

CORPORATION TAX - group relief - determination of profits of surrendering company - whether allowable losses of preceding accounting periods should be deducted from a realised chargeable gain - meaning of "profits" - meaning of "losses or allowances" - appeal allowed - ICTA 1988 s 403 (7) and (8)

THE SPECIAL COMMISSIONERS

M E P C HOLDINGS LIMITED Appellant:

and

CRISPIN MARK TAYLOR

(H M INSPECTOR OF TAXES) Respondent

SPECIAL COMMISSIONERS : MR T H K EVERETT

DR A N BRICE Chairman's name: use right arrow to move to starting point after this box

Sitting in London on 24 July 2000

Mr David Goldberg QC, instructed by Messrs PricewaterhouseCoopers, Chartered Accountants, for the Appellant

Mr Timothy Brennan of Counsel, instructed by the Solicitor of Inland Revenue, for the Respondent

CROWN COPYRIGHT 2000

DECISION

The appeal

1. M E P C Holdings Limited (the Company) appeals against a determination made by the Inland Revenue on 25 May 1999 that the amount available for surrender by the Company by way of group relief for the accounting period ending on 30 September 1994 was £42,304,116.00. The Company was of the view that the amount should be £48,344,400.00 and that it should not be reduced by realised chargeable gains of £6,040,284.00 which were more than offset by allowable losses brought forward from previous accounting periods.

2.. We were informed that three other companies wished to argue a similar point and that this was a test case.

The facts

3. The facts were not disputed. The Company is an investment company and at all material times was within the charge to corporation tax and was a member of a group relief group. Other companies in the group had made valid claims in respect of the amounts eligible for relief surrendered by the Company. In its accounting period ending on 30 September 1994 the Company made profits of £300,000 and had charges on income of £48,644,400. Thus charges on income exceeded profits by £48,344,400. In the same accounting period the Company

realised chargeable gains of £6,040,284 Allowable losses brought forward from past periods amounted to £60,583,017 and thus very substantially exceeded the chargeable gains.

The legislation

4. Chapter IV (sections 402 to 413) of Part X of the Income and Corporation Taxes Act 1988 (the 1988 Act) contains provisions about group relief. Section 402 provides that, in certain circumstances, relief for trading losses and other amounts eligible for relief from corporation tax may be surrendered by one company (the surrendering company) and allowed to another company who makes a claim (the claimant company) where both companies are members of the same group.

5. Section 403 describes the amounts eligible for relief which may be surrendered. The subsections of direct relevance to this appeal are subsections (7) and (8). At the relevant time those subsections provided:

"(7) Subject to the provisions of this Chapter and section 494(4), if in any accounting period the surrendering company has paid any amount by way of charges on income, so much of that amount as exceeds its profits of the period may be set off for the purposes of corporation tax against the total profits of the claimant company for its corresponding accounting period.

(8) The surrendering company's profits of the period shall be determined for the purposes of subsection (7) above without regard to any deduction falling to be made in respect of losses or allowances of any other period, or to expenses of management deductible only by virtue of section 75(3)."

The issue

6. The issue for determination in the appeal was whether, in determining the Company's profits for the purposes of section 403(7), the result of section 403(8) was that the amount to be included in profits in respect of chargeable gains was £nil being the net amount of the realised chargeable gain less the allowable losses brought forward (as argued by the Company) or whether the amount to be included in profits in respect of chargeable gains was the realised chargeable gain with no deduction for the allowable losses brought forward (as argued by the Inland Revenue).

7. In this decision we use the phrase "allowable losses" to mean losses which may be set against chargeable gains.

The arguments of the parties

8. The Company raised three main arguments. First it said that the meaning of the word "profits" in section 403(7) and (8) meant the inclusion of a net figure for chargeable gains less allowable losses. Secondly it said that the meaning of the words "losses or allowances" in section 403(8) meant trading losses or capital allowances and not allowable losses. And finally it said that it was the intention of the legislation that group relief was not available for brought forward losses and allowances in those cases where the surrendering company had had the option of surrendering them in previous years and had not done so; such an option was not available for allowable losses.

9. The Inland Revenue argued that the intention of the legislation was that the only amounts which could be deducted in calculating profits were amounts which could be deducted in the year of surrender and to take into account brought forward allowable losses would be to defeat that intention.

Reasons for decision

10. In considering the arguments of the parties we have first looked at the words of the legislation and we begin by considering the meaning of the word "profits" as used in section 403(7) and (8). The questions raised by the arguments of the parties about the meaning of these words were:

(1) Do "profits" for the purposes of section 403(7) and (8) include chargeable gains without any deduction of allowable losses? and

(2) If so, does the same argument apply to trading losses, capital allowances and management expenses?

11. We then consider the meaning of the words "losses or allowances" in section 403(8). The questions raised by the arguments of the parties about the meaning of those words were:

(3) What meaning of the words "losses or allowances" emerges from a consideration of the context of section 403 as a whole?

(4) What meaning of the words "losses or allowances" emerges from a consideration of other provisions of the 1988 Act?

(5) What meaning of the word "losses" emerges from the capital gains tax legislation?

12. Finally, we consider the intention of the legislation and here the question raised by the arguments of the parties was:

(6) What is the relevance of the intention of the legislation?

13. Mr Goldberg QC also put forward a number of other arguments which were not challenged by Mr Brennan. We therefore do not consider these but Mr Goldberg's skeleton argument (which runs to 32 pages) will be available should this Decision be appealed.

14. We consider each of the questions separately.

(1) Do "profits" for the purposes of section 403(7) and (8) include chargeable gains without any deduction of allowable losses?

15 The first question is whether, for the purposes of section 403(7) and (8), the word "profits" includes chargeable gains without any deduction of allowable losses.

16. Subsections (7) and (8) of section 403 refer to the surrendering company's profits. In considering this question references were made to the word profits in sections 6, 8 and 9 of the 1988 Act and in section 8(1) of the Taxation of Chargeable Gains Act 1992 (the 1992 Act).

17. Section 6 of the 1988 Act contains provisions relating to the charge to corporation tax. The relevant parts of section 6 provide:

"(1) Corporation tax shall be charged on profits of companies ...

"(4) In this section ...

(a) "profits" means income and chargeable gains.

18. Section 8 of the 1988 Act contains provisions relating to the general scheme of corporation tax and section 8(1) provides:

"(1) ... a company shall be chargeable to corporation tax on all its profits wherever arising".

19. Section 9 of the 1988 Act contains provisions relating to the computation of income and section 9(3) provides:

"(3) Accordingly, for the purposes of corporation tax, income shall be computed ... under the like Schedules and Cases as apply for the purposes of income tax, and in accordance with the provisions applicable to those Schedules and Cases, but ... the amounts so computed for the several sources of income, if more than one, together with any amount to be included in respect of chargeable gains, shall be aggregated to arrive at the total profits".

20. Section 8 of the 1992 Act contains provisions that a company's total profits should include chargeable gains. Section 8(1) provides:

"(1) ...the amount to be included in respect of chargeable gains in a company's total profits for any accounting period shall be the total amount of the chargeable gains accruing to the company in the accounting period after deducting-

(a) any allowable losses accruing to the company in the period, and

(b) so far as they have not been allowed as a deduction from chargeable gains accruing in any previous accounting period, any allowable losses previously accruing to the company while it has been within the charge to corporation tax."

21. In support of his argument (that the meaning of the word "profits" in section 403(7) and (8) meant the inclusion of a net figure of chargeable gains after deduction of allowable losses brought forward) Mr Goldberg QC argued that "profits" had to be computed in accordance with the statutory provisions. As a result of sections 6(4)(a), 8(1) and 9(3) of the 1988 Act, and of section 8(1) of the 1992 Act, what was included in the computation of profits was a net figure of chargeable gains after deduction of allowable losses and not a gross figure of chargeable gains from which allowable losses were subsequently deducted. In the present appeal, where the allowable losses were greater than the realised chargeable gain, no amount had been included in the profits but no deduction had been made in computing profits either. Mr Goldberg QC accepted that the legislation sometimes used the word "profits" and sometimes used the phrase "total profits" but he argued that, for the purposes of the charge to tax, both phrases meant the same thing. Mr Goldberg QC relied upon *Owton Fens Properties Limited v Redden* (1984) 58 TC 218 at 230H; *Tod v South Essex Motors (Basildon) Limited* (1987) 60 TC 598 at 611E-613D; and *Jones v Lincoln-Lewis & Others* (1991) 64 TC 112 at 121G.

22. For the Inland Revenue Mr Brennan argued that it was the plain meaning of section 6(4) of the 1988 Act that profits meant income and chargeable gains. Chargeable gains were an element of profits. Section 9(3) of the same Act provided that all income and chargeable gains were to be aggregated to arrive at total profits. So chargeable gains were treated as analogous to a source of income.

23. In considering the arguments of the parties we start with the legislation. First we record that we heard detailed argument from Mr Goldberg QC that, for the purposes of this appeal, the word "profits" meant the same as the phrase "total profits". That was not disputed by Mr Brennan and so we proceed on the basis that, at least for the purposes of this Decision, profits means the same as total profits.

24. We agree with Mr Brennan that profits means income and chargeable gains as that is clear from sections 6(4)(a) and 9(3) of the 1988 Act. But that does not tell us how chargeable gains are to be calculated. It is section 8(1) of the 1992 Act which indicates that the amount of chargeable gains to be included in a company's (total) profits for any accounting period is the total amount after deducting allowable losses both in that period and brought forward from a previous period. Thus the phrase "chargeable gains" is defined in section 8(1) of the 1992 Act as the net amount of realised chargeable gains after deduction of allowable losses for the same period and previous periods. Accordingly we conclude that the effect of the statutory provisions is that the word "profits" means income and the net amount of chargeable gains after deduction of allowable losses for the same accounting period and previous accounting periods.

25. Having reached that point we consider the authorities cited to us.

26. In *Owton Fens* (1984) the issue was whether an assessment to corporation tax, which assessment was in respect of interest only, could be amended in order to charge Schedule A income and also chargeable gains. The appellant argued that the assessment had to identify the different sources of income assessed and had failed to do so. Vinelott J held that the legislation required that all chargeable income and chargeable gains for a given accounting period were to be aggregated and included in a single assessment. An appeal against that assessment was an appeal against the profit chargeable to corporation tax.

27. In *South Essex Motors* (1987) the issue was whether the company could set against its chargeable gains of £374.00 allowable losses of £100,125.00 which the Inland Revenue had agreed could be carried forward from previous years when in fact no such allowable losses existed. The Inland Revenue argued that, as there had not been an allowable loss, it could not be carried forward and any agreement was not binding for future years of assessment. In a passage relied upon by Mr Goldberg QC at page 612H Knox J said:

"That treatment [reducing the chargeable gains by the allowable losses carried forward and thus increasing trading losses] assuming for the moment that there were losses for chargeable gains purposes of £100,125, or indeed of any figure of £374 or more, was correct in that chargeable gains for an accounting period are required by section 265(1) of the Income and Corporation Taxes Act 1970 [the predecessor of section 8(1) of the 1992 Act] to be those accruing in the relevant accounting period after deducting allowable losses previously accruing to the company so far as not already allowed as deductions. So that on the hypothesis that there was such an allowable loss of £100,125 the gain of £374 was liable to be extinguished by a set-off of that amount out of the £100,125 loss reducing it

to £99,751 and consequently increasing the trading losses to be carried forward since no set off under section 177(2) of the Income and Corporation Taxes Act 1970 [the predecessor of section 393A(2) of the 1988 Act] was now necessary or indeed possible under that subsection, there being no chargeable gains to be the subject of set off".

28. Lincoln-Lewis (1991) concerned section 42(2) of the Finance Act 1965 and the apportionment to three beneficiaries of chargeable gains made by non-resident trustees. The issue was whether the beneficiaries had interests in the settled property at the relevant time. In the passage relied upon by Mr Goldberg QC, Hoffmann J said at page 121G:

"Despite the reference in the second part of s 42(2) to the apportionment of "the chargeable gain", it is clear that what is being apportioned is the amount on which the trustees would have been chargeable under s20(4) namely, the total amount of chargeable gains accruing in the year of assessment after deducting any allowable losses. It is not an apportionment of any particular gains which may have accrued from time to time. The only time at which the amount to be apportioned can be ascertained in accordance with s20(4) is the end of the year of assessment"

29 Although none of these authorities is directly on all fours with the issue in the present appeal they do support the argument of Mr Goldberg QC that "chargeable gains" are the total amount of gains for any year reduced by allowable losses for that year and previous years. Thus they are consistent with the provisions of section 8(1) of the 1992 Act.

30. Having reached that point we conclude that in section 403(7) and (8) the surrendering company's "profits" means its income and chargeable gains and its chargeable gains means realised gains less allowable losses for the current and previous years.

(2) If so, does the same argument apply to trading losses, capital allowances and management expenses?

31. For the Company Mr Goldberg QC accepted that the purpose of section 403(8) was to restrict the availability of group relief so that trading profits could not be reduced by trading losses of preceding periods. Section 393 gave relief for trading losses and so in section 9(1) the calculation of trading profits meant the deduction of trading losses. He referred to sections 393(1) and (8) and 393A(1) of the 1988 Act; section 75(1) of the 1988 Act and sections 144 and 145(3) of the Capital Allowances Act 1990 (the 1990 Act). In each of these cases gross profits were first established and then a deduction made. However, he argued that allowable losses were treated differently as they defined the figure of chargeable gains brought into the computation in the first place. Section 9(3) of the 1988 Act and section 8(1) of the 1992 Act made it plain that the computation of gains was outside the computation of profits. It was the net figure of chargeable gains which was included in profits.

32. For the Inland Revenue Mr Brennan argued that the same argument (that chargeable gains meant net gains after the deduction of allowable losses) could also be applied to trading losses and the Company accepted that trading losses for previous accounting periods could not reduce profits for the purposes of group relief. He referred to section 393(1) of the 1988 Act where there was an automatic set-off of a loss in a trade from trading income in succeeding accounting periods and that was very like section 8(1) of the 1992 Act which

gave an automatic allowance for allowable losses in the preceding accounting periods. The explanation for the reference to section 75(3) at the end of section 403(8) was that brought forward management expenses were treated as management expenses of the accounting period to which they were carried forward.

33. Section 393(1) of the 1988 Act provides that trading losses of companies shall be set off against trading income of succeeding accounting periods. As section 393(1) provides that it is the trading income of succeeding accounting periods (and not profits) which is reduced by the carried forward trading loss, it supports the arguments of Mr Brennan that it is a net figure of trading income after the deduction of carried forward trading losses which forms part of profits (or total profits). That is similar to the treatment which we have found applies to chargeable gains.

34. Section 75(1) of the 1988 Act provides that, in computing the total profits for the purposes of corporation tax for any accounting period of an investment company management expenses for that period shall be deducted. Section 75(3) provides that, where management expenses and charges on income exceed the amount of profits, the excess shall be carried forward to succeeding accounting periods. Thus section 75(3), by providing that excess management expenses are deducted from total profits in the succeeding accounting period, is not similar to the treatment which we have found applies to chargeable gains as the carried forward amount is a deduction after the calculation of total profits and not a deduction in making the calculation.

35 Section 144 of the 1990 Act contains the general provision for the deduction or addition of capital allowances or charges in computing a company's profits for any accounting period. Section 145 provides that a capital allowance which is to be given by discharge or repayment of tax, and is to be available primarily against a specified class of income, shall, so far as may be, be deducted from income of the specified class for the same period. Section 145(2) provides that, if there is not sufficient income of the specified class, then the amount unallowed shall be carried forward to the succeeding period unless effect has been given to it by subsection (3). Section 145(3) provides:

"(3) Where such an allowance which is to be made for any accounting period (otherwise than by being carried forward from an earlier accounting period) cannot be given full effect under subsection (1) above in that period by reason of want or deficiency of income of the relevant class, the company may, on making a claim ..., require that effect shall be given to the allowance against the profits (of whatever description) of that accounting period and, if the company was then within the charge to tax, of preceding accounting periods ... and ... the profits of any of those accounting periods shall then be treated as reduced by the amount unallowed under subsection (1) above, or by so much of that amount as cannot be given effect under this subsection against profits of a later accounting period."

36. Thus, section 145(2) of the 1990 Act, in providing for unused allowances which are primarily to be taken against a specified class of income to be carried forward "in computing a company's profits", is similar to the provision in section 393(1) and thus is similar to the treatment which we have found applies to chargeable gains. On the other hand, section 145(3), which provides for allowances which cannot be used against specified income to be used against profits of whatever description of that or preceding accounting periods, is similar to the provisions of section 75(3) and thus is not similar to the treatment which we have found applies to chargeable gains.

37. We conclude that, in computing profits, it is net trading income after deduction of carried forward trading losses which is brought into account but that excess management expenses are deducted from total profits. The capital allowance provisions have similarities with both procedures.

38. We therefore do not find the references to section 393(1) and 75(3) of the 1988 Act and to section 145(3) of the 1990 Act to be of great assistance to us. We do, however, note that section 403(8) specifically provides that there is to be no deduction for "losses or allowances" or brought forward management expenses of preceding periods. In our view, therefore, it is necessary to determine the meaning of the words "losses or allowances" in section 403(8).

(3) What meaning of the words "losses or allowances" emerges from a consideration of the context of section 403 as a whole?

39. The third question concerns the meaning of the words "losses or allowances" in section 403(8) and asks what meaning of those words emerges from a consideration of the context of section 403 as a whole.

40. In order to consider this question we need to refer to subsections (1), (3), (4), (5), (7) and (8) of section 403 which, at the relevant time, provided:

"403 Losses etc. which may be surrendered by way of group relief

(1) Subject to the provisions of this Chapter, if in any accounting period

the surrendering company has incurred a loss, computed as for the purposes of section 393A(1), in carrying on a trade, the amount of the loss may be set off for the purposes of corporation tax against the total profits of the claimant company for its corresponding accounting period. ...

(3) Subject to the provisions of this Chapter, if for any accounting period any capital allowances fall to be made to the surrendering company which-

(a) are to be given by discharge or repayment of tax, and

(b) are to be available primarily against a specified class of income

so much of the amount of those allowances (exclusive of any carry forward from an earlier period) as exceeds its income of the relevant class arising in that accounting period (before deduction of any losses of any other period or of any capital allowances) may be set off for the purposes of corporation tax against the total profits of the claimant company for its corresponding accounting period.

(4) Subject to the provisions of this Chapter, if for any accounting period the surrendering company (being an investment company) may under subsection (1) of section 75 deduct as expenses of management any amount disbursed for that accounting period, so much of that amount (exclusive of any amount deductible only by virtue of subsection (3) of that section) as exceeds the company's profits of that accounting period may be set off for purposes of corporation tax against the total profits of the claimant company (whether an investment company or not) for its corresponding accounting period.

(5) The surrendering company's profits of the period shall be determined for the purposes of subsection (4) above without any deduction under section 75 and

without regard to any deduction falling to be made in respect of losses or allowances of any other period. ...

(7) Subject to the provisions of this Chapter and section 494(4), if in any accounting period the surrendering company has paid any amount by way of charges on income, so much of that amount as exceeds its profits of the period may be set off for the purposes of corporation tax against the total profits of the claimant company for its corresponding accounting period.

(8) The surrendering company's profits of the period shall be determined for the purposes of subsection (7) above without regard to any deduction falling to be made in respect of losses or allowances of any other period, or to expenses of management deductible only by virtue of section 75(3)."

41. In support of his argument that the words "losses or allowances" in section 403(8) meant trading losses and capital allowances and not allowable losses Mr Goldberg QC relied upon the context of section 403 as a whole. He argued that under section 403(1) a trading loss for that accounting period could be surrendered. Under section 403(3) certain excess capital allowances for that accounting period could be surrendered. Section 403(4) and (5) contained special provisions for investment companies and subsection (5) provided that profits should be determined without regard to "any deduction falling to be made in respect of losses or allowances of any other period". That provision repeated the provisions relating to trading losses and capital allowances in subsections (1) and (3). Subsections (7) and (8) contained provisions for charges on income and again precluded the deduction of losses or allowances of any other period. He argued that, within the context of section 403(8), the phrase "losses or allowances" referred back to the trading losses mentioned in section 403(1) and the capital allowances mentioned in section 403(3).

42. For the Inland Revenue Mr Brennan argued that trading companies were treated differently from investment companies. Section 403(1) dealt with trading losses and section 403(3) with capital allowances. However, section 403(7) dealt with charges on income and section 403(8) restricted charges which could be surrendered. If a section 403(7) company had Case III income of £1,000 and chargeable gains of £1,000 and charges on income of £5,000 then the surrenderable charges on income were £3,000. If a section 403(1) company had Case III income of £1,000, capital gains of £1,000 and a Case I loss of £5,000 then, under section 403(1), the surrenderable loss was £5,000.

43. We accept the arguments of Mr Brennan that section 403 provides a different treatment for trading companies on the one hand and investment companies on the other. We also note that his example assumes that in each case that there has been a chargeable gain. But the example does not assist in deciding whether, if there were allowable losses for past periods, they might be brought forward to reduce that chargeable gain. What we have to do is to consider the meaning of the words "losses or allowances" in section 403(8) and we find that exactly the same words have been used earlier in the section. In section 403(1) the word "loss" is used to mean a trading loss and the context in which it is used is to restrict a claim to the trading loss of that accounting period. In section 403(3) the word "allowances" is used to mean capital allowances and, again, the context in which it is used is to restrict claims to that accounting period. Subsections 403(4) and (5) deal with investment companies and the deduction of the expenses of management and section 403(5) uses the words "losses or allowances" again within the context of that accounting period. In our view, within the context of section 403, and the context within which the words are used in section 403(5),

they are intended to have the same meaning as the word "loss" in section 403(1) and the word "allowances" in section 403(3). Similarly, section 403(7) and (8) deal with charges on income and the same words "losses or allowances" are used within the context of restricting a claim to that accounting period. The conclusion is that the words have the same meaning as the same words used previously in the same section within the same context.

44 Section 403 has a certain symmetry. Subsection (1) deals with trading losses and specifically provides that they must be losses incurred in the accounting period. Subsection (3) deals with capital allowances and again specifically provides that they are exclusive of any carried forward from an earlier period. Subsection (4) deals with investment companies and the expenses of management and subsection (5) contains the provision (also in subsections (1) and (3)) that there should be no deduction for losses or allowances of any other period. Subsection (7) deals with charges on income and subsection (8) contains the (now familiar) provision about there being no deduction for losses or allowances of earlier periods. In our view, if Parliament had intended that the same words in the same context in the same section should have different meanings, then that would have been made clear.

45. We conclude that the meaning which emerges from a consideration of the context of section 403 as a whole is that, in section 403(8), the word "losses" means trading losses and the word "allowances" means capital allowances.

(4) What meaning of the words "losses or allowances" emerges from a consideration of other provisions of the 1988 Act?

46. The fourth question asks what meaning of the words "losses or allowances" emerges from a consideration of other provisions of the 1988 Act

47. In further support of his argument that the words "losses or allowances" in section 403(8) meant trading losses and capital allowances and not allowable losses Mr Goldberg QC referred to sections 407 and 409 of the 1988 Act and argued that section 407 set a ceiling on the claim by the claimant company and the amount which could be surrendered was limited by reference to trading losses and capital allowances but not by allowable losses. Section 409 applied to companies joining or leaving a group and section 409(3)(a) provided that references in section 403 to losses and allowances should be construed in accordance with section 409(2). That only included trading losses and capital allowances and not allowable losses. The references in sections 108, 623(7)(a) and 646(5)(a) were not directly of help but reinforced the pattern that the phrase "loss or allowance" never included a reference to an allowable loss. It would be extraordinary if the only subsection where the phrase "loss or allowance" included an allowable loss were to be subsection 403(8).

48. For the Inland Revenue Mr Brennan accepted that, in the contexts of sections 108, 409, 623(7)(a) and 646(5)(a) the reference was to trading losses and capital allowances but argued that the words did not have the same meaning in section 403(5) and (8). In section 409(3) the whole point of the provision was a reference to an earlier provision. The section was not dealing with allowable losses because allowable losses could not be surrendered by way of group relief but that did not mean that in section 403(8) losses or allowances did not include allowable losses as well as trading losses. Mr Brennan also cited *Smith v Schofield* (1992) 65 TC 669 and argued that subsection 403(8) had to be construed within the context of section 403, the group of sections and the scheme of the

legislation and that reference should not be made to other contexts or to marginal anomalies.

49. We agree with Mr Brennan that, in considering the meaning of words in section 403 we should primarily have regard to that section and to the group of sections of which it is a part. That means that we should consider sections 407 and 409 both of which appear in Chapter IV of Part X with section 403.

50. Section 407 contains provisions relating to the relationship between group relief and other relief. The relevant part of section 407 provides:

"407. Relationship between group relief and other relief

(1) Group relief for an accounting period shall be allowed as a deduction against the claimant company's total profits for the period-

(a) before reduction by any relief derived from a subsequent accounting period, but

(b) as reduced by any other relief from tax (including relief in respect of charges on income under section 338(1) determined on the assumption that the company makes all relevant claims under section 393A(1) of this Act and section 145(3) of the 1990 Act (set off of capital allowances against profits)."

51. Section 407 looks at the position of the claimant company in relation to group relief and provides that group relief is given after any other relief from tax under section 393A(1) of the 1988 Act and section 145(3) of the 1990 Act. Section 393A(1) of the 1988 Act refers to trading losses and section 145(3) of the 1990 Act refers to capital allowances. Thus we agree with Mr Goldberg QC that section 407 does not mention allowable losses. However, section 407 deals with the position of the claimant rather than of the surrendering company. Parliament could have intended different considerations to apply to the claimant company on the one hand and the surrendering company on the other. Accordingly, we do not find the context of section 407 to be conclusive in reaching a decision about the deductions which may not be made by the surrendering company.

52. Section 409 contains provisions about companies joining or leaving a group. The relevant parts provide:

"409. Companies joining or leaving group or consortium

(1) Subject to the following provisions of this section, group relief shall be given if, and only if, the surrendering company and the claimant company are members of the same group .. throughout the whole of the surrendering company's accounting period to which the claim relates, and throughout the whole of the corresponding accounting period of the claimant company.

(2) Where on any occasion two companies become or cease to be members of the same group, then, for the purposes specified in subsection (3) below, it shall be assumed as respects each company that-

(a) on that occasion (unless a true accounting period of the company begins or ends then) an accounting period of the company ends and a new one begins, the new accounting period to end with the end of the true accounting period (unless before then there is a further break under this subsection); and

(b) the losses or other amounts of the true accounting period are apportioned to the component accounting periods; and

(c) the amount of total profits for the true accounting period of the company against which group relief may be allowed in accordance with section 407(1) is also apportioned to the component accounting periods;

and an apportionment under this subsection shall be on a time basis according to the lengths of the component accounting periods ...

(3) Where the one company is the surrendering company and the other company is the claimant company -

(a) references in section 403 to accounting periods, to profits, and to losses, allowances, expenses of management or charges on income of the surrendering company shall be construed in accordance with subsection (2) above..."

53. Section 409(2) and (3) applies to both the surrendering and the claimant company leaving a group. Section 409(2) provides for an apportionment of losses and profits between accounting periods and section 409(3) provides that the provisions of section 403 as to "profits, and to losses, allowances, expenses of management or charges on income of the surrendering company" are applied accordingly. The Inland Revenue accept that the same words, namely "losses, allowances" in section 409(3)(a) mean trading losses and capital allowances. We are at a loss to understand how the words could have a different meaning in section 403(8).

54. We refer very briefly to sections 108, 623(7)(a) and 646(5)(a).

55. Section 108 appears in Chapter VI (Discontinuance and Change of Basis of Computation) of Part II (Income Tax: Basis of Assessment, etc) of the 1988 Act. Section 105 provides that, where receipts are made after a discontinuance, losses, expenses and debits and capital allowances may be deducted. Section 108 provides an election for carry-back and refers to "any loss or allowance deducted in pursuance of section 105". Section 108 uses the words "loss or allowance" but refers back to section 105 which itself uses the words "losses, expenses and debits and capital allowances". The Inland Revenue accept that these words mean trading losses and capital allowances. The context of section 108 is the discontinuance of a trade and not group relief. Accordingly, we do not consider that the meaning of the words in that context assists in deciding the meaning of similar words in the context of section 403.

56. Section 623 appears in Chapter III of Part IV of the 1988 Act which concerns retirement annuities. Section 623 defines relevant earnings. Subsection (6) provides that "net relevant earnings" means earnings after deductions in respect of losses or capital allowances arising from activities, profits or gains of which would be included in computing relevant earnings. Subsection (7) (a) refers to "any such loss or allowance of the individual as is mentioned in subsection (6)(c) above". Thus, section 623(7)(a) uses the words "loss or allowance" but refers back to section 623(6)(c) which defines the losses and allowances as arising from trading.

57. Section 646 appears in Chapter IV of Part IV of the 1988 Act which Chapter deals with personal pension schemes. Section 646 defines the meaning of net relevant earnings. Subsection 646(2) described the deductions to be made from relevant earnings and subsection 646(2)(d) refers to "deductions in respect of

losses or capital allowances, being losses or capital allowances arising from activities, profits or gains of which would be included in computing relevant earnings of the individual". Subsection (5) (a) refers to "such loss or allowance of the individual as is mentioned in subsection (2)(d) above". Section 646(5)(a) also refers to "loss or allowance" but refers back to section 646(2)(d) which again defines the losses or capital allowances as arising from trade.

58. We are not surprised, therefore, that the Inland Revenue accept that, in both sections 623(7)(a) and 646(2)(a), the words "losses or allowances" mean trading losses or capital allowances.

59. We conclude that the meaning which emerges from a consideration of other provisions of the 1988 Act, and, in particular from section 409(2) and (3), is that the phrase "losses or allowances" in section 403(8) means trading losses or capital allowances and not allowable losses.

(5) What meaning of the word "losses" emerges from the capital gains tax legislation?

60. The fifth question asks what meaning of the words "losses" emerges from a consideration of the capital gains tax legislation.

61. In further support of his argument that the words "losses or allowances" in section 403(8) meant trading losses and capital allowances and not allowable losses, Mr Goldberg QC argued that, throughout the Taxes Acts, the word "loss" was used to mean a trading loss (as in sections 393 and 393A of the 1988 Act) and the word allowance was used to mean a capital allowance as in sections 9, 144 and 145 of the 1990 Act. In the capital gains tax legislation there was no reference to a loss but always to an allowable loss and he referred in particular to sections 2(2), 8(1) and 16 of the 1992 Act. In section 16 the phrase "allowable loss" was artificially defined. Also, the indexation provisions for capital gains tax had the result that the indexation calculation could give rise to an allowable loss when in fact there had been a gain and he cited *Smith v Schofield* at 686D and 709H. Thus allowable losses were not losses in the ordinary meaning of the word and could include what was in fact a gain.

62. Section 393 of the 1998 Act deals with "a loss in the trade" as also does section 393A. The 1990 Act uses the word "allowance" to mean a capital allowance. The 1992 Act uses the words "gains" and "chargeable gains" and "losses" and allowable losses". However, it is only "chargeable gains" which are chargeable to capital gains tax and it is only "allowable losses" which may be deducted.

63. We therefore conclude that the Taxes Acts use the word "losses" to mean trading losses and "allowable losses" to mean capital losses which may be deducted from capital gains. However, if section 403(8) had referred to "any losses", we might have been open to persuasion that a general reference to "any losses" could include allowable losses. But section 403(8) refers to "losses or allowances" within the context of a whole section where those words mean trading losses and capital allowances.

(6) What is the relevance of the intention of the legislation?

64. The sixth question asks what is the relevance of the intention of the legislation.

65. For the Company Mr Goldberg QC argued that the policy of the group relief legislation was to ensure that current surplus reliefs could be surrendered and that there should not be relief both for current surplus reliefs and brought forward losses or allowances which could have been surrendered in earlier years but were not. If a taxpayer failed to surrender reliefs in year 1 it should not be able in effect to surrender them in year 2, That could not happen with an allowable loss which was not surrenderable until the net gains were brought into charge. The taxpayer had no choice but to deduct an allowable loss from a chargeable gain. The requirement to ignore carried forward reliefs was to prevent the abuse of choice and once a choice had been made it could not be changed later. He also argued generally that the Company was entitled to take advantage of a relief subject only to express or implied statutory restrictions, implications being made only where necessary and where the statute unambiguously so required. He cited Carr v Armpledge [2000] STC 410 at 416C.

66. For the Inland Revenue Mr Brennan argued that the plain words of section 403 demonstrated the intention that only deductible amounts of the period could be taken into account in calculating the profits of the surrendering company.. To take into account brought forward capital losses would defeat the intention of the section. The clear policy of section 403(7) and (8) was to prevent a taxpayer company surrendering charges on income save to the extent that they exceeded the profits of the current year. It was not possible to carry forward an allowable loss and surrender it.

67. In our view the intention of the legislation should primarily be derived from the language used, read in the context of the statute as a whole. Words should be given their normal and natural meaning having regard to the context within which they appear. Nothing should be read in or implied. For the reasons mentioned above we consider that the meaning of the words "losses or allowances" in section 403(8) is trading losses or capital allowances and not allowable losses.

Decision

68. Our decision on the issue for determination in the appeal is that, in determining the Company's profits for the purposes of section 403(7), the result of section 403(8) is that the amount to be included in profits in respect of chargeable gains is £nil being the net amount of the realised chargeable gain less the allowable losses brought forward.

82. Accordingly, the appeal is allowed.

Chairman's name: use right arrow to move to starting point

T H K EVERETT

NUALA BRICE

SPECIAL COMMISSIONERS

Date of Release: 27th September 2000