Appeal number: FTC/05 & 83/2010
[2012] UKUT 42 (TCC)

Corporation tax – capital allowances – machinery or plant – conversion, fitting out and refurbishment of public houses – whether items of cost qualify for allowances under section 24 CAA 1990 or section 66 CAA 1990 (or both) – consideration of what amounts to alterations to an existing building incidental to the installation of machinery or plant – decision in principle on sample expenditure –

UPPER TRIBUNAL
TAX CHAMBER

J D WETHERSPOON PLC **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S

REVENUE AND CUSTOMS (*Corporation Tax*) **Respondents**

Tribunal: Mr Justice Briggs
Howard M Nowlan

Sitting in public

Julian Ghosh QC, James Henderson and Jonathan Bremner of Counsel, instructed by Deloitte LLP, for the Appellant Company

Timothy Brennan QC and Rupert Baldry QC of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This is an appeal (or appeals) from two successive decisions in the same proceedings of Mr Theodore Wallace and Mr John Walters QC, sitting in June 2007 as Special Commissioners and in June 2009 as the First-Tier Tribunal (Tax Chamber). We will refer to them, respectively, as "the First Decision" and "the Second Decision" and collectively as "the Decisions".

2. The Decisions resolved appeals by J D Wetherspoon plc against the disallowance by HMRC of claims for capital allowances for expenditure on the fitting out and refurbishing of public houses which had originally been made in its revised corporation tax return for the accounting year to 31 July 1999, and disallowed in a closure notice dated 14 May 2003. The effect of the closure notice was to adjust downwards the expenditure in that year on qualifying allowances in respect of building costs, professional fees and head office costs from some £33.7 million odd to some £17.5 million odd.

3. The disputed claims related to a large number of JDW's public houses, but the parties sensibly agreed to limit the purview of the Special Commissioners to two pubs as test cases, namely the Prince of Wales, in Cardiff and First Post, in Cosham (near Portsmouth). The aggregate value of the disputed items was, nonetheless, still £0.5 million odd in relation to the Prince of Wales and some £84,000 odd in relation to the First Post. Each of these aggregates related to a large number of individual disputed items in each pub.

4. In delivering the First Decision, the Special Commissioners sensibly confined their review still further, so as to focus their reasoning upon a much smaller number of specific items, in the expectation (which proved to be unfounded) that the parties would be able to resolve the remainder by the application of the principles applied by the Special Commissioners in relation to those few.

5. That approach did lead to a substantial narrowing of issues (subject of course to appeal) as to the effect of the principles applied in the First Decision upon the other items in dispute. Nonetheless, there remained a substantial body of what were described in the Second Decision as "unclear items", which the First-Tier Tribunal then dealt with, but only in relation to the Prince of Wales pub, in the Second Decision. For this purpose they relied upon the evidence (including cross-examination) deployed at the hearing in 2007, together with further submissions of counsel on the unclear items.

6. Neither party was content with the Decisions. There has therefore been an appeal by JDW and a cross-appeal by HMRC. Consistent with the approach taken at the 2009 hearing, the factual purview of the appeal and cross-appeal has been limited to the Prince of Wales pub.

7. The matters in dispute before us were argued, and may conveniently be addressed, under the following three headings:

   A. Plant or Premises – section 24

   B. Incidental Expenditure – section 66

   C. Apportionment of Preliminaries

8. Under A, JDW appeals on the ground that the Decisions wrongly categorised four decorative items included within the fit-out of the public parts of the Prince of Wales as failing to qualify as plant because they had become part of the premises. The items in question consisted of panelling, cornices and architraves and metal end-pieces to balustrades.

9. Under B, JDW complained that the decisions adopted an incorrectly narrow construction of the phrase, in section 66, "capital expenditure on alterations to an existing building incidental to the installation of machinery and plant for the purposes of the trade", and thereby excluded expenditure on substantial parts of the kitchen and toilet areas constructed and fitted out at the Prince of Wales. For its part HMRC supported the construction of section 66 applied in the Decisions, but complained that, in respect of certain items in the kitchen and toilet areas, that construction had not then been applied, in one instance by reason of irrationality in the Tribunal's approach to the evidence.

10. Under C, HMRC cross-appeals on the ground that the Tribunal was wrong to permit expenditure on certain preliminary items to be apportioned by reference to the ratio between qualifying and non-qualifying (for capital allowances) works within the project for refurbishment of the Prince of Wales as a whole, upon the ground that since those items were "trade-specific" it was incumbent on JDW to prove the precise amount of them expended upon qualifying works.

The Prince of Wales

11. In order to set this litigation about particular items of expenditure in a large project in its proper context, it is convenient briefly to describe the works at the Prince of Wales as a whole. JDW has a substantial reputation for the conversion of existing buildings of various types into large public houses. The building which is now the Prince of Wales pub was previously a theatre, and what the Tribunal described as an outstanding listed building. Its conversion into a prestigious pub took some eighteen months, and included the provision of a new toilet area, and an entire new floor including a new bar and a new kitchen area. It was one of some 288 fit-out projects being undertaken by JDW during the tax year in question. The process involved not merely refurbishment but the creation within the building of entire new rooms, requiring the erection of new walls, floors and ceilings as well as the replacement at basement level of floors by new,

stronger floors. Both in the main public areas and (in particular) in the ladies' toilet area, JDW went to considerable lengths to provide an appealing 'ambience' for the purposes of attracting customers.

A. Plant or Premises – section 24

12. Section 24 of the Capital Allowances Act 1990 (which was in force at the material time) provides, so far as is relevant, as follows:

> "(1) Subject to the provisions of this Part, where –
>
> (a) a person carrying on a trade has incurred capital expenditure on the provision of machinery or plant wholly and exclusively for the purposes of the trade and
>
> (b) in consequence of his incurring that expenditure, the machinery or plant belongs or has belonged to him,
>
> allowances and charges shall be made to and on him in accordance with the following provisions of this section."

In relation to machinery or plant, the allowance was 25 % per annum on a reducing balance basis. No allowance was given for capital expenditure on buildings to be used as public houses.

13. It is common ground that the requirements of sub-section (1)(b) are satisfied in relation to the disputed items and that JDW incurred capital expenditure on them wholly and exclusively for the purposes of its trade. The question in issue is whether JDW's expenditure on those items constituted expenditure "on the provision of …plant".

14. Neither the 1990 Act nor any of its predecessors ever provided a definition of plant, but a considerable body of case law made good that deficiency. Some non-exhaustive assistance is now to be found in Schedule AA1, which was inserted by the Finance Act 1994, with effect after 29 November 1993. So far as is relevant, it provides as follows:

> "1. (1) For the purposes of this Act expenditure on the provision of machinery or plant does not include any expenditure on the provision of a building.
>
> (2) For the purposes of this Schedule "building" includes any asset in the building -
>
> (a) which is incorporated into the building, or
>
> (b) which, by reason of being movable or otherwise, is not so incorporated, but is of a kind normally incorporated into buildings;

and in particular includes any asset in or in connection with the building included in any of the items in column 1 or column 2 of the following Table ("Table 1").

(3) Sub-paragraph (1) does not affect the question whether expenditure on the provision of –

(a) any asset falling within column 2 of Table 1,

…

is for the purposes of this Act expenditure on the provision of machinery or plant.

(4) Table 1 is to be read subject to the notes following it."

15. Column 1 (of Table 1) headed "Assets included in the expression "building" " includes the following six classes:

A. Walls, floors, ceilings, doors, gates, shutters, windows and stairs.

B. Mains services, and systems of water, electricity and gas.

C. Waste disposal systems.

D. Sewerage and drainage systems.

E. Shafts and other structures in which lifts, hoists, escalators and moving walkways are installed.

F. Fire safety systems.

16. Column 2 (headed "Assets so included, but expenditure on which is unaffected by the Schedule") consists of a diverse list of sixteen categories ranging from movable partition walls to swimming pools and including, in particular:

"14. Decorative assets provided for the enjoyment of the public in the hotel, restaurant or similar trades".

In the Notes referred to in paragraph 1(4) there is included the following:

1. An asset does not fall within column 2 if its principal purpose is to insulate or enclose the interior of the building or provide an interior wall, a floor or a ceiling which (in each case) is intended to remain permanently in place."

17. We were initially puzzled as to the reason for the elliptical nature of column 2 of Table 1 which lists items which are apparently to be included in the expression "building" but then removed from the ambit of paragraph

1 (1) by paragraph 1(3)(a). Mr Timothy Brennan QC for HMRC told us (with the apparent agreement of Mr Julian Ghosh QC for JDW) that most of the categories in column 2 were included as a form of shorthand reference to decided cases on items of that kind, so as to assist practitioners in this potentially intricate field at a time when decisions of the Special Commissioners were not routinely available in published form, as they, and those of their successors the FTT, have since become. We accept that explanation. For example, item 14 in column 2 is plainly a reference to the decision of the House of Lords in *Commissioners of Inland Revenue v Scottish & Newcastle Breweries* (1982) 55 TC 252 in which decorative items including bagpipes, pistols, deerskins and murals screwed to the walls of a hotel and a sculpture representing seagulls in flight in the forecourt were all held to be plant rather than part of the premises.

18. That unusual use of column 2 of Table 1 as a signpost to, or summary of, decided cases on the occasionally difficult borderline between plant and premises reflects the fact that, although the issue ultimately turns upon statutory construction, it is to the essentially judge-made interpretation of the meaning of "plant" in its context as part of section 24 and its predecessors that it is necessary to turn.

19. For present purposes, counsel were substantially in agreement that the entirety of the relevant authority is to be found summarised and re-stated in the judgments of Hoffmann J and the Court of Appeal in *Wimpy International Ltd v Warland* (1988) 61 TC 51, a case about expenditure on the improvement and modernisation of fast-food and pizza restaurants. The items in dispute consisted principally of improvements such as floor and wall tiling, glass shop fronts, raised and mezzanine floors, staircases and false ceilings (see page 83G). They also included, relevantly for present purposes, a particular type of wall panelling: see page 67F.

20. Hoffmann J began by re-stating the threefold test for the identification of plant originally promulgated by Lindley LJ in *Yarmouth v France* (1887) 19 QBD 647, at 658, namely that:

    (1) The item should not be part of the trader's stock in trade.

    (2) That it should be used for the carrying on of the trader's business (the business use test).

    (3) That it should not be used as the premises or place upon which the business is conducted (the premises test).

    See page 82 D to E. Thus, an item which was not stock in trade and which passed the business use test would nonetheless fail to qualify as plant if it failed the premises test. The central issue in the *Wimpy* case, and in this part of the present appeal, is whether the disputed items did indeed fail the premises test, notwithstanding that (as is common ground on these appeals) they all passed the business use test.

21. Having recognised, at page 84C, that the premises test may be finessed if the premises are themselves plant (as was the dry dock in *Commissioners of Inland Revenue v Barclay, Curle & Co. Ltd* (1969) 45 TC 221, Hoffmann J explained the premises test, in relation to additions or improvements to buildings, as follows, at page 85B to F. The references to Lords Lowry and Templeton are to their speeches in *Scottish & Newcastle Breweries* (supra) and *St John's School v Ward* 49 TC 524:

> "How does one apply the premises test to items which were not incorporated as part of the original building but have been added by way of subsequent improvement? Lord Lowry, as we have seen, said that the question was whether something had "become part of the premises", and Templeman J spoke of "integral parts of the building". The question is not, I think, the same as whether it has become part of the realty for the purposes of the law of real property or a fixture for the purpose of the law of landlord and tenant. In *Yarmouth v France* Lindley LJ contemplated that fixed chattels might be plant. In the *Scottish & Newcastle Breweries* case the House of Lords approved a decision of the Commissioners that a fixed but not easily removable metal sculpture was not "part of the permanent structure of the hotel" and therefore qualified as plant.
>
> Adopting the words of Lord Lowry, the question seems to me to be whether it would be more appropriate to describe the item as having become part of the premises than as having retained a separate identity. This is a question of fact and degree, to which some of the relevant considerations will be: whether the item appears visually to retain a separate identity, the degree of permanence with which it has been attached, the incompleteness of the structure without it and the extent to which it was intended to be permanent or whether it was likely to be replaced within a relatively short period. Mr Aaronson submitted in reply that if, contrary to his submission, this was the proper test, those considerations constituted a series of separate hurdles which had to be overcome before an item could be regarded as a part of the premises. It had to have been attached with the intention of being a permanent fixture, it must have been actually and irremovably fixed and it must not be a mere ornament or embellishment. I do not agree. In my judgment these matters are factors to be taken into account in answering the question posed by Lord Lowry."

22. In the Court of Appeal Fox LJ, with whom Lloyd and Glidewell LJJ agreed, broadly endorsed Hoffmann J's analysis: see pages 96B-E and 97B-F. He concluded, in agreement with Hoffmann J, that:

> "The question is whether it would be more appropriate to describe the item as part of the premises rather than as having retained a separate identity."

In relation to the question whether the tests were functional he said, at page 97B:

> "It is proper to consider the function of the item in dispute. But the question is what does it function as? If it functions as part of the premises it is not plant."

23. Before leaving the *Wimpy* case, we remind ourselves of the following guidance from Lloyd LJ as to the function of an appellate court such as the Upper Tribunal, at page 105. Having noted Lord Wilberforce's observation in *Scottish & Newcastle* (supra) at page 271 that there is no universal formula or single test which can solve every problem in relation to the identification of plant, he continued:

> "So what is to be done? The answer is, I think, that in these cases the courts should be especially reluctant to upset the decisions of Commissioners, unless it can be shown not only that they have erred in law but also that their error is palpable. It is not enough to show that they may have applied the wrong test, as seems to be suggested by Mr Aaronson at one stage, or that they have not stated the test in the most precise language, or that they have omitted to refer to some factor which they ought to have taken into account. Where the Judges have themselves failed to find a universal test, the Commissioners are not to have their language examined too closely, or dissected line by line. So the cases will, I hope, be rare when it is held that the Commissioners have, on the face of it, applied the wrong test. Still rarer should be those cases where it is held that they must have applied the wrong test, because of their findings on the facts."

24. The Tribunal dealt with this issue, in the First Decision, solely by reference to the decorative panelling installed at the Prince of Wales pub: see paragraphs 56-67. In summary, they began with a succinct description of the panelling, which is not in any way challenged on appeal. It consisted of plywood veneered to look like oak with ogee planted panel mouldings, skirtings and decorative friezes. It extended to 2050mm from the ground leaving an area of un-panelled wall between it and the ceiling. It covered most but not all of the walls. It was attached to the walls and columns with softwood battens so as to lie proud of the plasterwork on the walls. It was specifically designed for the Prince of Wales pub so as to fit the parts to be covered, and was clearly a feature (by which we infer they meant an attractive feature) of the premises.

25. In paragraphs 58-62 the Tribunal summarised the effect of the *Scottish & Newcastle* and *Wimpy* cases, quoting in full Hoffmann J's list of what he called "some of the relevant considerations", noting that, in relation to the decorative panelling, some of those considerations pointed one way and some the other. After a reasonably detailed application of Hoffman J's list of relevant considerations to the decorative panelling in issue, during which they noted that it was capable of being removed without more than surface damage to the plasterwork, albeit unlikely to be removed in the short term, and that, visually, it appeared to retain a separate identity, the Tribunal noted that, nonetheless, Hoffmann J's list was not intended to be exhaustive.

26. At paragraph 63 they identified the critical question as:

> "whether the decorative panelling is more appropriately described as part of the premises in which the pub's trade is carried on or instead as an embellishment used to enhance the atmosphere of those premises."

They continued with the following two paragraphs, at which the main thrust of Mr Ghosh's submissions has been aimed:

" 64. A factor not mentioned by Hoffmann J in *Wimpy International*, but which seems to us to be helpful to consider in the context of the decorative panelling is the extent to which the panelling can be regarded as an unexceptional component which would not be an unusual feature of premises of the type to which the Appellant is inviting the public. If an item is or becomes such an unexceptional component of the premises into which it is introduced, that, in our view, is a factor tending to the conclusion that it does not retain a separate identity for relevant purposes. The relevance of this factor is, we consider, supported by the treatment in para. 1(2) of Schedule AA1 of any asset in a building which is not incorporated into the building but is of a kind normally incorporated into buildings, as effectively, part of the building, and also the exclusion from this treatment, by item 14 of Column 2 of Table 1 in Schedule AA1, of "decorative assets provided for the enjoyment of the public in the hotel, restaurant or similar trades".

65. Because the decorative panelling in the Prince of Wales effectively turns the premises, or that part of them to which it is applied, from an unpanelled room into a room which is mainly panelled, we consider that it is an unexceptional component of the type of premises, in contradistinction, for example, to the fixed but not easily removable metal sculpture, which was held, in *Scottish & Newcastle Breweries*, to be plant."

The Tribunal's conclusion was that, balancing all those matters, the panelling was more appropriately to be described as having become part of the premises than as having retained a separate identity. Accordingly they concluded that it did not qualify as plant.

27. Mr Ghosh was constrained to accept that most of the Tribunal's summary of the relevant principles, extracted from the *Scottish & Newcastle* and *Wimpy* cases was orthodox and unexceptional. He accepted that the Tribunal were required to conduct a multi-factorial balancing of competing considerations to which this appellate court should afford real respect. Nonetheless, he submitted that the Tribunal's reliance in paragraphs 64 to 65 on what may be labelled "the unexceptional component" consideration represented the erection of a new and wholly illegitimate legal test, and that the Tribunal's reference to paragraph 1(2) of Schedule AA1 was wholly illegitimate in a case in which neither party submitted that the Schedule had any direct application.

28. We have not been persuaded by this submission. Taking the "unexceptional component" point first, we consider that the Tribunal was by no means seeking to lay down some principle of general application, but rather explaining their reasoning in relation to the borderline item constituted by this particular panelling. It was in their view ordinary panelling which simply turned what would otherwise have been an un-panelled room into a mainly panelled room. In short, its effect was upon the premises, by contrast with the distinctive items in *Scottish v Newcastle Breweries*, such as the sculpture (and, we would add, the tapestries, stags heads, bagpipes and murals) which were distinctive embellishments in their own right. It is in that context noteworthy that in the *Wimpy* case the Special Commissioners allowed as plant some wall panelling and that this was not appealed. But this was by no means unexceptional panelling, since it included finishings in bronze or silver mirrors or infills of melamine, hessian or a textured sandstone effect: see 61TC 51, at 67 F-G.

29. Secondly, there was nothing wrong with the Tribunal's use of the analogy with Schedule AA1. Our understanding is that the Tribunal correctly recognised that item 14 in column 2 was, as we have explained, included as a form of shorthand for decorative embellishments of the type allowed in *Scottish v Newcastle Breweries*, by contrast with items which either were or, in the ordinary course would usually be, incorporated into buildings.

30. It is clear from the First Decision that the Tribunal never lost sight of the fact that the legal principle to be applied was to ascertain whether, in all the circumstances, the panelling had retained its separate identity, or lost it by becoming part of the premises. This is, in our view, plainly not a case in which a tribunal, having apparently stated the law correctly, then lost sight of it in considering the facts.

31. Above all, we consider that Mr Ghosh's submission falls foul of the prohibition enunciated by Lloyd LJ in the *Wimpy* case, because it does indeed constitute an attempt by excessive dissection of the language of the decision of the fact finding body to identify some error of law in a context where the question raises matters of fact and degree which are susceptible to no universally acceptable criteria.

32. Mr Ghosh submitted in addition that the legal question whether the panelling had become part of the premises was in essence a physical question, depending on the way in which it had been secured to the walls and columns. Again, we consider that, while the manner in which an item has been fastened to premises is plainly relevant, questions of physical fastening are plainly not conclusive. The manner in which panelling is fastened to walls is an essentially technical question, which may for all we know be dependent on building or fire regulations. In that context we note that in the *Wimpy* case the manner of attachment of the panelling to the walls differed between the various premises under review precisely because of the effect of fire regulations.

33. Finally Mr Ghosh submitted that the question whether any particular item had become part of the premises had to be answered functionally, that is, by asking whether the function of the item was to provide shelter or housing, or alternatively, to provide an attraction to customers for the purposes of the trade. On that analysis, he submitted that the panelling plainly fell into the latter category.

34. Again, we reject this submission. While all the tests for the identification of plant are, in a sense, functional, the functional aspect of the premises test is, as Hoffmann J made clear, to be addressed to the premises as a whole, rather than to the item in dispute. As Lord Hoffmann put it, at 61 TC 51, 86B:

> "Once it has been decided that the building or structure is premises and not plant, the functional test is in my judgment exhausted. Additions or improvements to premises are excluded by the premises test not by virtue of the separate functions of items which *ex hypothesi* have lost their separate identity but simply because they have become part of the premises."

35. For those reasons, the appeal in relation to the panelling at the Prince of Wales pub fails. We can deal much more briefly with the appeals in relation to the cornice work, architraves and balustrade ends. The essence of Mr Ghosh's submission on these items was that on the unchallenged evidence they were all removable, and therefore not part of the premises at the Prince of Wales pub. Having been shown photographs of each of the items in issue, we consider it fanciful to suppose that any of them could be regarded as having retained their separate identities; separate that is from the ceilings, walls and balustrades of which they each form part. Since those ceilings, walls and balustrades are all clearly part of the premises, so are the cornices, architraves and balustrade end-fittings. We cannot, in short, imagine how any legal analysis of the nature of plant, as opposed to premises, could lead to a conclusion that those items were plant. In fairness, Mr Ghosh did not suggest that, if JWD lost its appeal in relation to the panelling, it could nonetheless succeed in relation to any of those additional items.

B Incidental Expenditure – section 66

36. In contrast to the first issue, there is a considerable gulf between the respective contentions of the Appellant and the Respondents in relation to the meaning of section 66. We will therefore first give our views on the interpretation of the section and, by reference to examples of disputed items, the pointers that should be considered in applying it.

37. The parties have listed a large number of items of expenditure, in relation to which one or other is appealing. If we merely gave a decision on what we consider to be the right legal approach, the parties would almost

inevitably find that there was continuing disagreement between them as to how our decision should be applied in relation to certain items of expenditure. We will therefore make clear how we consider that section 66 operates in relation to the main items of disputed expenditure.

38. In order to save confusion, we will always refer (even if this involves adjusting quotations from earlier cases without indicating that) to the section that provided for relief for basic expenditure "on the provision of plant and machinery" as the provision in force for the purposes of this appeal under the Capital Allowances Act 1990, i.e. section 24, and to the section that conferred allowances in relation to certain expenditure on altering existing buildings, incidental to the installation of plant or machinery, as section 66.

The wording of section 66

39. Section 66 provides as follows:-

"66. Building alterations connected with installation of machinery or plant

Where a person carrying on a trade incurs capital expenditure on alterations to an existing building incidental to the installation of machinery or plant for the purposes of the trade, the provisions of this Part shall have effect as if that expenditure were expenditure on the provision of that machinery or plant and as if the works representing that expenditure formed part of that machinery or plant."

The parties' respective contentions

40. It was broadly common ground between the parties that all expenditure on the actual installation of plant or machinery qualified for allowances, as being expenditure "on the provision of plant or machinery" under section 24. The parties also agreed that section 24 extended to expenditure to ensure that plant could actually be operated. So for instance in the case of a cooker, the installation expenditure, qualifying for allowances under section 24, would result in someone being able to switch the cooker on, and to get to it, so as to open its doors. Accordingly section 66 was not the section that gave relief for the basic installation expenditure. Beyond being common ground, this is implicit in the wording of section 66 which effectively assumes the installation, and then addresses expenditure "incidental to the installation". The dispute in relation to section 66 thus related to what further expenditure might qualify for relief when plant or machinery was installed in an existing building such that building alterations were made. On this subject the Appellant advanced a broad construction of the section, whilst the Respondents contended for a much narrower construction.

41. The Appellant contended that "expenditure on alterations to existing buildings, incidental to the installation of plant" included any expenditure

incidental to the installation directed to making the plant more usable. Having regard to the point just mentioned, to the effect that allowances would be available for expenditure under section 24 to ensure that installed plant was working, a much wider meaning was to be given, for section 66 purposes, to the notion of making installed plant usable. Accordingly, because:-

- the installation of a cooker required walls to be plastered and covered in wipe-clean tiles throughout the kitchen to meet Health and Safety requirements;
- the installation of toilet bowls, where there had hitherto been no toilet block, in practice necessitated the construction of partitions, block-work dividing-walls, doors, and the provision of floors with wipe-clean tiled surfaces to enable anyone to use the sanitary ware; and
- the provision of beer cooling machinery in the cool room necessitated a drain to enable the floor to be cleaned and spilt beer to be removed, and a slightly inclined floor to direct water to the drain,

it was contended that all the expenditure on building alterations relevant to those items was expenditure "incidental to the installation" of the relevant items of plant.

42. It was implicit in these contentions that allowances would be available for expenditure in relation to existing buildings under section 66 for many items that might equally be needed in constructing kitchens, toilets and cold rooms in new buildings, regardless of the fact that none, or hardly any, of them would qualify for allowances when the same plant was installed in a new, purpose-built, building.

43. In stark contrast, the Respondents contended that the items for which allowances could be claimed under section 66 were for alteration works incidental to the pure physical installation of the plant in an existing building, and not to alterations geared to facilitating the better use of the installed items. Thus the Respondents gave as an example of an allowable item the moving of a staircase in an existing building where the installation of plant might prevent people accessing other floors that they had previously been able to access. Similarly, if a large item of plant was installed in an existing building, and it blocked the windows so that old windows had to be bricked up and new window apertures created, that type of alteration to the building, consequent upon the installation of the plant, was all that the section provided for. It followed from the Respondents' contentions that the section was providing for allowances for expenditure particularly occasioned by the installation of plant in an existing, rather than a new, building that of its very nature the expenditure would not have to be incurred, at least in a similar way, in the case of installations in a new building.

Certain matters of common ground between the parties

44. Prior to summarising the respective contentions of the parties in more detail, it is worth making two preliminary points, on which the parties were in agreement.

45. The first is that, although section 66 has existed in virtually identical form for approximately 67 years, and its purpose and ambit are not entirely clear, there has been no reported case on section 66. There were very important remarks in relation to one of the predecessors to section 66 made by Lords Reid and Donovan in *Commissioners of Inland Revenue v. Barclay, Curle & Co. Ltd* (1969) 45 TC 221, to which we will return, but that was a case about what is now section 24. The absence of authority does perhaps suggest that section 66 has been of relatively little practical significance over the years. This may indicate that section 66 has not hitherto been taken to provide authority for claiming plant and machinery allowances in existing buildings on a much more generous basis than for new buildings.

46. Secondly, it was agreed between the parties that if some expenditure did qualify for allowances because of section 66, there was no question of the allowance then being denied by the provisions of Schedule AA1 of the Capital Allowances Act 1990. This is because expenditure qualifying under section 66 is deemed to be expenditure on the provision of the plant itself and accordingly it is fictitiously treated as not being expenditure on altering a building. If, for example, the expenditure under section 66 involved alterations to a wall so as to accommodate a cooker, it would be deemed to be expenditure on the provision of the cooker, not the wall. Thus the provisions of the Schedule about walls that might ordinarily circumscribe allowances under section 24 have no effect upon alterations which qualify under section 66.

The Appellant's contentions in more detail

47. The Appellant's case was anchored upon dicta of Lord Reid in the House of Lords in the *Barclay, Curle* case. That case involved the construction of a dry dock, where the House of Lords concluded, by majority, that the whole dock, including all its concrete walls (rather than just the gates and the obviously mechanical parts of the structure) were plant, and that the cost of excavating the land in which to erect the dock was all expenditure on the provision of plant, qualifying for allowances under section 24. There were obviously no alterations to any existing building to which the predecessor to section 66 had any application.

48. The Revenue had argued that, if "provision" was wide enough to include the excavation expenditure, as being necessitated by the installation of the dock, then section 66 could never have any application at all. Lord Reid dealt with this submission in the following passage (at pages 239-240):

> "So the question is whether, if the dock is plant, the cost of making room for it is expenditure on the provision of the plant for the purposes of the trade of the dock owner. In my view this can include more than the cost of the plant itself, because plant cannot be said to have been provided for the purposes of the trade until it

is installed; until then it is of no use for the purposes of the trade. This plant, the dock, could not even be made until the necessary excavating had been done. All the Commissioners say in refusing this part of the claim is that this expenditure was too remote from the provision of the dry dock. There, I think, they misdirected themselves. If the cost of the provision of plant can include more than the cost of the plant itself, I do not see how expenditure which must be incurred before the plant can be provided can be too remote.

The Crown relies on Section 66 as showing that "provision" cannot have the meaning which I have ascribed to it. That section is as follows:

"Where a person carrying on a trade incurs capital expenditure on alterations to an existing building incidental to the installation of machinery or plant for the purposes of the trade, the provisions of this Chapter shall have effect as if the said expenditure were expenditure on the provision of that machinery or plant and as if the works representing that expenditure formed part of that machinery or plant."

Here the word used is "incidental" to the installation of the plant. "Incidental" is a wider word than "necessary". In my view, expenditure necessary for the installation of the plant is already covered by s.24. But it may be that the exigencies of the trade require that, when new machinery or plant is installed in existing buildings, more shall be done than mere installation in order that the new machinery or plant may serve its proper purpose. Where that is the case this section enables the cost of the additional alterations to be included. If this section meant that no preliminary expenditure is within the scope of s.24, there would be an anomalous and unreasonable difference between the provision of plant in a new building or in the open and the provision of plant in an existing building. So I do not regard this section as supporting the Crown's argument."

49. Lord Upjohn dissented and would have held that the cost of the concrete was not expenditure on plant, so that the question whether the excavation expenditure qualified for relief under section 24 did not arise at all. He did however say that, had he concluded that the whole dock (including the concrete) was all plant, then he agreed with Lord Reid's analysis of the excavation issue.

50. The only other member of the House of Lords to make any reference, direct or indirect, to the proper meaning of s. 66 was Lord Donovan, one of the majority who granted allowances for the concrete and the installation expenditure. He considered that the installation expenditure qualified under section 24 in the following passage in which he went on to consider the wording of s. 66:

> "As regards the cost of the necessary excavation, I think this comes within the words "expenditure on the provision of machinery or plant" in s. 24, again regarding the dry dock as a whole. Similar expenditure incurred in relation to a building or structure is now regarded as "expenditure on the construction" of such a building or structure for the purposes of s. 265(1) without any further or more express provision, and I think rightly so. The Crown say that, if a comparable construction be given to the relevant words in s. 24, relating to plant and machinery, then s. 66 of the Act would be unnecessary. But that section relates to "alterations to an existing building *incidental* to the installation of machinery or plant", and its wording suggests that it was enacted simply as an assurance to remove doubts about a particular kind of case."

The Respondents' contentions

51. The Respondents first placed reliance on the language of section 66 and encouraged us to apply what they claimed to be its relatively clear words. The Respondents stressed the way in which the drafting of section 66 differed from that in section 24, in that the expenditure had to be "incidental to the <u>installation</u>", rather than to the "<u>provision</u>" of the plant. It would apply only to something required by that installation, and only where it occasioned the need for some building alteration. It went beyond section 24 because some building alterations might sensibly be said to be "incidental to the installation", whilst not designed actually to install the plant. The examples in paragraph 43 above were good examples of the type of expenditure that was not necessary actually to install the plant, but were still required as alterations to the existing building, in consequence of, or "incidental to", the installation of the plant.

52. Accepting that *Barclay Curle* decided that section 24 applied to necessary installation expenditure, so that section 66 covered something more, the Respondents submitted that it should be given a fairly narrow application. Lord Reid himself sought to avoid one asymmetry by rejecting the suggestion that installation expenditure was only allowable under section 66 and thus only for installations in existing buildings. We should accordingly seek to confine the application of section 66 to situations where installations in existing buildings might occasion the need for alterations in a way that would generally be irrelevant with installations in new buildings. For otherwise, we would occasion an equally odd asymmetry, for if allowances were granted on the broad construction claimed by the Appellant, they would be available for many items of expenditure on existing buildings that would be equally common in new-build situations, where plainly no allowances would be available.

53. In addition to the two examples of expenditure that they considered would be covered by their interpretation of section 66, the Respondents drew our attention to a particular element of expenditure in relation to the Prince of Wales where allowances had been claimed and readily conceded under section 66. The restaurant required a food-hoist for food to be sent up from the basement kitchen to the restaurant area, and the hoist and

accompanying machinery were obviously plant or machinery. Relief was then claimed, and given, under section 66, for shuttering that had to be constructed around the line of travel of the hoist. In a new building, the walls would have been built around the lift shaft, and expenditure on those walls would have been building expenditure, not qualifying for allowances, both on general principles, and as a result of the inclusion of such items in Column 1 of List 1 in Schedule AA1. Where the existing building had to be altered however, as an immediate and direct result of the installation of the plant and machinery, section 66 applied to that expenditure. That, the Respondents claimed, was the typical, relatively limited, situation to which section 66 was directed.

Our decision on the meaning of section 66

54. We are required to apply tax law purposively Section 66 does not in terms provide a new or separate category of allowable expenditure. Rather, it is a deeming provision which requires expenditure on certain alterations to existing buildings to be treated as expenditure on the provision of plant or machinery even if, apart from the section, it would not have been so treated. The touchstone for that deeming provision is that the expenditure on alterations be "incidental to the installation of the machinery or plant". Viewed purposively, the focus of the section is on the point that if plant is installed in an existing building rather than in a purpose-built new building, it is entirely possible that something will not fit, and that this will lead to alterations having to be made to the existing building. In the case of a purpose-built new building, there will generally be no equivalent need for such expenditure. Thus section 66 levels the playing field between new and existing buildings by affording taxpayers relief for expenditure on existing buildings which would not be needed in relation to the installation of the same plant in new buildings, or in the open.

55. The Appellant's case, that section 66 applies to any alterations designed to facilitate the better use of installed plant, would often have exactly the opposite result. In most of the situations where disputed allowances are claimed in this Appeal it would involve the grant of allowances for items of expenditure that could equally arise in new-build situations. This would create an asymmetry of the type Lord Reid appeared concerned to avoid in *Barclay Curle*.

56. There appears to be no ground for assuming some Parliamentary purpose that an additional subsidy should be given for renovations, and the re-use of existing buildings, to account for the asymmetry that the Appellant's contentions would generally involve. Section 66 and its predecessors have been in force for well over 60 years and no such purpose appears yet to have been discerned in any text book or academic commentary. We consider that a proper focus upon what we have described as the touchstone for the application of section 66 does achieve what we have identified as its purpose. The question is, in relation to each disputed alteration, whether the expenditure is truly incidental to the installation of

plant. The Special Commissioners appeared to take the same view. At paragraph 77 of the First Decision they concluded that:

> "…… section 66 was not intended to create a wholly new category of expenditure going beyond items truly incidental to the installation of plant….. there is a real distinction between alterations to a building incidental to the installation of plant and alterations consequential on the installation of plant."

57. Although Mr Ghosh criticised this summary on the ground that it confined allowances under section 66 to the ground already covered by section 24, we disagree with that criticism and consider that the Special Commissioners were making very much the point that we have sought to repeat. That the Special Commissioners were not confining the application of section 66 to pure installation expenditure covered by section 24 was made clear by some of the allowances that they conceded under section 66, where section 24 was plainly insufficient for the purpose.

The Starting Point

58. The question whether particular alterations are incidental to the installation of plant calls first for a general understanding of the relationship between the alterations, the plant, and the project intended to be advanced by each of them. Thus, while particular alterations may, viewed in isolation, contribute to the better use of particular plant, viewed in the round, they may also serve wider purposes which are not 'incidental' to the installation of that or any other plant.

59. Although we are dealing with the interpretation of section 66 on a general basis at present, we consider that the creation of apparently fairly luxurious and appealing toilet blocks for men and women in the conversion of the theatre into a pub and restaurant at the Prince of Wales in Cardiff provides an excellent example for the point that we have in mind. In an apparently void basement area, the renovation involved the creation of both a major kitchen and the toilet blocks. The creation of the toilet blocks involved the construction of walls around each of the mens' and womens' toilet areas, the construction of both block-work, and panelled divisions so as to create the individual toilet cubicles, the creation of panels behind the toilet cubicles, screening off the pipe-work and the cisterns, wipe-clean tiling on the block-work division walls, and non-slip wipe-clean floor tiling. The toilet blocks of course contained basins and sanitary ware.

60. We consider it realistic to say that the renovation involved the construction of toilet blocks from scratch; and naturally the toilet blocks contained some items of plant, being the sanitary ware, the wash basins and the toilet bowls and cisterns.

61. The Appellant's contention starts with the sanitary ware. We are almost asked to visualise toilet bowls in an empty void, whereupon we are then asked to conclude that nobody would use the toilets, unless cubicles were created. Having created the partitions, and then naturally attached cubicle doors, floor and wall tiling is then said to be incidental, as are the partitions to screen off the cisterns. The resultant position is that it is suggested that the entire building work on the toilet blocks is said to be expenditure on building alterations, incidental to the installation of the plant, namely the actual toilet bowls and cisterns.

62. We consider that description to be extremely unrealistic. The realistic summary is that the overall renovation involved the construction of luxurious toilet blocks, into which various items of plant were installed. Whatever the precise order of construction and installation, we consider that the Appellant's contention that the building works are all incidental to the installation of the toilet bowls and cisterns involves the tail wagging the dog.

63. It happens that the Special Commissioners reached a different conclusion in relation to the expenditure on the toilets, and we will address that below. On the general point, however, as to whether the very first point of interpretation was indeed to address whether, in a realistic sense, the expenditure on various items in a newly-created room could be said to be expenditure incidental to the installation of plant, we note that the Special Commissioners themselves adopted very much the approach that we have just indicated, when themselves considering the kitchen walls and the wipe-clean tiling. The argument there had been whether the kitchen was built and tiled as one operation (tiling quite possibly being adopted for several reasons), whereupon various items of plant and machinery were installed, or whether the installation of the cooker made the wipe-clean tiling expenditure, and the expenditure on the plastering and even the walls, incidental to the installation of the cooker. The basis for this contention was that it was said, in Mr. Large's undisputed evidence, that the fumes and spills from the cooker rendered wipe-clean tiling obligatory, and the dividing walls had to be built to keep the kitchen atmosphere and the pub atmosphere (smoking not having been banned at the time) separate. The Special Commissioners concluded that:

> "…. It would be stretching section 66 beyond its evident purpose to allow expenditure on the construction of kitchen walls to qualify, on the basis that the exigencies of the Appellant's trade, including statutory or regulatory requirements, require that kitchen walls themselves must be constructed so that the cooker may serve its proper purpose. The construction of the kitchen walls was not incidental to the installation of the cookers (or other kitchen equipment). It was part of the creation of a kitchen, in which the cookers and other kitchen equipment could function properly."

We agree both with that conclusion and its reasoning. It exemplifies the need to start with a broad assessment of what is incidental to what.

The situations where section 66 does apply

64. Having now considered (in paragraphs 54 to 57) the purposive approach and concluded that the scope of section 66 is intended to be fairly limited, and having noted (in paragraphs 58 to 63) that section 66 does not apply when expenditure cannot realistically be said to be incidental to the installation of plant in any sense, we now turn to consider the intended application of the section, and the situations where we consider that it does properly confer allowances. Where other appeals raise quite different facts, we expect that different approaches might be appropriate, since our present approach is very much based on the examples of expenditure currently in dispute.

65. We accept the point made by the Respondents, to the effect that if the installation of plant in an existing building means that certain alterations have to be made to the building, albeit that they may not affect the operation or use of the plant, then allowances can be claimed for those alterations. Thus, we agree with the example advanced by the Respondents that if the installation of plant necessitates some alteration to a pre-existing staircase because the installation of the plant would otherwise prevent use of the staircase to get to other floors, then expenditure on that alteration would qualify for allowances under the section.

66. Whilst as a general rule we accept that it is section 24, rather than section 66 that covers the expenditure on installing plant or machinery, we do not rule out the application of section 66 to some items of expenditure that might well be directly related to the installation of plant. For instance if the existing staircase, referred to in the previous paragraph, had to be modified to facilitate access to the plant, it would be odd if that expenditure failed to qualify under section 66, when that conceded by the Respondents in their example mentioned in paragraphs 43 and 65 did qualify for allowances. The expenditure on moving the staircase to facilitate access to the installed plant might equally qualify for allowances under section 24, though allowances under that section might be denied by the case law in relation to “premises” or by the provisions of Schedule AA1. But we consider that the expenditure would still qualify under section 66.

67. Another relevant disputed item of expenditure on building alterations is the claim in this case for the expenditure on strengthening the kitchen floor in order to support the weight of commercial cooking equipment (cookers, freezers etc) in the kitchen. It seems to us that that can qualify for allowances under section 66. It does not incidentally conflict with our general proposition that section 66 will usually confer allowances for alterations to existing buildings, where similar expenditure would not have to be incurred with a purpose-built new building. In that case, the appropriate floor would be designed into the building as an integral part of the overall building work, and this is why the need to make specific

alterations on an installation in an existing building deals with a somewhat different situation.

68. The Special Commissioners conceded allowances under section 66 for tile splash-backs adjacent to newly-installed basins, and there was some discussion as to whether it was then inconsistent to deny allowances for fully-tiled walls in the kitchen, or, more relevantly, for a fraction of such tiling attributable to the splash-back area to match the feature that purpose-designed splash-backs would have qualified for allowances. We found this distinction a relevant one that supports two distinct points.

69. We first consider that if a basin is installed in an existing building, and a small area of splash-back tiling is provided around the basin, then this is an example of the sort of thing that Lord Reid specifically contemplated. In other words the tiling is not necessary to enable the basin to be installed, or to function and to be used. The splash-back tiling can be said however to be an alteration to the existing building, incidental to the installation on the basis that it was designed to enable the basin to be used without damaging the adjacent brickwork, and for no other purpose. To deny allowances on this example would appear to us to be in direct conflict with Lord Reid's remarks.

70. In contrast however, if a whole room or a kitchen is being tiled for numerous purposes, then even the area around a sink or basin is being tiled because the whole kitchen or work-areas in the kitchen are being tiled. There is therefore a distinction between the specific splash-back tiling, created simply because of the installation of the sink, and the continuation of the entire tiling around the work areas of the kitchen for numerous reasons. In our view, neither such general tiling, nor any "fractional element" of it, would qualify under section 66.

71. In paragraphs 65 and 66 above we considered two situations where we expected alterations to an existing staircase, occasioned by the installation of plant, to qualify for allowances under section 66. A contrasting situation where we would not expect allowances to be available is again one that was provided by the Prince of Wales project. If a theatre is converted into a pub and restaurant so that a complete new floor has to be added, with staircases to connect it to the floors below and above, the construction of those staircases should generally be taken to be part of the main renovation operations. The fact that there might be items of plant on any of the various floors ought not then to lead to arguments on a remote basis of causation that people could not get to the items of plant without the staircase. With new floors, there simply must be staircases.

72. The decisions of the Special Commissioners and the First-tier Tribunal placed considerable reliance on there being a required "nexus" between the installation of plant and the alterations to the building. We agree with this. It was in our view the Tribunal's way of summarising the requirement that the claimed expenditure was on alterations "incidental to the installation of the…plant". It did not involve the introduction of any extra or illegitimate test.

The Appellant's reliance on Mr. Large's evidence

73. We must briefly address the Appellant's heavy reliance on the evidence of Mr. Large. Mr. Large had given evidence in relation to virtually every item of disputed expenditure, and he had generally pointed to the practical reason, or the Health and Safety or other regulatory requirements, as to why some installed item of plant occasioned the need for some building alteration to be made. From this it was contended that because none of Mr. Large's evidence had been questioned or undermined in any way in cross-examination, we were bound to allow the Appellant's appeal on various items because of that undisputed evidence.

74. An example of this approach was the suggestion that a cooker in a kitchen could not be used until there were wipe-clean and non-slip tiled surfaces in the kitchen. Such surfaces were claimed to be required on account of spills and fumes from the cooker.

75. The fact that Mr. Large's evidence was not questioned in cross-examination does not mean that the Special Commissioners and the First-tier Tribunal necessarily accepted all his evidence. While we accept that they did not specifically reject any of the evidence, three factors are noteworthy. Firstly, the Special Commissioners had undertaken site visits to both pubs whose renovations were treated as typical, and they also made clear that they had seen many photographs to inform their decisions. It was implicit that this evidence had also been instrumental in the conclusions that they reached, and we believe that they meant (rather politely) that they regarded this evidence as being more instructive in some cases than the various claims and assertions made by Mr. Large. Secondly, as regards the limited significance of wipe-clean tiling in the kitchen, the Special Commissioners were provided with quotations from Health and Safety directives that did seem to make wipe-clean tiling desirable or obligatory in commercial kitchens, but those quotations did not make the surprising leap of suggesting that this requirement was founded solely or even predominantly on spills or fumes from cookers. Thirdly, common sense suggests that the most obvious reason for wipe-clean tiling in commercial kitchens would be to satisfy hygiene requirements in work areas used for the preparation of raw food. The suggestion that tiling was required solely or even principally because of spills and fumes from cookers seems, even if not specifically questioned, extraordinarily improbable. The suggestion that allowances be claimed for kitchen tiling, the plastering under the tiling, and for kitchen doors all because of spills, fumes and smell from cookers seems to us to have been a massive leap based on a fragment of evidence.

76. We reiterate the point that our actual decision in relation to the Appellant's appeal in relation to the kitchen tiling and other similar items is based not on now questioning this evidence, which is not our function, but on the fundamental point addressed in paragraphs 58 to 63 above.

Incidental costs being disproportionate

77. At one point in the First Decision, the Special Commissioners indicated that they would generally expect building alteration expenditure incidental to the installation of plant to be less than the expenditure on the plant and its basic installation, or at least not to be disproportionately more. Oddly, in relation to the cold room floor, where allowances under section 66 were conceded for the cost of providing a drain and an inclined floor, by way of alterations to a pre-existing floor, the Special Commissioners then observed that the fact that the cost of those building alterations was indeed disproportionately more than the cost of the trade-specific drainage equipment, that we took to be installed to expel water from the drainage duct, did not preclude the claim for allowances.

78. We see no reason why qualifying expenditure on incidental alterations to an existing building should have to be less, or not disproportionately more than, the expenditure on the provision of the plant items to which the alterations are incidental. We imagine that such expenditure would usually be less, but can see no reason why it should not, in an appropriate case, be significantly more. As we have just indicated, the Special Commissioners appeared to sanction this approach in relation to the cold-store floor, and we consider that that approach was correct.

Consistency with Lord Reid's approach

79. We do not consider that our interpretation of section 66 is irreconcilable with the remarks of Lord Reid, quoted above. It is important to remember that when *Barclay Curle* came before the House of Lords, the issues before the House were whether the entire dry dock was one integral element of plant, and whether installation expenditure was allowable under section 24. Lord Reid's remarks in relation to section 66 were thus directed only to dismissing the then argument that section 24 did not provide allowances for installation work because, at least in the isolated context of an installation in an existing building, it was section 66 that conferred allowances for installation expenditure. All that Lord Reid actually said about the scope of section 66, beyond rejecting the argument that it had any relevance in narrowing the effect of section 24, was that "it may be that the exigencies of the trade require that, when new machinery or plant is installed in existing buildings, more shall be done than mere installation in order that the new machinery or plant may serve its proper purpose." This wording is far from suggestive that there had been much discussion about what section 66 might actually cover, and the very speculative nature of the observation just quoted does not suggest that some particular application was clear and obvious to Lord Reid. Lord Donovan was even less prescriptive about the scope of the section.

80. Having regard to the fact that we have just outlined (in paragraphs 66 and 69 above) two circumstances where section 66 might indeed provide allowances for building alterations so that plant might better serve its proper purpose, and having regard to the examples provided by the Respondents where they readily concede allowances even when alterations

have nothing whatever to do with the functioning of the plant, we consider that our conclusions are not prohibited by Lord Reid's remarks. We accept his conclusion that section 24 is the basic provision for installation expenditure and that section 66 should not be interpreted so as to create unintelligible asymmetries between existing and new buildings. We believe that, had Lord Reid thought it necessary to outline in full the circumstances where section 66 might confer allowances, he would not have found fault with our interpretation. We believe that he would have been surprised to learn that his remarks were being quoted to confer allowances on a raft of remote expenditure, where plant was installed in existing buildings, albeit that similar expenditure would be incurred in new-build situations, where it would manifestly fail to qualify for allowances.

We turn now to the decisions of the Special Commissioners and the First-tier Tribunal on the various items of disputed section 66 expenditure, and the cases where items are now the subject of the Appellant's appeal or the Respondents' cross-appeal

The kitchen tiling and doors

81. The Special Commissioners and the First-tier Tribunal rejected the section 66 claims for allowances for the kitchen tiling, the plastering behind the tiling, and the installation of doors to isolate the kitchen atmosphere and the pub atmosphere (smoking not having been banned when the pub was created) from each other. The Appellant's claim that the installation of the cooker led to all these requirements was in our view rightly rejected. We agree with their earlier conclusion that a kitchen was being created, in which there would of course be numerous items of plant. We assume that the kitchen as such contained no plant items adjacent to which there were purpose-designed splash-backs, but we consider that any such splash-backs would be the only items that would qualify as regards tiling on the walls or floors under section 66.

Strengthening the kitchen floor

82. The Special Commissioners allowed the section 66 claim for allowances for strengthening the kitchen floor, and this is one of the three areas where the Respondents have cross-appealed. Not only do we see no ground to disturb the findings of the Special Commissioners, but we consider the example of the strengthening of the kitchen floor to be one of the very best examples of a building alteration that is incidental to the installation of plant, and that was properly allowable under section 66. We admit to being slightly confused about the pre-existing nature of the kitchen floor, albeit that it was obvious that the floor was the floor of the basement, since that is where the kitchen was created. There are references to the kitchen floor having involved work in removing existing concrete, and to there having been a timber-suspended floor in the pre-existing basement. Whatever the exact detail, Mr. Large's evidence was that it was the weight of plant and machinery in the kitchen that required the strengthening of the

kitchen floor, or possibly the creation of a new strong floor in place of the concrete and timber construction previously situated in the area that became the kitchen. Suggestions by the Respondents that the weight of people moving in the kitchen and other general user items was what necessitated the strengthening of the floor seem to us to be unfounded. We find it entirely credible that the weight of commercial cookers and freezers, and indeed other equipment such as large commercial dishwashers, would have necessitated strengthening the kitchen floor. We see no reason therefore to disturb the earlier decision that this expenditure was properly allowable under section 66.

The kitchen lighting

83. We ignore all points in relation to kitchen lighting. The Decisions left open the question of whether the kitchen lighting was "trade-specific" (so potentially to qualify for allowances), albeit that they confirmed the Appellant's claim that such lighting could at least theoretically be trade-specific. It was then implicit that if the parties eventually agreed that some or all of the kitchen lighting was trade-specific, then the cost of cutting holes into the ceiling would be allowable under section 66. On account of the points that we made in paragraphs 58 to 63, we are not sure that we would necessarily have reached the same conclusion, but we ignore this because the Respondents have not appealed against the conclusion recorded in the previous sentence.

The toilet cubicle partitions, block-work dividers, the panels behind the sanitary ware shielding the pipe-work and cisterns, and the floor and wall tiling

84. The decision of the First-tier Tribunal clarified that, in addition to allowing the claim for allowances under section 66 in relation to the panelled dividers between cubicles, they did not mean to draw a distinction between those dividers and others that were apparently block-work. Accordingly, even the expenditure on the block-work dividers and the partitions shielding the pipe-work and cisterns was all allowable, though expenditure on the tiling on the floor and walls was not allowable.

85. The Appellant now appeals in relation to the tiling, and the Respondents cross-appeal in relation to the block-work, albeit that the Respondents then oddly draw a distinction between the block-work partitions and the other partitions (that we assume probably to be laminate covered MDF, or some similar material), and do not cross-appeal in relation to the decision granting allowances under section 66 for those non-block-work partitions. The Respondents did confirm, however, when asked by us, that they considered that allowances had wrongly been conceded in relation to the expenditure on the non block-work partitions, though they were not now seeking to overturn that decision.

86. Our decision is that the Appellant's claim for additional allowances in relation to tiling etc is dismissed, the Respondents' cross-appeal in relation to the block-work expenditure is allowed, and because no cross-appeal was made in relation to the non-block-work partitions, the decision of the First-tier Tribunal stands as regards those partitions. In principle, however, we consider that for the reasons given in paragraphs 58 to 63, no allowances should have been granted for any expenditure in relation to the construction of luxurious toilet blocks for men and women in the previous void area of the basement. Allowances should have been given under section 24 for the plant items, and their installation, but not for the creation of the toilet areas.

87. We are indeed curious as to why the Special Commissioners initially granted allowances for the cubicle partitions, when entire toilet areas were created, when they took the opposite, and in our view, the correct, approach when dealing with all the expenditure on claimed building alterations in creating the kitchen. A new kitchen and toilet blocks were created, and it seems to us that the reasoning in paragraphs 58 to 63 applies to both.

The cold-store floor and drainage system

88. Our understanding of the drainage requirements in the cold store is that condensation and spillages from the beer-cooling equipment made trade-specific drainage equipment essential to expel water and spilt beer from the cold store. In order to feed the relevant trade-specific equipment, which we take to have been installed plant or machinery, a lowered drain duct had to be created in the floor, and in order that the floor should slope towards the drain, the existing floor had to be removed and replaced by a slightly inclined floor. It seems to us that, on the basis that our understanding is that the drainage duct actually feeds water and spilt beer into trade-specific fluid extraction equipment (which seems realistic with drainage in a basement that we assume to be below ground level), all these costs were properly allowable under section 66.

The hoist shuttering

89. The Respondents conceded that the shuttering constructed around the food-hoist was eligible for allowances under section 66, but the First-tier Tribunal dismissed the claim for tiling on that shuttering in the basement (presumably where the lift was adjacent to the kitchen). The Appellant appeals in relation to that tiling.

90. We reject that appeal. The tiling was simply a finishing coat round the shuttering, no more eligible for allowances than the painting (or plastering and painting if both were required) where the lift passed through the higher floors.

Summary

91. It follows, in summary, that we have dismissed all the section 66 appeals by the Appellant; we have dismissed the section 66 cross-appeals by the Respondents in relation to the strengthening of the kitchen floor, and the drainage work required in the cold store, and we have allowed the Respondents' cross-appeal in relation to all the expenditure claimed under section 66 in the toilet areas, except the expenditure on the non-block-work cubicle partitions. We would have allowed an appeal by the Respondents had they appealed against the Special Commissioners' grant of allowances for those partitions, but the Respondents did not so appeal

C Apportionment of Preliminaries

92. Preliminaries are, by their nature, items of overhead expenditure which cannot be, or which hav not been, attributed to any single item in the building project. Some, like insurance, are inherently incapable of being so attributed. Others, like scaffolding, may be capable of specific attribution, but the time and cost involved in the process of specific attribution is often disproportionate to the amount at stake. Thus, apportionment of preliminaries between items which do, or do not, qualify for capital allowances is the only solution in relation to un-attributable preliminaries, and may be the sensible solution where attribution is uneconomic.

93. In the present case the parties were in dispute about a class of preliminaries which were 'trade specific', that is, attributed to particular types of building activity, such as scaffolding, electrical and photography of work in progress, but which had not at the time been attributed to specific items of work. They are set out at paragraph 34 of the First Decision, and hence acquired the label 'Para 34 items' during the appeal. JDW claimed to be entitled to apportion them for capital allowances between allowable and non-allowable works in the ratio derived from the respective aggregate specific costs of those two classes as a whole. We shall call that a pro rata apportionment.

94. HMRC maintained that a trader seeking capital allowances must specifically attribute all expenditure which is capable of attribution, however time-consuming or uneconomic that process may be. Accordingly HMRC maintained both before the Tribunal and on this appeal that no part of the Para 34 expenditure was allowable because it had only received a trade specific rather than item specific attribution, and because those items were not inherently incapable of specific attribution.

96. In order to meet a possible argument that pro rata apportionment might produce an excessive recovery for JDW, its expert Mr Phillippo spent 20 to 25 days work on an item by item attribution of the preliminaries at the Prince of Wales, leading to his unchallenged conclusion that (on HMRC's case as to the allowable items of work) pro rata apportionment of

preliminaries was worse for JDW than specific attribution: see paragraphs 105 – 106 of the First Decision.

97. The Tribunal's conclusion was that a pro rata apportionment of the para 34 items, and of any preliminaries where a detailed item by item attribution would be disproportionately time consuming or expensive, was a legitimate basis for claiming capital allowances for preliminaries, because it was a reasonable, common-sense solution which accorded with generally accepted accounting practice: see paragraphs 109 – 111 of the First Decision and paragraphs 106 – 112 of the Second Decision.

98. To the extent that this sensible conclusion involved any issue of law at all, we unhesitatingly agree with it. It cannot have been the intention of the legislature that a trader should have to spend more on the minute attribution of preliminaries to underlying items of work than either their cost or the value of the capital allowance thereby to be obtained. The question whether this common-sense approach was mis-applied to the Para 34 items is plainly a matter of fact and degree with which it would be wrong for us to interfere, although our review suggests that the Tribunal's application to these items of their general approach to preliminaries was plainly correct. Accordingly HMRC's cross appeal on this point entirely fails.

MR JUSTICE MICHAEL BRIGGS **JUDE HOWARD NOWLAN**

RELEASE DATE: 31 JANUARY 2012