisions about computations". Having regard to that heading section 48 cannot oust the effect of sections 46 and 68 which is that the GAAP profit must be adjusted by the section 68 deduction to obtain taxable profits;

(8) the explanatory notes to CTA 2009 indicate that the section 68 deduction relates to actual expenditure not to GAAP accounts debits: “9. The allowance pre-dated the capital allowances regime and applies to expenditure incurred…”;

(9) the way in which section 41 TCGA describes and deals with renewals allowances requires that (section 74(1)(d) and) section 68 be construed as referring to actual expenditure;

(10) if "expense" is limited to GAAP accounts debits, section 68 is redundant because any capital item would not be written off in the GAAP accounts and so no "expense" would be incurred on which section 68 (which relates only to capital costs) could operate. Even if a capital item were written off only in part in the GAAP accounts the availability of deduction would be dependent on the vagaries of accounting policy. That cannot have been intended; and

(11) the object of the Tax Rewrite Project which gave rise ot CTA 2009 was not to change the law. That is confirmed by the long title to the Act: the long title is a plain guide to the general objectives of the statute: *Black-Clauson International* 1975 AC 591 at 647F). Prior law was that such items would be deductible. Section 68 should be construed so that they remain so.

Discussion

115. I take the Appellant’s arguments in turn

116. (*1) “brought into account”*. To my mind the words "debits and "credits" in section 48 refer only to accounting debits and credits. I do not think it would be a normal use of language to refer to adjustments made to GAAP profits to arrive at taxable profits as credits or debits. The words in "brought into account" indicate that the sums are part of the calculation of profit and do not suggest something wider: debits or credits are "brought into account” in the computation of GAAP profits.

117. (2) *Tax debits* The argument that section 68 is an adjustment required by law so that "expenses" must include the tax debits and credits created by it is circular. The argument runs only if "expenses" in section 68 includes a deduction mandated by section 68.

118. The company's argument was also put in a slightly different way:

(1) section 46 CTA specifies GAAP profits as the starting point for the calculation of taxable profits but is subject to any adjustment required by law. Thus they say that the words "profits of the trade" (being a figure on which corporation tax is payable) is the GAAP profit after such adjustment.

(2) Section 68 authorises the deduction of a capital replacement expense. It is a permissive rule within section 51 and therefore overrides any prohibitive rule (see section 51(1));

(3) if section 48 had the effect of restricting the allowance available by reason of section 68 it would therefore be overridden by virtue of section 51;

(4) thus if section 48 requires "expenses" in section 68 to be read as limited to debits in computing GAAP profits (which would mean that there would be no deduction of the disputed expenses because there was no such debits and the gap profit occupation) it must give way to section 68 with a result that in effect "expense" should not be read as so limited in section 68.

119. This argument is also circular. It requires that one starts with the proposition that section 68 gives rise to a deduction and its logic then requires the deduction.

120. (3) *Other statutory provisions in the Corporation Tax Acts*. The company refers to various sections of Chapter 5 Part 3 which expressly authorise deductions in computing taxable profits. It says that if the word "expenses" as used in those sections was restricted to GAAP profit debits then the provisions would have little or no meat - either because no GAAP profit debit would be recognised to which the relevant sections might apply, or because if one was recognised it would be allowable (or its deduction not proscribed) on general principles. As a result it says "debits" must be read as "tax debits" - those items made deductible by the relevant provisions, and "expenses" as including those tax debits. The provisions of CTA 2009 to which the company referred are the following:

(i) Section 61 CTA which relates to pre-trading expenses and requires that such expenses to be deducted as if incurred at the start of the trade.

It seems to me that limiting the meaning of expenses to GAAP profit debits does no violence to the intention of this section which is to treat such debits as arising, and so being deductible, once trade has started.

(ii) Sections 62 to 67 which treat a trader who occupies a lease in relation to which a premium (or the like) has been paid (and taxed) as "incurring an expense of a revenue nature" equal to a proportion of the premium. These provisions specifically provided for the deduction of the expense.

It seems to me that any general limitation "expenses" to GAAP profit debits by section 48 is ousted by the express words of these provisions. Section 48 cannot apply by virtue of section 48(3). There is no conflict or anomaly.

(iii) Section 69 which authorises a deduction "for a payment" for a restrictive covenant.

This section makes no reference to expense. The meaning of "expense" is irrelevant to its operation. It cannot bear on the construction of section 48.

(iv) Section 82 which applies where a company has incurred "expenses in making a contribution to a local enterprise organisation" and a deduction would not otherwise be allowable for the expense.

I see no lack of intended force in this provision if "expenses" are limited to GAAP profit debits. It seems quite possible that such a contribution may be debited in computing GAAP profits and yet, absent this provision, not be deductible for tax purposes because for example it was capital in nature or not made wholly and exclusively for the purposes of the trade.

(v) Section 87 which authorises a deduction if a trader "incurs expenses of a revenue nature on research and development related to the trade".

The restriction "expenses" to GAAP profit debits would seem to me to have little effect on this provision whose ambit is expressly restricted to items of a revenue nature.

(vi) Sections 89 which authorises the deduction of "expenses incurred" in applying for patents (section 90 makes similar provision for trademarks).

I accept that if in GAAP accounts such expenses were capitalised, the effect of HMRC's construction of section 48 would be to deny a deduction in the computation of the trading profits of the company for those costs. But Part 8 CTA 2009 provides a separate code for the relief of such costs and I see no anomaly in their exclusion from the general provisions of Part 3.

121. I am therefore not persuaded that HMRC's construction section 48 would deprive these provisions of purpose.

122. The company also argues that elsewhere in CTA 2009 the Act: (a) uses the terms "debit" and "credit" to mean an amount determined for tax purposes (which Mr Hickey christened "a tax debit" or a "tax credit") rather than the debits and credits which arise in the computation of GAAP profits and (b) includes express provision that "debits" and "credit" mean those drawn from GAAP profit computation. These, it says, indicate that the use of those terms in section 48 is not confined to GAAP profit debits. The company gives a list of examples of such provisions.

(i) The Loan Relationship rules in Part 5 expressly provide (section 307 (2)) the general rule that the amounts to be brought into account as debits and credits are those recognised in determining GAAP profits; they then provide extra rules for the modification of those debits and credits to determine those which are to be brought into account - that is to say to produce what may be called tax debits and credits.

I accept that the result of succeeding provisions of the Loan Relationship code is that the effect of sections 297 to 301 is that only those debits and credits determined by those later provisions are to be treated as receipts and payments to be brought into account in calculating taxable profits, and thus might be viewed as a species of tax credit or debit. But the structure of these provisions starts with debits and credits; by contrast the structure of Part 3 starts with profit and there is no modification of debits and credits in its provisions, merely the adjustment of deductible expenses. It does not seem to me that this structure or the express allusion to GAAP profits in section 307 indicates that debits and credits in section 48 mean some form of adjusted tax debits and credits.

(ii) Chapter 3 Part 8 provides for "debits to be brought into account for tax purposes in respect of" intangible assets. Sections 728 and 729 provide that where expenditure on an intangible fixed asset is written off in the accounts or amortised a "debit must be brought into account for tax purposes".

Thus, the company says, this Part recognises that the debit is a tax debit which may, but also (by virtue of later provisions in the Part) may not, be the same as a GAAP profit debit.

This does not indicate to me that elsewhere in CTA "debit" also means a tax debit. As with the Loan Relationship provisions accounting debits and credits are adjusted to create those which are "to be brought into account", and by sections 745 to 751 those particular debits are given effect. The structure of the Part gives a particular meaning to the terms and that structure is not present in the general rules of Part 3.

The company says that its interpretation is supported by section 865 of Part 8 which applies "if a debit is ... recognised ... for accounting purposes". It says that that is about quantifying a debit rather than about what a debit is. I disagree. The provision sets a condition for whether a debit "could be brought into account for the purposes of" the Part: that condition is that there be accounting debits. The words underline the distinction between "debits brought into account" and accounting debits. That distinction is not there or needed in Part 3.

(iii) The derivative contract rules in Part 7. The company makes the point that section 595(2) speaks of the debits or credits to be brought into account and indicates that these are those recognised in the GAAP profits. As with Part 8 I accept this indicates a difference between debits and credits to be brought into account and those which arise in the computation of the GAAP accounts. But that is by virtue of these specific provisions and does not support the same construction of Part 3.

(iv)Section 89 CTA I have discussed this above.

(v) Section 999 CTA applies where a company "incurs expenses in setting up an SAYE scheme, and authorises a deduction for those expenses.

The company says that such expenses would be capital and would not otherwise be allowed. If "expenses" were limited to accounting expenses list in this section would have little benefit.

But that contention assumes that for accounting purposes the expense would be capitalised and not debited in computing GAAP profits. It does not seem to me impossible - although there was no evidence on the point - that such expenses could be written off when incurred. If so there would be GAAP debits. But even if the expenses were capitalised for GAAP purposes I see no reason why section 999 should be treated as authorising a deduction.

(vi) Section 1000 authorises a deduction for the "expenses" of setting up an employee share ownership trust. The company says these expenses are capital in nature so that restricting "expenses" to accounting debits would render the provision nugatory.

For the same reason as in relation to section 999, I disagree.

(vii) In Part 16 (Expenses of Management), section 1255 defines "debits" and "credits" as those terms are used in sections 1225 to 1227 as GAAP profits debits and credits. The company says that the absence of such a definition in Part 3 indicates that the same is not intended.

But Part 16 is concerned not, as Part 3 is, with trade, but with expenses of management. The section 48 debits and credits arise from the trading GAAP profits. There needs to be express provision in relation to nontrading accounts.

(viii) Part 13 authorises deductions for research and development "expenditure". Section 87 is entitled "expenses of research and development"; the company suggests that that indicates that "expenditure" means the same as expenses.

I disagree. The terminology and Part 13 is centred on "expenditure". I see no reason to equate that with “expense”.

123. The company says that the provisions in relation to which these issues occur are not limited to those in the examples. I have not conducted further research into the Act but it seems to me that on the basis of the examples given that there is nothing in the Act would suggest that HMRC’s interpretation of section 48 is wrong.

124. *(4) Section 48 is subject to provision to the contrary : 48(3*). It does not seem to me that section 68 is a provision to the contrary within section 48(3). It makes no reference to debits or credits

125. *(5) "expenses incurred"; not “expenses*”. It seems to me that a debit can properly be described as "incurred". It is born in computing profits. "Incurred" indicates the suffering of the effect of something and need not refer only to a cash payment.

126. *(6) The section 72 transitional provisions.* I see no anomaly arising from treating “expenditure incurred” in section 72(4) as having a different meaning from “expenses” in section 68. The effect of so doing is that if there was expenditure before 1 April 2016 a deduction for the expense (the debit) was allowable for periods ending both before and after that date, but if the expenditure was incurred after 1 April 2016 no deduction for the expense (no debits) is available.

127. Even if I were wrong in this I do not find later statutory provisions are a good guide to the meaning of earlier ones.

128. *(7) Section 46 FA 98 was a minor or consequential provision.* On the view I take a section 74(1)(d), section 46 makes no difference to its application. Thus it has in this regard no effect. That is consistent with its "minor and consequential" heading.

129. *(8) The Explanatory Notes.* In *R(oao Westminster City Council) v National Asylum Support Service* [2002] UKHL Lord Steyn said in relation to the process of statutory interpretation:

> “ In all cases the object is to see what is the intention expressed by the words used ... the meaning of words varies according to the circumstances with respect to which they were used ... again, there is no need to establish an ambiguity before taking into account the objective circumstances to which the language relates. Applied to the subject under consideration result is as follows. In so far as the Explanatory Notes cast light on the objective setting or contextual scene of the statute, and the mischief at which it is aimed, such materials are therefore always admissible aids to construction. They may be admitted for what logical value they have ..."

130. The use of the words "expenditure incurred" in the Explanatory Notes for the section 68 indicates that, as the notes themselves say, the section was intended to be “based on” section 74(1)(d). But that section had already been interpreted as meaning that expenditure incurred was that which appeared in GAAP profit and loss account (see *Jenners*). It therefore does not seem to me that the context described by those notes indicates that "expenses" need mean anything other than the debits or credits in the GAAP accounts.

131. *(9) Section 41 TCGA* Section 39 TCGA excludes expenditure allowable in computing the profits of a trade from the computation of a capital gain, but this rule is subject to section 41 which provides that section 39 shall not exclude "expenditure in respect of which capital allowances or renewals allowance is made". Section 45(5) TCGA defines renewals allowance as meaning a deduction allowable in computing in the profits of a trade -

> "by reference to the cost of acquiring assets ... in replacement of another asset."

132. This, the Appellant says, indicates the TCGA recognises the concept of Renewals Allowances and that they may provide for deductions and computing trading profits. The references in section 41 to "expenditure" and “cost” recognise that the Renewals Allowance is given by reference to expenditure and that "expenses" in section 68 must therefore mean the actual cost or expense incurred on "tools".

133. I do not consider that section 41 is relevant to the construction of section 68 CTA 2009. It uses different words and plainly has a wider reach - for its provisions clearly cover items of revenue nature as well as those of a capital nature. A question arises as to whether a deduction be given "by reference to the cost of acquiring assets" includes deduction under section 68, but I see no reason why a debit in the GAAP

accounts should not be regarded as such a cost. Thus I see no limitation in the efficacy or purpose of section 41 occasioned by treating "expenses" in section 68 as limited to GAAP accounts debits.

134. *(10) redundancy.* The company says that section 68 concerns itself with capital items; but if a cost is capital in nature it will not be deducted in computing the GAAP profits. Thus the section has no effect on HMRC's interpretation.

135. Mr Baldry accepts that the potential ambit of section 68 is small, being limited he says to the cost of items which from the tax point of view are of a capital nature but which from an accounting perspective are nevertheless properly debited in calculating profit for the year. He gives as an example immaterial costs taken as a debit in computing GAAP Profits.

136. It seems to me that a cost which form a tax perspective is capital, being intended to secure an enduring benefit, is written off in the GAAP accounts because the benefit is irrecoverable or because it appears that it is unlikely to result in future benefit. I accept that on the interpretation I favour the scope of the provision is limited but it does not seen to me to be illusory.

(11) Prior legislation etc. Although the title of CTA 2009 is "An Act to restate, with minor changes, certain enactments relating to corporation tax; and for connected purposes" and the Explanatory Notes to section 68 indicate that "it is based on that part of section 74(1)(d) ... which relates to deduction for the replacement ("supply") or alteration of [tools]" there are a number of differences between the words of the provisions which persuade me that although section 68 is "based on" section 74(1)(d) it does not replicate its effect:

(1) section 74 relates to the "supply, repairs or alteration" of tools whereas section 68 relates only to "replacing or altering" tools. The word "repairs" has disappeared and "replacement" has taken the place of "supply"; The Explanatory Notes indicate that the excision of "repairs" was made because it was considered that repair expenditure would be deductible in any event on general principles; and that "supply" had been construed as "replacement".

(2) section 68 is limited to items which are of a capital nature. Given my earlier conclusion that any deduction permitted by section 74(1)(d) would be disallowed if capital in nature by section 74(1)(f) I believe that this is a change in the law although it appears to embrace at least part of the Renewals Practice;

(3) section 74 contained a prohibition on sums exceeding those actually expended which is a missing from section 68.;

(4) section 68 is an express authorisation of deduction, at best section 74(1)(d) is an implicit authorisation; and.

(5) section 68 referred to "expenses"; whereas section 74 to "sums expended".

137. Further even if section 68 were designed to replicate the effect of section 74(1)(d) I have concluded that no deduction would arise under the provision of that section even if it applied to capital expenses.

138. For these reasons I reject the arguments of the Appellant and prefer the submission of HMRC. I conclude that because no debit was recognised in the company's GAAP profit and loss account for these costs no deduction under section 68 is available.

Tools

139. The definition of "tools" in section 68(3) makes its meaning the same as implements, utensils or articles in section 74(1)(d). My conclusion in relation to those words in that section was that the tractor and trailer units did not fall within them. For the same reasons they do not fall within "tools".

Conclusion

140. I conclude that "expense" in section 68 is limited in meaning to a debit in the GAAP accounts. No such debit was made in respect of the disputed expenditure. No deduction is available. Further the units were not tools for the purpose of section 68(3) so no deduction is available.

PART 2: Para 51A

141. Paragraph 51 Sch 18 FA 1998 provides that if a person has paid an amount of tax which he believes was not due, that person may make a claim to HMRC for its repayment. But para 51A provides that HMRC are not liable to give effect to such a claim where, among other possibilities, Case G applies. That is to say where:

> "(a) the amount paid, or liable to be paid, is excessive by reason of a mistake in calculating the claimant's liability to corporation tax, and
>
> (b) liability was calculated in accordance with practice generally prevailing at the time."

142. In *HMRC v Household Estate Agents Ltd* [2008] STC 2045, Henderson J considered the effect of similar words in paragraphs 45 schedule 18 FA 1998. In relation to the meaning of "practice generally prevailing" he said this at [58]:

> "Without attempting to give an exhaustive definition, it seems to me that a practice may be so described only if it is relatively long established, readily ascertainable by interested parties, and accepted by HMRC and taxpayers' advisers alike."

143. In *Boyer Alan Investment Services Ltd v HMRC* [2012] UK FTT 558, Judge Berner gave further consideration to the elements identified by Henderson J in *Household Estate Agents.* He said:

> (1) to be ascertainable required that the practice was not inchoate and that it be sufficiently precise and devoid of uncertainty in its application [34];
>
> (2) although a published statement of practice was the paradigm of an ascertainable practice, it was possible for a practice to be ascertainable if settled,

defined and agreed between, or communicated between, taxpayers or otherwise sufficiently identified to the outside world [35];

(3) a published practice was likely to be capable of being regarded as having become generally prevailing over a shorter period than one merely established in practice [36];

(4) an internal practice of HMRC would not be generally prevailing until it could be identified with reasonable clarity and precision by taxpayers [37];

(5) that quality of clarity and precision must be present in the understanding of HMRC and taxpayers alike [38];

(6) in order for the practice to be "generally" prevailing it must have been adopted by HMRC and generally, but not universally, by the taxpayer community [38];

(7) the practice would not be settled if it was not applied in a consistent manner.

144. As Mr Baldry accepted, in this appeal the burden of proof in showing the the existence of a generally prevailing practice rested on HMRC, being the party which wished to assert that the bar in Case G applied.

145. The company made its original corporation tax return for 2008 without making any claim that the expenditure on the trailer and tractor units was deductible in completing its taxable profits, and treated that expenditure as eligible for capital allowances. If I am wrong and section 74(1)(d) did authorise a deduction for those costs, the costs would not have been eligible for capital allowances (section 4(2) Capital Allowances Act 2001) and the company would have made a mistake in calculating its liability to corporation tax. As a result the requirement of paragraph (a) of Case G would be satisfied.

146. As to paragraph (b) of Case G, the practice generally prevailing at the time, HMRC say that at the time the company filed its corporation tax return, namely 21 December 2009, the practice generally prevailing in relation to replacement assets where capital allowances had been claimed in relation to the original asset was that capital allowances would be claimed on all significant plant machinery and no deduction would be claimed under section 74(1)(d). As a result paragraph (b) applied and HMRC would not be liable under the claim because the company had claimed capital allowances on the tractors and trailers rather than a deduction for their costs.

147. The company says that:

(1) para (b) of Case G refers to the "practice prevailing at the time". It suggests that this is at the time the tax was paid by mistake but says that establishing prevalence requires a broad sweep of time;

(2) established practice may not mean just established among road hauliers;

(3) HMRC must show that the practice was generally prevailing in the sense described in *Boye;*.

(4) A casual straw poll of HMRC's staff cannot establish generally prevailing practice; and

(5) section 41(4) and (5) TCGA recognise the availability of a renewals allowance alongside capital allowances and thus indicating prevailing practice different from that which HMRC contend.

Para 51A: The Evidence and Findings of Fact.

148. I heard oral evidence from Raphael Hussain, one of HMRC's officers, who, from 2017, had been responsible for updating that part of HMRC's manual which related to repairs and renewals.

149. Mr Husain exhibited various pieces of guidance published by HMRC since 2003 -

(1) guidance published in 1995 (and available online from 2006 to 2018) which spoke of section 74(1)(d) as being statutory authority for the deduction of renewals costs of "small assets" such as loose tools. (This is termed the "statutory renewals basis: I retain that description despite my earlier conclusion as to the effect of section 74(1)(d)). The guidance indicated that the allowance was extended beyond the narrow range of section 74(1)(d) on which it termed the “non statutory renewals basis” and I have called the Renewals Practice. It said that a claim to use the non-statutory Renewals Practice could be allowed if certain conditions were fulfilled. Those included a condition that no capital allowance had been claimed for the original asset which was being replaced.

(2) HMRC's business income manual (BIM) published in 2013 (also published by CCH in 2014), a section of which dealt with deduction under section 68 CTA. This did not contain the former reference to "loose tools" but indicated that beer glasses in a pub, spanners used by car mechanic and cutlery in a cafe would generally qualify for deduction under these provisions, but not "lorries in a haulage firm", among other things. It is noteworthy that this was published after Turners had made its claim (I do not regard it as being relevant therefore to HMRC practice at or around the time its return was made or its tax paid); and

(3) the 2014 version of the BIM which repeated the content of the 2013 version.

150. Mr Hussain also explained that he had asked nine experienced colleagues at HMRC whether they recalled any claim being made for the deduction of the costs of lorries or other large items on the "statutory renewals basis" He received responses from five or six of those colleagues. None had seen such a claim.

151. In this context he also notes that Mrs Webberly, the inspector who initiated the enquiries into the company's returns wrote to the company in 2013 saying that the company’s claim was the first time in 30 years as an inspector that she had seen such a claim, and that a straw poll around her office elicited no report of such a claim.

152. Mr Husain arranged a review of returns submitted between 2010 and 2016 (and for some companies their 2009 accounts) by haulage firms considered (as I understood it by his colleagues) to be comparable to Turners with the object to determining whether claims similar to the company's had been made by those firms on the statutory renewals basis. It was difficult to assess the rigour with which this exercise was conducted because I was shown no record of the detail of the instructions given or the replies received, but it seems that the accounts, returns and risk assessments made by HMRC in respect of the chosen companies had been inspected for references to replacements, renewals or section 74(1)(d). The result of the exercise was that no instances of claims under the statutory or nonstatutory renewals basis for large items were identified and that capital allowances had been claimed for lorries etc. It was not clear to me that this meant that these companies had made no such claims because the deduction made may not have been identified under these headings, or because no enquiry had been made in relation to return which would identify claims of this nature: it was also not clear to me whether the documents searched would have permitted the identification of "large items".

153. Mr Husain also referred to the exercise being conducted by reference to the records of three groups and as being limited to businesses in the haulage industry.

154. I was also shown a number of publications:

(1) Tolleys Practical Tax Service of 26 July 2000 described the renewals basis as flowing from section 74(1)(d) and the items which qualify as being "such as loose tools". It notes that under the renewals basis no relief was given for the original acquisition.

(2) Simons Taxes for 2007. This says that the cost of replacements of implements, utensils and articles is deductible and that it includes items such as "loose tools"; it also describes the Renewals Practice for "large items of machinery" as an alternative to claiming capital allowances;

(3) In an article, “Renewals on Rails” in Taxation of 23 October 2013 Mike Truman argues that *Caledonian* is authority for the proposition that section 74, and so section 68, authorise a deduction for large items such as rolling stock.

(4) Taxation of 16 October 2014. This contains an answer to a reader’s question which notes HMRC's view that section 68 applies to a narrow range of items but questions its correctness: "obtaining relief may be a matter of going to tribunal". Another answer refers to the Truman article "Renewals on Rails.

(5) Corporate Tax 2015/16 (Bloomsbury) recites the "statutory renewals basis" and regards the scope of "trade tools" as limited by *Hyam*. It described a consessionary basis existing prior to 2013 permitting a revenue deduction “if the company agreed to a number of detailed conditions”

(6) Tiley’s Revenue law 2016 speaks of a Revenue practice of allowing the cost of replacing plant and machinery as a revenue expense. It says that the practice applies only to the replacement of implements, utensils and articles such as loose tools and similar assets, and that it seemed best to regard the practice as an extra statutory concession dating from times prior to capital

allowances. Where the basis is adopted the allowance given is the excess of the cost of the new item over the disposal value of the replaced item. It describes the practice as an alternative to capital allowances.

(7) Tolley's Capital Allowances (2015) says that prior to 2013 the nonstatutory renewal basis could be used as an alternative to capital allowances "particularly for small items". Under it no allowance was given for the original cost. "In general the renewal bases (both statutory and nonstatutory) were used for small items such as loose tools in a factory or crockery in a restaurant. It was possible for other classes of plant and machinery to attract capital allowances so the two bases ran side-by-side."

(8) Capital allowances: Transactions and Planning 2008/9 (Tottel). Here it is stated that an alternative to claiming capital allowances is the renewals basis which was confirmed by *Caledonian*.

(9) Corporation tax 2009/10 Juliana Waterston. Core Tax Annuals. Here it is said that "expenditure incurred on replacing or altering tools used in a trade is capital in nature. However a specific deduction is granted for replacing or altering small items used in trade (CTA 2009 section 68)".

(10) Taxation of Landlords 2015 CIOT says that "there is a view that" costs of replacing larger items may be allowable under section 68 and that *Caledonian* may support that view. It indicates that HMRC have a different opinion and advisers would "need to take a view" when advising clients.

(11) A brief from the Fyles Accountants in 2018 notes HMRC's view that “tools” in section 68 relates only to small items but says that the whole issue of renewals allowances has been unclear for many years.

(12) A Taxation Magazine article of 2014 says that most advisers had expected HMRC to allow deductions for the replacement of items such as fridges but HMRC had formally disagreed.

Discussion

155. The published materials indicate that there were, both before and in the period surrounding the company's 2008 return three bases upon which certain expenditure on the replacement of equipment could be claimed and would be allowed by HMRC as a deduction. They were:

(1) capital allowances for plant and machinery;

(2) the "statutory renewals basis" - a basis which relied upon section 74 as authority for the deduction of replacement items; and

(3) the non statutory renewals basis or Renewals Practice.

156. Each of these was accepted by HMRC and acknowledged by taxpayers. The existence of each could be readily ascertained from HMRC's publications and standard texts.

157. The terms of the capital allowance basis were readily ascertainable from the legislation. The terms of the Renewals Practice were also adequately clear.

158. The terms of the statutory renewals basis were in my view, less clearly ascertainable. It was clear that taxpayers could claim, and HMRC would except, claims for the replacement of items akin to loose tools. It was not clear that large items of plant and equipment were covered by this basis. The only source which made confident statements that the cost of items such as lorries were deductible on this basis was Mike Truman's article. That is insufficient in my view to conclude that it was readily ascertainable or generally accepted that it extended to such items.

159. If I am wrong (as must be the premise of this section of this decision) and section 74(1)(d) did authorise deduction of expenses on items such as lorries, then, because of section 4(2) Capital Allowances Act, a claim to capital allowances would not have been allowable. But it is clear to me that such claims to capital allowances were made and were accepted by HMRC: that is made clear in the published material..

160. The treatment and acceptance of the Renewals Practice as an alternative to capital allowances confirms me in this conclusion. It indicates that taxpayers did claim capital allowances for items which, if the statutory renewals basis authorised deduction, should not have been claimed, and thus that there was a settled and clear practice of claiming capital allowances for such items accepted by the taxpayers and HMRC alike.

161. Further even if a non statutory renewals basis were a relatively long established readily ascertainable and sufficiently precise basis for the deduction of the costs of replacement of items such as the trailers and tractors, that was an alternative to the practice – also generally prevailing and clearly ascertainable - of claiming capital allowances and not deductions.

162. I therefore conclude that the liability to corporation tax computed in the company's original corporation tax for return for 2008 was calculated in accordance with practice generally prevailing at the time of claiming capital allowances on items such as tractors and trailer units and thus within paragraph (b) of Case G.

163. As a result HMRC would not as a result of section 51A, be liable to meet the company's claim.

Conclusion

164. I dismiss the appeals

165. **Rights of Appeal**

166. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

CHARLES HELLIER

TRIBUNAL JUDGE
RELEASE DATE: 26 February 2019