Neutral Citation Number: [2021] EWCA Civ 283

Case No: A3/2020/0873

IN THE COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE UPPER TRIBUNAL (TAX AND CHANCERY CHAMBER)
(Snowden J and Judge Hellier)
[2019] UKUT 0367 (TCC)

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 3 March 2021

Before :

LORD JUSTICE DAVID RICHARDS
LADY JUSTICE ROSE
and
LORD JUSTICE DINGEMANS

- -

Between :

(1) EASTERN POWER NETWORKS PLC
(2) SOUTH EASTERN POWER NETWORKS PLC
(3) LONDON POWER NETWORKS PLC
(4) UK POWER NETWORKS (TRANSPORT) PLC **Appellants**

- and –

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

- -
- -

Jonathan Peacock QC and Sarah Black (instructed by **ADE Tax**) for the **Appellants**
David Ewart QC and Marika Lemos (instructed by **the General Counsel and solicitor for HM Revenue and Customs**) for the Respondents

Hearing dates: 3 and 4 February 2021

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Approved Judgment

Covid-19 Protocol: This judgment was handed down remotely by circulation to the parties' representatives by email, release to BAILII and publication on the Courts and Tribunals Judiciary website. The date and time for hand-down is deemed to be 3 March 2021 at 10.30 a.m.

Lady Justice Rose:

1. The four Appellants are the subject of enquiries opened by the Respondents ('HMRC') into their corporation tax returns for the periods ended 31 December 2011 to 2013. The enquiries are carried out pursuant to the powers set out in Part IV of Schedule 18 to the Finance Act 1998 and relate to claims made by the Applicants for consortium relief. HMRC have asked for a great deal of information and numerous documents in the course of the enquiries. The Appellants have already provided them with much but not all of what they were asked for. HMRC have issued formal information notices pursuant to Schedule 36 to the Finance Act 2008. Those information notices have been challenged by the Appellants but we were told that those proceedings have been stayed pending the resolution of this appeal.

2. According to paragraphs 32(1A) and 34 of Schedule 18, an enquiry is completed when an officer of HMRC issues a closure notice. That notice informs the company that HMRC have completed their enquiry, states HMRC's conclusions and makes any amendments to the tax return that are required to give effect to those conclusions. If the company disagrees with HMRC's conclusions, it may launch an appeal against the revised assessment under paragraph 34(3) of Schedule 18 but the company cannot do that until the enquiry has been closed. If the company considers that the enquiry has gone on too long and that HMRC have enough material to complete their enquiry, paragraph 33 of Schedule 18 provides that a company may apply to the tribunal for a direction that HMRC give a closure notice within a specified period. If the company makes such an application, the tribunal must give that direction unless satisfied that HMRC have reasonable grounds for not yet giving a closure notice.

3. Consortium relief is a kind of corporate group relief. Where one company within a corporate group has made a trading loss and another company in the same group has made a profit, then although each company is usually treated as a separate taxpayer, the loss-making company can surrender its loss so that it can be set against the profit that was made by a company elsewhere in the group. The conditions which must be fulfilled before a taxpayer can claim consortium relief are set out in Part 5 of the Corporation Tax Act 2010 ('the CTA'). A company is owned by a consortium, broadly, when at least 75% of its shares are owned by other companies each of which owns at least 5% of the company's share capital (as defined). The companies who own at least 5% of the ordinary share capital are referred to as the members of the consortium. Again broadly, where a taxpayer company is owned by a consortium and a member of that consortium is a company in a corporate group, then if there is another company in the same corporate group as that member that has made a loss, that loss-making company can surrender its loss to the taxpayer company which is part owned by the consortium member. The consortium member in that situation is referred to as the 'link company' because it forms the link between the surrendering company which made the loss elsewhere in the group and the profitable company owned by the consortium. The amount of the relief that the profitable claimant company can claim is supposed to reflect the size of the interest that the link company has in the claimant company. So if, for example, the link company only 'owns' 15% of the profitable company owned by the consortium, it should only be able, through its link with the surrendering company, to set off losses against 15% of those profits. The proportion of ownership is specified as being the lowest proportion out of a number of different possible metrics. The important metric here is the percentage of

votes that the link company has as a result of its shareholding in the claimant company. In other words, the more votes that the link company can exercise at a general meeting of the shareholders of the claimant company, the more of the claimant company's profits can be offset by the surrendering company's losses via the link company, if that is the lowest of the possible ownership proportions.

4. Where the consortium company wishes to rely on the proportion of votes as its lowest ownership proportion, there is therefore an incentive for the link company to hold as high a proportion of votes at the claimant company's general meetings as possible. But usually that high level of votes would give the link company control over the affairs of the claimant company. The other shareholders in the claimant company might not want the link company to have that level of control, so they may put in place a scheme whereby even though the link company has a high proportion of votes (maximising the amount of loss relief the claimant company can claim), it does not have enough votes to control the claimant company. The statutory provisions in issue here are designed to stop that kind of scheme where the purpose of the scheme is to maximise the tax advantage provided by the consortium relief. The question to which HMRC's enquiries are directed is whether there is a scheme here caught by this anti-avoidance provision. The Appellants say that it is clear if the statutory provisions are properly construed that there is no such scheme and they are entitled to the consortium relief that they claimed in their corporation tax returns. They say that there is nothing further that HMRC need investigate and HMRC should be directed to issue closure notices to bring their enquiries to an end. HMRC say that there is one condition for the availability of consortium relief that they have not yet finished investigating. That element is the purpose for which certain steps were taken by the Appellants - steps which HMRC say may constitute a scheme that falls foul of the anti-avoidance provision. They want to continue investigating this and they therefore contend that there should be no closure notice issued.

5. The FTT (Judge McKeever) held that the arrangements identified by HMRC did not fall within the anti-avoidance provision so that the purpose for which they were made was irrelevant. She directed that a closure notice be issued: [2017] UKFTT 494 (TC). The Upper Tribunal (Snowden J and Judge Hellier) disagreed and held that the arrangements were potentially caught by the provision so that HMRC were entitled to continue to investigate the purpose behind the arrangements. The Appellants now appeal to this court with permission of the Upper Tribunal.

The legislation in more detail

6. A consortium is defined in section 153 CTA as follows:

> "(1) For the purposes of this Part a company is owned by a consortium if—
>
> (a) the company is not a 75% subsidiary of any company, and
>
> (b) at least 75% of the company's ordinary share capital is beneficially owned by other companies each of which beneficially owns at least 5% of that capital.

> (2) The other companies each owning at least 5% of the share capital are the members of the consortium for the purposes of this Part.
>
> (3) If—
>
> (a) a trading company is a 90% subsidiary of a holding company and is not a 75% subsidiary of any company apart from the holding company, and
>
> (b) as a result of subsection (1), the holding company is owned by a consortium,
>
> then for the purposes of this Part the trading company is also owned by the consortium."

7. A '75% subsidiary' is defined in section 151 by cross-referring to section 1154(3) so that it includes a subsidiary where at least 75% of its ordinary share capital is owned directly or indirectly by the consortium.

8. According to section 130 CTA, a claimant company may make a claim for group relief for an accounting period in relation to a surrendering company's losses if the following requirements are met: first, that the surrendering company consents to the claim; secondly, that there is an 'overlapping period' that is common to the claim period and the surrender period (as defined); and thirdly, that at a time during the overlapping period one of four other sets of conditions is met. It is not disputed that the first two requirements of consent and overlapping period are met here. The set of conditions with which we are concerned is referred to in the legislation as "consortium condition 3" and is set out in section 133(2) to (4). Only section 133(2) is relevant to this appeal. That provides for when consortium condition 3 is met:

> "(2) Consortium condition 3 is met if—
>
> (a) the claimant company is a trading company or a holding company,
>
> (b) the claimant company is owned by a consortium,
>
> (c) the surrendering company is not a member of the consortium,
>
> (d) the surrendering company is a member of the same group of companies as a third company ("the link company"),
>
> (e) the link company is a member of the consortium, . . . and
>
> (f) the surrendering company and the claimant company are both UK related. . ."

9. Section 137 CTA provides for the deduction for relief from the total profits of the claim period. Section 137(3) provides that the ability to deduct is subject to, amongst other things, the limitations set out in sections 143 to 149. The limits that apply to a

claim based on consortium condition 3 are set out in section 146(4) to (7). Section 146(6), by cross-referring to section 144(2), limits the amount of relief to what is called 'the ownership proportion' of the claimant company's available total profits of the overlapping period. The term 'the ownership proportion' is defined in section 144(3) (as modified in effect by section 146(6) for our purposes). This provides that the ownership proportion is the same as the lowest of the following proportions:

(a) the proportion of the ordinary share capital of the claimant company that is beneficially owned by the link company;

(b) the proportion of any profits available for distribution to equity holders of the claimant company to which the link company is beneficially entitled;

(c) the proportion of any assets of the claimant company available for distribution to such equity holders on a winding up to which the link company would be beneficially entitled; or

(d) the proportion of the voting power in the claimant company that is directly possessed by the link company.

10. As I have said, the Appellants rely on the fourth of those options, the proportion of the voting power in the claimant company which is directly owned by the link companies. That fourth option was added to section 144(3) by the Finance (No 3) Act 2010 but was in force for all the accounting periods with which we are concerned. It was added at the same time as section 146B which is at the heart of this appeal. Section 146B sets a further limitation on the amount of consortium relief that can be claimed. So far as is relevant it provides:

> "**146B Conditions 1 and 3: claimant company not controlled by surrendering company etc**
>
> (1) [dealing with claims based on consortium condition 1]
>
> (2) This section also applies if—
>
> (a) the claimant company makes a claim for group relief based on consortium condition 3, and
>
> (b) during any part of the overlapping period, arrangements within subsection (3) are in place which enable a person to prevent the link company, either alone or together with one or more other companies that are members of the consortium, from controlling the claimant company.
>
> (3) Arrangements are within this subsection if—
>
> (a) the company, either alone or together with one or more other companies that are members of the consortium, would control the claimant company, but for the existence of the arrangements, and

> (b) the arrangements form part of a scheme the main purpose, or one of the main purposes, of which is to enable the claimant company to obtain a tax advantage under this Chapter.
>
> (4) The group relief to be given on the claim is to be determined as if the claimant company's total profits for the overlapping period were 50% of what they would be but for this section (see section 140(2) to determine the total profits for the overlapping period)."

11. For the purposes of claims based on consortium condition 3, 'the company' referred to in subsection 3(a) is the link company. A 'tax advantage' referred to in section 146B(3)(b) is defined in section 1139 CTA as including a relief from tax or an increased relief from tax. 'Control' is defined for the purposes of section 146B by section 1124 as follows:

> ""control" means the power of a person ("P") to secure—
>
> (a) by means of the holding of shares or the possession of voting power in relation to that or any other body corporate, or
>
> (b) as a result of any powers conferred by the articles of association or other document regulating that or any other body corporate,
>
> that the affairs of company A are conducted in accordance with P's wishes."

It is accepted by the Appellants that for our purposes 'control' includes having enough votes at the company's general meeting to procure the passing of board resolutions.

12. It is common ground between the parties that the same "arrangements" must be examined under both subsection (2) and subsection (3) of section 146B. As Mr Peacock QC, appearing for the Appellants, put it, section 146B(3)(a) requires the court to suppose a counterfactual in which the arrangements being tested do not exist, whereas section 146B(2)(b) requires the court to consider the effect of the arrangements being in place.

The facts

13. The Appellants are all wholly-owned trading company subsidiaries of the company UK Power Networks Holdings Ltd ('UKPNHL'). They are therefore treated as also being owned by the consortium by virtue of section 153(3) CTA. They have earned profits during the periods covered by HMRC's enquiry, that is in the years ended December 2011, 2012 and 2013 and claimed in their tax returns to offset some of those profits using consortium relief relying on consortium condition 3.

14. UKPNHL was originally formed in June 2010 as a shell bid vehicle by three independent, though inter-related, investors for the purpose of acquiring the power transmission services business previously owned by the EDF Energy Group. The investors were the Hutchison Whampoa group which is a Hong Kong-based

international group listed on the Hong Kong stock exchange, Cheung Kong Infrastructure (which owns the company known at the time as Hong Kong Electric Company) and the Li Ka-Shing Foundation. The three initial shareholders in UKPNHL were Devin International Ltd ('Devin') which was owned by the Hong Kong Electric Company, Eagle Insight International Ltd ('Eagle') which was owned by the Li Ka-Shing Foundation and CKI Number 1 Limited ('CKI-1') which is a member of the Hutchison Whampoa group of companies.

15. When it was first acquired, UKPNHL had a basic set of articles of association, three issued shares held one each by Devin, Eagle and CKI-1 and equal voting rights. Between 11 September 2010 and 30 December 2010 there were various amendments to the rights of the UKPNHL shareholders. On 11 September 2010, the three shareholders entered into an agreement to settle the contributions each would make to fund the £3 billion needed to buy the EDF business and to set out the respective rights they would acquire if their bid were successful. The agreement was that Devin and CKI-1 would both put in 40% of the funding and own 40% each of the company and Eagle would contribute 20% and own 20%. The agreement provided that the proportions of votes at Board level were to be 49.5% to CKI-1, 16.8% to Eagle and 33.7% to Devin. This reflected the commercial intention, Mr Peacock said, that none of the three would control UKPNHL, regardless of their respective levels of contribution to the financing.

16. On 29 October 2010, once the acquisition of the EDF business by the consortium via UKPNHL had been completed, the parties entered into a new shareholders' agreement and a new set of articles of association was adopted. At this stage two new companies joined as shareholders, CKI Number 2 Limited ('CKI-2') and CKI Number 3 Limited ('CKI-3'). I refer to CKI-1, 2 and 3 as 'the CKI Companies"; they are all members of the same corporate group. The October shareholders agreement provided for a new share structure with A and B ordinary shares. The upshot of that agreement was that the ordinary share capital of UKPNHL was then owned as follows: 33.6% by CKI-1, 32% by CKI-2, 32% by CKI-3, 0.8% by Eagle and 1.6% by Devin. At that point Eagle and Devin dropped out of the consortium because they no longer owned at least 5% of the shares of UKPNH, so the members of the consortium were only the three CKI Companies. The percentage of votes held by the shareholders was varied by the new articles of association only slightly from previous position so that CKI-1 had 27.6% of the votes, CKI-2 and CKI-3 had 11% each, Eagle had 16.8% and Devin had 33.6%.

17. The October articles made an important change for the purposes of this appeal. The voting threshold in article 7.5 required to pass shareholder resolutions was increased from a simple majority (which for convenience I will call 50%) which had applied in the absence of any express provision on the matter in the original articles to 75% ('the 75% Voting Threshold'). The new article read:

> "Save to the extent not permitted by the [Companies] Act, any resolution of the company or the Members shall require a majority of 75% in order to be validly passed."

18. On 30 December 2010 UKPNHL adopted a further new set of articles of association. Through various changes to the voting rights, this caused the combined voting rights of the CKI Companies to increase from 49.6% to 74.6%, with CKI-1 holding 25.2%

of the votes, CKI-2 24.7% and CKI-3 24.7%. Eagle had 8.6% of the votes and Devin 16.9%. The other potential ownership proportions did not change so that after 30 December 2010 and during all the relevant overlapping periods the CKI Companies were the three members of the consortium which together with Eagle and Devin owned UKPNHL. The CKI Companies together held 97.6% of the ordinary share capital of UKPNHL and 74.6% of the votes. Also on 30 December 2010, CHKI-3 and the owner of Devin entered into a voting agreement, referred to in the decisions as the December Voting Agreement or 'DVA', by which CKI-3 promised that it would not exercise its votes in UKPNHL without the prior written consent of the other party to the agreement.

19. One of the other companies in the group of which all the CKI Companies are members was Hutchison 3G UK Holdings UK ('Hutchison UK'). It incurred significant expenditure over the relevant period in developing the 3G mobile network in the UK. It suffered considerable losses in the relevant years and those are the losses which Hutchison UK consented to surrender to the Appellants. All three CKI Companies are therefore link companies forming the link between the loss-making Hutchison UK and the profitable Appellants. The other potential ownership proportions set out in section 144(3)(a), (b) and (c) were said by the Appellants to be higher than the 74.6%, so that the lowest ownership proportion for the purposes of section 144(3) was the proportion of voting rights. The Appellants' claim for relief was therefore made adopting that proportion as the ownership proportion.

20. HMRC are pursuing their enquiry because they consider that section 146B(4) may apply to reduce the amount of relief available by treating the Appellants' total profits for the overlapping periods as if they were 50% of what they would otherwise be. The question is therefore whether any of the changes in the succession of shareholders agreements and articles of association amount to "arrangements" for the purposes of section 146B(2)(b) and (3)(a). If they do not, then there is no need for HMRC to continue their inquiries to determine the purpose of the scheme of which the arrangements form part. If they do, then HMRC do need to come to a view on the purpose.

The judgments below

21. The FTT decided many issues in addition to the ones which were the subject of the appeal to the Upper Tribunal and are now before us. Judge McKeever concluded that none of those other issues provided reasonable grounds for HMRC to continue with their enquiries which meant that the only justification for refusing to direct the issue of the closure notice was if HMRC needed to consider the purpose of the scheme. She then considered whether she should decide the legal issue raised by the case, that is whether there were arrangements falling within section 146B(2)(b) and section 146B(3)(a). The principal authority on the point is *Vodafone 2 v HM Revenue and Customs* [2006] EWCA Civ 1132, [2006] STC 1530. In that case Vodafone had applied for a closure notice in relation to an enquiry into whether certain profits should be apportioned to the taxpayer company pursuant to the tax provisions relating to controlled foreign companies. The issue in the enquiry was whether the taxpayer was right to contend that an exemption from those provisions applied. However, Vodafone raised a more fundamental point that the tax provisions themselves were contrary to EU law. Vodafone applied to the Special Commissioners for a closure notice direction on the ground that because the legislation to which the enquiry related

was contrary to EU law, there was no basis for the enquiry to continue. There was no doubt that the issue of compatibility needed to be determined in order to decide whether they should direct HMRC to issue a closure notice. The Court of Appeal held that the Special Commissioners did have jurisdiction to decide an incidental question of law in the course of deciding whether to direct the issue of a closure notice.

22. Judge McKeever then went on to consider whether, since she had jurisdiction to do so, she should exercise her discretion to decide the point of law in the case before her. She recorded the submissions of Ms Lemos for HMRC that it was neither necessary nor appropriate for the FTT to decide the question of law. Ms Lemos had argued that the novel issues raised by section 146B could not be analysed in the abstract but required highly specific, highly detailed enquiries into the facts: [175]. Mr Peacock had argued that the legal issues were fundamental to the enquiry and were pure questions of law that could be determined on the basis of agreed facts. Judge McKeever concluded that the outstanding information notices were all concerned with the reasons and purposes behind certain actions, by which she meant that they all related to whether section 146B(3)(b) was satisfied. At [232] she decided that she should decide the point:

> "232. I have concluded that none of the other issues discussed above provide reasonable grounds for the Respondents to continue with their enquiries which means that this issue: the relevance of purpose, is fundamental to the enquiry. If the applicants' construction of section 146B is correct, purpose is not relevant. If the Respondent's interpretation is correct, purpose is relevant. This is precisely the sort of question which Park J had in mind in *Vodafone 2*. If the Tribunal decides the question of law, it will determine the application for the closure notice."

23. The first step then was to identify the arrangements. She recorded Ms Lemos' submission that the arrangements consisted of the increase in the voting threshold from the original 50% to 75% and the December Voting Agreement: [243]. She rejected the contention that the December Voting Agreement was part of the arrangements and there has been no appeal against that part of her decision. She held that the relevant arrangement was the increase in the voting threshold to 75%: [256].

24. The next question was what was meant by the requirement in section 146B(3)(a) that the CKI Companies as the link companies would have controlled the Appellants, 'but for' that arrangement. The Appellants argued that the test required a loss of pre-existing control and that here the test was not met because the CKI Companies had never at any point controlled UKPNHL. Judge McKeever rejected this argument:

> "267. I agree with Ms Lemos that the language of section 146B(3)(a) does not require pre-existing control. The purpose of section 146B is to prevent consortia and others implementing arrangements of the prescribed kind which confer a tax advantage. The arrangements may be put in place at the outset, before anyone had any control to lose. The enquiry demanded by section 146B(3)(a) is whether there are

> arrangements, and if so, whether the consortium would control the claimant if the arrangements were not there."

25. She held that since the CKI Companies now held 74.6% of the votes in UKPNHL, they would control it if the voting threshold had not been raised from 50% to 75% by the October articles of association. The test in section 146B(3)(a) was met. Judge McKeever then considered whether the arrangements also fell within section 146B(2)(b). She held that this condition was not satisfied because the arrangements did not enable Eagle and Devin to prevent the CKI Companies from controlling the Appellants. She said at [273]:

> "If either Eagle or Devin vote with the CKI companies they could pass a resolution. But this does not mean that if both Eagle and Devin vote against the consortium it can be said that the arrangements (the increase in the threshold) have "enabled them to prevent" the CKI companies exercising control because they simply do not have control. That is the position in any company where a shareholder has, or group of shareholders have, a minority interest under the Articles of Association. By definition, they cannot control the company. It is pushing the language of subsection (2) too far to say that the ability of the other shareholders to vote against the minority enables them to prevent the minority from controlling the company."

26. She therefore concluded there was no person enabled by the increase in the voting threshold to prevent the CKI Companies from exercising control of the claimants. The increase in voting threshold was not an arrangement to which section 146B applied because section 146B(2)(b) was not satisfied. That made it unnecessary for HMRC to enquire into the purposes of the scheme so she directed HMRC to issue a closure notice within 30 days of the release of the decision.

27. There was an appeal by HMRC on the section 146B(2)(b) issue and a cross-appeal by the Appellants on the section 146B(3)(a) issue. The Upper Tribunal described the "arrangements" relied upon by HMRC as being either (i) the 75% Voting Threshold by itself; or (ii) the combined effect of the 75% Voting Threshold and the votes of Devin and Eagle which together amount to 25.4% of the voting rights at UKPNHL's general meetings: [46].

28. The Upper Tribunal started its analysis at [50] and [51] with an example of a case which would plainly be caught by section 146B if the necessary purpose were established. This was where a company which has a subsidiary with tax losses is invited to join a consortium with two others; it subscribes for the majority of the shares but agrees with the existing members that it will only cast the votes attached to those shares if one of the existing members consents. In that case the "arrangement" would be the voting agreement which enabled the existing shareholders party to the agreement to stop the new member from exercising its majority of votes.

29. The Upper Tribunal then dealt with the Appellants' argument that something like the 75% Voting Threshold that was part of the company's articles of association could not be an 'arrangement' within the meaning of the section. They concluded at [66] that the 75% Voting Threshold in article 7.5 was capable of falling within the

meaning of the term 'arrangements' for the purposes of section 146B. They disagreed with the conclusion of Judge McKeever on section 146B(2)(b):

> "71. So, as a matter of ordinary language, we consider that arrangements might be said to prevent a consortium company from "controlling" a company in either of two situations. The first is if the consortium company holds sufficient voting power to pass resolutions under the company's constitution, but the arrangements impose an external constraint upon the exercise of that voting power so that the consortium company cannot be certain that its wishes will prevail. That situation is the one given in the example in paragraphs 50 and 51 above.
>
> 72. The second situation is if the arrangements operate internally under the company's constitution so that the voting power of the consortium company is inadequate to assure it of passing the resolutions necessary to give effect to its wishes. In either case it could be said, without doing violence to the statutory language, that the consortium company is prevented from "controlling" the company by its voting power, and that the arrangements enable another person or other persons to prevent it controlling the claimant company.
>
> 73. Specifically, and as applied to the instant case, we consider that it is entirely in accordance with the language and structure of s.146B(2)(b) to say that the existence of the 75% Voting Threshold in Article 7.5 enables Eagle and Devin to prevent the CKI companies from having the power to secure that the affairs of UKPNHL are conducted in accordance with their wishes, because even with 74.6% of the voting power, the CKI companies cannot be sure of being able to pass a resolution of UKPNHL."

30. The Upper Tribunal did not regard that conclusion as 'pushing the language of subsection (2) too far' as Judge McKeever had thought. They recognised that Parliament cannot have intended that every time a shareholder has a minority interest in a company, section 146B would be satisfied because the other shareholders are 'enabled' by their votes to 'prevent' the minority shareholder from controlling the claimant company. The potential width of the class of arrangements falling within section 146B(2)(b) was reduced by the two requirements in section 146B(3): "Approaching the structure of the section in that way means that there is no reason to construe s.146B(2)(b) restrictively, because potential anomalies which might arise if regard were only had to s.146B(2)(b), are in fact limited or removed by the operation of s.146B(3)": [78]. They therefore held that the FTT had erred in finding that the arrangements constituted by article 7.5 of the UKPNHL articles of association did not satisfy section 146B(2)(b).

31. The Upper Tribunal upheld the FTT's conclusion that section 146B(3)(a) was satisfied. The conclusion was strongly reinforced by the point made by the FTT that section 146B must be capable of applying to arrangements which are in place from the outset of the life of a consortium where there has been no pre-existing control to

be lost: "To read the section otherwise would be to create a large hole in the legislation for no apparent legislative purpose." They concluded that the arrangements constituted by the 75% Voting Threshold satisfied the requirement in section 146B(3)(a) because, had that provision not been in the articles of UKPNHL, the CKI Companies would have controlled UKPNHL during the overlapping periods. They therefore allowed the appeal, dismissed the cross appeal and set aside the direction made by the FTT.

The appeal

32. The Appellants rely on three grounds of appeal. The first ground is that the Upper Tribunal failed properly to identify the relevant arrangements for the purposes of section 146B(2)(b) and section 146B(3)(a) because they referred at some points to the arrangement being the 75% Voting Threshold by itself and at some points to the combined effect of the 75% Voting Threshold and the minority votes holdings of Devin and Eagle. Ground 2 contends that the Upper Tribunal was wrong to hold that section 146B(2)(b) should be given a broad interpretation to be cut down only by the effect of section 146B(3). Ground 3 argues that the Upper Tribunal's interpretation fails to give any meaning to the requirement in section 146B(2)(b) that the arrangements enable a person to prevent the link company from controlling the claimant company. In their respondent's notice, HMRC invite this court, in so far as it is necessary, to uphold the decision of the Upper Tribunal on the ground that the arrangements encompass the parties' share rights, by which I assume they mean their voting rights, as well as the 75% Voting Threshold itself.

33. In fact during the course of argument it became clear that the Appellants were attacking the Upper Tribunal's conclusion both that section 146B(2)(b) and that section 146B(3)(a) were satisfied, or at least were arguing that there is no single definition of arrangement in this case that can satisfy both tests. It was also clear that Mr Ewart QC appearing for HMRC relied primarily on the arrangement being the 75% Voting Threshold by itself, without needing to rely on the combination of that and the voting rights of the minority shareholders.

The content of the 'arrangements' in this case

34. Mr Peacock confirmed that he was not now asserting that an article in the claimant company's articles of association could not as matter of principle constitute an arrangement for this purpose. It was also common ground that the term 'arrangements' used in section 146B includes an arrangement comprising a single item.

35. I can dispose briefly of one criticism made by Mr Peacock which was that the Upper Tribunal misunderstood the decision of the FTT and were wrong to say that they were agreeing with and upholding the FTT's analysis on section 146B(3)(a). The FTT's analysis was, he argued, based on the case presented by HMRC to the FTT that the arrangement comprised 'the *increase* in the voting threshold to 75%' whereas the case presented to the Upper Tribunal by HMRC and that the Upper Tribunal accepted was that the arrangement comprised the 75% Voting Threshold *itself*. This seems to me a distinction without a difference. The actual increase in the voting threshold which took place when the new articles of association were adopted occurred only on 29

October 2010 – that was not the arrangement but was the setting up of the arrangement, the arrangement being the ongoing 75% Voting Threshold.

36. It is also useful to state at this point that I am satisfied reading the Upper Tribunal's decision as a whole that they approached the application of section 146B on the basis that the arrangement being tested was the 75% Voting Threshold and not a combination of that plus the minority shareholders' votes. They were right to do so. The relevant arrangement here, at least at this stage of HMRC's enquiry, is the fact that the voting threshold set by article 7.5 of UKPNHL's articles of association requires a majority of 75% of the votes before a resolution can be passed at general meeting.

Applying section 146B(3)(a)

37. The structure of section 146B requires the two limbs of subsection (3) to be applied to the arrangements first, because section 146B(2)(b) only comes into play if arrangements within subsection (3) are in place during any part of the overlapping period. Applied to the facts of the present appeal, the question posed by section 146B(3)(a) is whether the CKI Companies (being the link companies) would control UKPNHL but for the existence of the 75% Voting Threshold. That test requires the comparison of the situation with the arrangement in place with the situation where the arrangement does not exist. What would be the situation here but for the 75% Voting Threshold? It would be that the CKI Companies would have 74.6% of the votes, in accordance with the articles of association adopted on 30 December 2010, but that the voting threshold would still remain at 50% because the article 7.5 adopted in October 2010 would not exist. In that counterfactual world, there seems to me no doubt that the CKI Companies would control UKPNHL and hence the Appellants.

38. Mr Peacock argues that this analysis ignores the fact that the 'but for' test in section 146B(3)(a) requires a causative link between the removal of the arrangement from the counterfactual and the absence of control. He was not maintaining that there needs to have been previous control for the purposes of section 146B(3)(a) though he did still argue that that was needed for section 146B(2)(b). He argued that it was common ground that on the facts of the present case, the existence of the 75% Voting Threshold did not *cause* control of UKPNHL to change. At no time had the CKI Companies had control, whether one regarded the voting threshold applicable in the counterfactual as being the pre-October 2010 voting threshold or the 50% threshold that applies by default in the absence of any contrary provision in a company's articles. One cannot say, in the present case, that the 75% Voting Threshold caused the link companies' lack of control and that causative requirement is what section 146B(3)(a) is designed to impose.

39. In my judgment there does not need to be a causative link any more complicated than that expressly required by the wording of the provision, namely that in the absence of the 75% Voting Threshold, the CKI Companies hold enough votes (i.e. over 50%) to control UKPNHL. I therefore reject the submission that the Upper Tribunal erred in failing to apply a causative test in section 146B(3)(a). They applied the test that is required by the provision by comparing the position with and without the 75% Voting Threshold and determining that since the CKI Companies had no control with the arrangement in place but would have control in the absence of the 75% Voting Threshold, the test was satisfied.

40. The Appellants argue further that the Upper Tribunal erred because it is not permissible to assume that in the hypothetical world in which the voting threshold was not increased in October 2010, the consortium members would still have increased the CKI Companies' votes to 74.6% in the December revisions. If one disregards the increase in the voting threshold, one must also disregard the increase in votes because this accords with the commercial understanding between the respective parties that none of the CKI Companies, Devin or Eagle was intended to have sufficient votes to pass resolutions unilaterally. That is not, in my view, what the section requires. The increase in the CKI Companies' voting power from 49.5% to 74.6% is not part of the arrangement being tested and so does not fall to be disregarded when constructing the counterfactual in section 146B(3)(a). I cannot improve on the reasons given by the Upper Tribunal when rejecting the same argument put to them:

> "93. … we consider that the statutory wording of s.146B(3)(a) – "but for the existence of" does not invite attention to the process by which the arrangements were put into place, or invite a speculative inquiry into what would have happened if they had not been put in place. The natural reading of the "but for the existence of" test is one that simply requires it to be postulated that the arrangements are not in existence at the relevant time. There is a clear contrast with s.146B(3)(b) which does invite an inquiry into the purposes for which the arrangements were introduced.
>
> 94. That conclusion is also consistent with what we understand to be the structure and purpose of the different sub-sections of s.146B. As we have explained, s.146B(2)(b) starts by identifying the type of arrangements which are intended to be caught, and s.146B(3) then limits the scope of that net. In other words, the purpose of the "but for the existence of" test in s.146B(3)(a) is to eliminate from the scope of s.146B a case in which, at the relevant time, there is some reason other than the arrangements in question, which stops the consortium companies from controlling the claimant company."

41. The Appellants' submission begs the question: why was the voting share of the CKI Companies raised by the December changes to the articles of association, given that the increase had no effect on the control of UKPNHL? That is precisely the question that HMRC wish to investigate further under section 146B(3)(b). One cannot ignore the increase of voting rights from 49.5% to 74.6%, since that is the basis on which the Appellants assert that the lowest ownership proportion for the purposes of section 144(3) is 74.6% rather than 49.5% and hence that their entitlement to consortium relief is higher than it would have been if the voting threshold had not been changed.

Applying section 146B(2)(b)

42. The question posed by section 146B(2)(b) is whether during any part of the overlapping period, the 75% Voting Threshold enabled a person to prevent the CKI Companies from controlling UKPNHL. Again, I do not see any difficulty in saying that with the 75% Voting Threshold in place, Eagle and Devin are enabled to use their

25.4% of the voting rights to prevent the CKI Companies from controlling UKPNHL. If the voting threshold had stayed at 50% and the CKI Companies had 74.6% of the votes, Eagle and Devin would not be able to prevent that.

43. Mr Peacock argued that the use of the word 'enable' in the provision indicates that Parliament intended that there should be a loss of pre-existing control by the link companies. Here, the CKI Companies never had control of UKPNHL, not under the June 2010 articles nor the 29 October 2010 articles nor the 30 December articles. That reflected the wider commercial deal between the parties which was that none of them should have control over the venture.

44. I agree with the reasoning of the Upper Tribunal that there is no requirement that the link company at some point had control which was lost as a result of the arrangement being put in place. As the Upper Tribunal recognised, this would make it easy for claimant companies to avoid the application of the provision by setting up the articles of association to achieve the desired result from day one or to sequence the changes as the parties have done here so as to avoid control ever being conferred on the link company. The paradigm case at which section 146B is aimed may well be that posited in argument by Mr Peacock and by the Upper Tribunal at [50] and [51], namely where the link company holds a sufficient majority of the votes in the claimant company to pass a resolution itself but enters into a voting agreement with another shareholder not to exercise those votes otherwise than in accordance with the other shareholder's wishes. However, shareholders have a variety of mechanisms by which they can allocate whatever financial and controlling interests amongst themselves that they want; by issuing different classes of shares with different rights attached, by providing in the articles of association that resolutions concerning specified matters require a larger majority of votes to be adopted than others, or by entering into side agreements as to how they will exercise such rights as they have. Mr Peacock fairly accepted that anti-avoidance provisions such as section 146B must be drafted so that they apply not only to the paradigm case but to the other ways in which the same effect can be achieved. That is what the drafter has attempted here and it would be a poor attempt if it could be side-stepped as easily as the Appellants contend.

45. I also agree with the point made by Mr Ewart that if a loss of pre-existing control during the overlapping period was required in order for section 146B(2)(b) to be satisfied, the provision could never apply to more than one overlapping period. If control were lost within the first overlapping period so that the provision applied to that period, there would be no further loss of control in any subsequent overlapping period so the test would not be met. That cannot be what Parliament intended.

46. A point was raised during argument about whether the reference to 'a person' in section 146B(2)(b) can be read as 'persons' applying section 6(c) of Interpretation Act 1978 or whether a contrary intention appears from the use of the expanding words "either alone or together with one or more other companies which are members of the consortium". That expanding wording attaches to the link company but not to the enabled 'person'. It cannot be right that the section only applies where a single person is enabled to prevent control. The expanding words are needed in respect of the link company because those other members of the consortium who jointly control the claimant company might not themselves be link companies and so would not be

included simply by treating the phrase 'the link company' as including 'the link companies'. They do not indicate that 'a person' is limited to the singular.

47. That does not entirely solve the problem identified by Mr Peacock which is that here Eagle and Devin are not just two persons each of which can prevent the link company from controlling the claimant. One must aggregate their voting rights against the CKI Companies in order for them to prevent the CKI Companies from controlling UKPNHL. Mr Peacock argued in reply that because the blocking 25.4% of the votes was split between Devin and Eagle, there was no person or persons able to prevent the CKI Companies from controlling UKPNHL. They could each only do so with the cooperation of the other. If there was an agreement between them to vote their shares together then that would be a separate element in the arrangement. In the absence of any such agreement between them, neither of them alone is enabled by the 75% Voting Threshold to prevent the CKI Companies from controlling UKPNHL.

48. Mr Ewart argued that there is no need to identify a particular person who is enabled to prevent the link company from controlling the claimant. All that one needs to know is that the link companies here have 74.6% of the votes and there is an arrangement in place which sets the voting threshold at 75%. That means that there must be other holders of voting rights who have the ability to stop them. He argues therefore that it does not matter that there is no single person who acting alone could block the CKI Companies from controlling UKPNHL. The fact that there are other vote holders who could, if they voted together, defeat the link company is enough to satisfy the test – they are each enabled to prevent control.

49. Although the wording of the provision could be clearer, I have concluded that Mr Ewart must be right. It would not make sense to limit the application of section 146B(2)(b) to a situation where the link company had votes just short of the voting threshold and the blocking share of the vote was held by one single, other person. Again, that would make it very simple for consortium members to avoid the application of the provision and require, in each case where the blocking tranche of votes was split between more than one non-consortium member, the existence of some agreement between them as to how they would cast their votes before the provision could come into play. The wording of the provision does not suggest that Parliament envisaged that one would need to investigate the question as to how likely or unlikely it is that those other vote holders will vote in the same way on any particular issue so as to defeat the link companies. The provision works as it must have been intended to do where there is one or more link companies whose votes are aggregated when arriving at the lowest ownership proportion. On the other side of the equation there may be one or more "enabled persons" and one must aggregate their votes to determine whether there is a person or whether there are persons who are enabled by the arrangement to prevent control.

50. This also, in my judgment, provides the answer to Mr Peacock's further submission that there is no possible content of the 'arrangements' here that can satisfy both section 146B(2)(b) and section 146B(3)(a). Looking at section 146B(2)(b) first, Mr Peacock submits that if one asks what is it that enables Eagle and Devin to block the CKI Companies from using their 74.6% share of the votes to control UKPNHL, the answer is that two elements are necessary. The first element is the fact that the voting threshold is set at 75% and the second element is that Eagle and Devin together have 25.4% of the votes. For the arrangements to pass through the gateway of section

146B(2)(b), therefore, the 'arrangements' being tested must contain those two components and section 146B(2)(b) would not be met if the arrangement comprised the voting threshold alone. But if that is right, Mr Peacock said, when one comes to apply the gateway in section 146B(3)(a), one has to consider the position in the absence of the whole arrangement, including both the absence of the 75% Voting Threshold and also the absence of Eagle and Devin's 25.4% shareholding as well. This leads to a nonsensical 'but for' counterfactual where the voting threshold remained at 50% but the only votes are the 74.6% of the votes held by the CKI Companies. Section 146B(3)(a) therefore only works if one treats the arrangement as limited to the single element of the 75% Voting Threshold by itself. Then one can say that if the voting threshold had not been increased to 75% the position would now be that the voting threshold would be 50% and the CKI Companies with their 74.6% of the votes would be able to control UKPNHL. But conversely, that single element 'arrangement' which works for section 146B(3)(a), does not get through the gateway of section 146B(2)(b) because the reason why Eagle and Devin are enabled to prevent CKI Companies from controlling UKPNHL is not only because of the voting threshold, but also because they hold 25.4% of the votes.

51. The fallacy of this argument lies in the first proposition. I do not consider that one needs an arrangement combining the two elements in order to get through the section 146B(2)(b) gateway. One can readily apply section 146B(2)(b) to the arrangement comprising only the 75% Voting Threshold without needing to add in the votes of Eagle and Devin as part of the arrangement. It is the voting threshold together with the fact that the CKI Companies hold only 74.6% of the votes that enables other persons, in this case Eagle and Devin combined, to prevent them from controlling UKPNHL.

52. In my judgment therefore there is an arrangement here, namely the 75% Voting Threshold, that satisfies both section 146B(2)(b) and section 146B(3)(a). HMRC must therefore continue their enquiries to determine whether that arrangement forms part of a scheme which has the purpose specified in section 146B(3)(b). I would therefore uphold the decision of the Upper Tribunal and dismiss the appeal.

The procedure followed in this application

53. Mr Peacock acknowledged rather wryly at the start of his oral submissions that if the Appellants hoped that their request to the FTT to determine this issue of law would bring their dispute with HMRC to a swift end, then that hope has really not been fulfilled. I certainly agree with that. Instead of speeding things up, it has led to HMRC's enquiries becoming stalled for over four years. We are now 11 years on from the relevant events and over seven years on from the start of HMRC's enquiries. If my Lords agree with me that we should uphold the Upper Tribunal's decision, HMRC will now have to pick up the threads and to come to a conclusion on whether there needs to be any amendment to the Appellants' tax returns. If they amend those returns to reduce the consortium relief claimed, the Appellants may well challenge that before the FTT and, given the amount of money involved and the likely complexity of the issues, that decision may well then make its way up to one or more appellate levels.

54. The *Vodafone* case was a very particular instance where the legal issue was not simply one among many issues that was raised by the construction of anti-avoidance

legislation. It was, as Arden LJ said, a point that was so fundamental as to be capable of bringing the enquiry to a halt if decided in a particular way: [26]. In my judgment, the jurisdiction to decide an incidental point of law in an application for a closure notice direction is useful, as the *Vodafone* case shows, but only if the discretion to exercise it is used sparingly. The position that we have found ourselves in this appeal demonstrates why. It will very often be the case that a statutory provision sets a number of cumulative conditions to be satisfied before it applies. Some of those conditions may be relatively straightforward and require little information from the taxpayer and some may require more extensive information. Taxpayers should not be encouraged to pick and choose which information they provide and then ask the tribunal to decide the applicability of one element in the hope that a "quick win" will bring the rest of the enquiry to a halt. That is a recipe for inefficient, stop/start enquiries and risks wasting a great deal of judicial time. Judge McKeever undertook a detailed analysis of the information requests and received written and oral evidence from the HMRC officer as to the relevance of the information requested and the history of the enquiry. Although Judge McKeever said that it was not necessary to set out the history in detail, her summary exposition nevertheless took up several pages of her decision.

55. The issue determined by this application does not resolve the entire dispute between the parties. Even if the Appellants had succeeded in showing that there were no arrangements here for the purposes of section 146B, we were told that HMRC have other points they can pursue on the accuracy of the Appellants' tax returns, one of which is that there are arrangements here falling foul of a different anti-avoidance provision, section 155. That would result in the entitlement to loss relief being set at nil because UKPNHL would not be regarded as being owned by a consortium at all. There seem to be various scenarios possible at the end of the enquiries that will mean that this whole exercise has been pointless.

56. The approach adopted in this application has also required the tribunals and this court to apply the statutory provision in the absence of any clear findings of fact about the scheme as a whole and without any agreed statement of facts. We raised with the parties at the hearing what would have been the position if the FTT had decided that the arrangements did potentially fall within section 146B and the Appellants had later brought a substantive appeal before the FTT against the amendment of their returns. What would be the status of the FTT's decision on this legal point when the same issue came to be debated in the substantive appeal once all the facts were known? The discussion quickly ran into the choppy waters of legal precedents and issue estoppel.

57. I would therefore firmly discourage the FTT from embarking on the kind of hearing that occurred here. There is a separate route by which a taxpayer can challenge an information notice served by HMRC if it regards the notice as disproportionate or unfair. The jurisdiction conferred on the tribunal to direct HMRC to issue a closure notice is not generally a suitable vehicle for deciding points of law in the course of an enquiry such as the present.

Lord Justice Dingemans:

58. I agree.

Lord Justice David Richards:

59. I also agree.