[2014] UKUT 0098 (TCC)

FTC/30/2013

Corporation tax – disposal of qualifying corporate bonds – disposal of debts - section 116(10) Taxation of Chargeable Gains Act 1992 – held-over capital gain brought into charge – joint election under section 171A TCGA – whether disposal by repayment of the debt underlying the bonds is a disposal 'to' a person outside the corporate group – whether the bonds exist after the repayment of the debt and are disposed of 'to' the debtor – reliance on extra-statutory material for construction of relevant provisions

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

BETWEEN:

DMWSHNZ LIMITED
(in members' voluntary liquidation)

Appellant

- and –

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

TRIBUNAL: the Hon Mrs Justice Rose

Sitting in public in London on 22 and 23 January 2014

Mr Graham Aaronson QC and Ms Zizhen Yang instructed by Ernst & Young LLP for the Appellant

Mr Michael Gibbon QC instructed by the General Counsel and Solicitor for HM Revenue & Customs for the Respondents

DECISION

The appeal of the Appellants IS DISMISSED

REASONS

1. This is an appeal against the decision of the First-tier Tribunal (Tax) dated 21 December 2012 (Judge Jonathan Cannan and Mrs Caroline de Albuquerque). It arises from HMRC's decision to reject a purported joint election made under section 171A of the Taxation of Chargeable Gains Act 1992 ('TCGA'). The effect of the election would have been to enable a sister company of the Appellant to set off a loss of about £92 million incurred by that sister company against a capital gain of about £88.7 million made by the Appellant. That would have reduced the group's corporation tax liability on the chargeable gains and losses to zero. If HMRC's rejection of the joint election is upheld, the Appellant will have to pay corporation tax on its capital gain of about £29 million.

The transaction

2. The facts are not in dispute and were clearly and comprehensively set out in the First-tier Tribunal's decision.
3. Until 22 October 2003 the Appellant was a member of the Bank of Scotland Group. On 9 September 1998 the Appellant sold its shares in its wholly- owned New Zealand subsidiary which was a company called Countrywide Banking Corporation Limited ('Countrywide'). The acquirer of the shares in Countrywide was NBNZ Holdings Limited ('NBNZ') and the consideration for the shares was NZ$850 million. The consideration was satisfied by NBNZ providing the Appellant with 10 year unsecured floating rate notes ('the Loan Notes'). In other words, instead of NBNZ paying the NZ$850 million to the Appellant in cash, that sum was thereafter treated as money lent by the Appellant to NBNZ with NBNZ promising to pay the loan off over 10 years in accordance with the terms of the Loan Notes. In loan note parlance, NBNZ was the issuer of the Loan Notes and the Appellant was the holder of them.
4. The Loan Notes were qualifying corporate bonds for the purposes of capital gains tax ("CGT") and I will have to consider the significance of this later. This meant that although a capital gain was crystallised on the disposal of the shares by the Appellant in 1998, that gain would only be charged to tax on a future triggering disposal of the Loan Notes. As at 2002 the held-over gain created by the 1998 sale of Countrywide shares was about £203.7 million.
5. In 2003 Bank of Scotland was owed £42,150,000 by an investment trust called Geared Income Investment Trust PLC ('Geared Income'). Lloyds TSB Bank PLC was owed a similar amount. Together the two banks appointed joint administrative receivers. The effect of this was that capital losses realised by Geared Income would be allowable for CGT purposes. Geared Income thereby realised capital losses on its investments of approximately £180 million.
6. A planned re-structuring was then put in place with a view to enabling the Group to set off Bank of Scotland's share of the losses in Geared Income against the held-

over gains attached to the Loan Notes in the hands of the Appellant. Pursuant to the re-structuring certain transactions took place. These resulted in the crystallisation of a capital loss of about £92 million by another company called GIIT Realisations 3 Limited ('GR3'). As part of the restructuring, the Appellant and GR3 were brought within the same corporate group. On 28 October 2003, the Appellant served notice on NBNZ under the terms of the Loan Notes that it wanted the repayment of NZ$370 million of the Loan Notes. NBNZ paid that amount to the Appellant on 28 November 2003, thereby bringing into charge to tax a held-over gain from the 1998 transaction of about £88.7 million.

7. On 1 December 2003 the Appellant and GR3 purported to make a joint election pursuant to section 171A TCGA to deem the disposal of the Loan Notes as having been made by GR3 rather than the Appellant. They thought that the effect of this would be to enable GR3 to set off the capital loss of £92 million against the capital gain of £88.7 million. The issue in this appeal is whether that was indeed the effect.

The legislation

8. Corporation tax on chargeable gains arises when profits are made on certain disposals of assets. The terms 'assets' and 'disposals' are given very wide definitions by the TCGA. It is common ground here that the debt owed by NBNZ to the Appellant as a result of the 1998 sale of the Countrywide shares is an asset for these purposes and also that the satisfaction of a debt constitutes a disposal of that asset. Every company within a corporate group is treated as a separate entity for capital gains purposes, but the TCGA includes provisions that prevent chargeable losses or gains arising when assets are moved around between companies in the same corporate group. Thus at the relevant time for our purposes, section 171 TCGA provided:

> "171 **Transfers within a group: general provisions**
>
> (1) Where—
>
> > (a) a company ("company A") disposes of an asset to another company ("company B") at a time when both companies are members of the same group, and
> >
> > (b) the conditions in subsection (1A) below are met,
>
> company A and company B are treated for the purposes of corporation tax on chargeable gains as if the asset were acquired by company B for a consideration of such amount as would secure that neither a gain nor a loss would accrue to company A on the disposal.
>
> …
>
> (2) Subsection (1) above shall not apply where the disposal is—
>
> > (a) a disposal of a debt due from Company B effected by satisfying the debt or part of it; or
> >
> > (b) a disposal of redeemable shares in a company on the occasion of their redemption; or

(c) a disposal by or to an investment trust; or

(cc) a disposal by or to a venture capital trust; or

(cd) a disposal by or to a qualifying friendly society; or

(d) a disposal to a dual resident investing company;

…

(4) For the purposes of subsection (1) above, so far as the consideration for the disposal consists of money or money's worth by way of compensation for any kind of damage or injury to assets, or for the destruction or dissipation of assets or for anything which depreciates or might depreciate an asset, the disposal shall be treated as being to the person who, whether as an insurer or otherwise, ultimately bears the burden of furnishing that consideration."

9. This meant that if Company A had an asset that it wanted to sell which would generate a capital gain and Company B in the same group had an asset that it wanted to sell which would generate a capital loss, Company A could transfer its asset to Company B without thereby generating a gain, Company B could then sell both assets and set the loss on one off against the gain on the other. Mr Aaronson QC appearing for the Appellant told me that in the past, much time and effort was devoted by corporate groups and their advisers to moving assets around the group in order to make sure that losses and gains could be matched up in this way. The First-tier Tribunal described section 171 as a 'very straightforward and uncontroversial piece of tax planning which helped to ensure full use of allowable losses within a group of companies'.

10. Section 171A TCGA was introduced into the TCGA by section 101 of the Finance Act 2000. In the accounting period ending 31 December 2003 with which we are concerned, section 171A provided as follows:

"171A **Notional transfers within a group**

(1) This section applies where—

(a) two companies ("A" and "B") are members of a group of companies; and

(b) A **disposes of an asset to a person** who is not a member of the group ("C").

(2) Subject to subsections (3) and (4) below, A and B may, by notice in writing to an officer of the Board, jointly elect that, for the purposes of corporation tax on chargeable gains—

(a) the asset, or any part of it, shall be deemed to have been transferred by A to B immediately before the disposal to C;

(b) section 171(1) shall be deemed to have applied to that transfer;

(c) the disposal of the asset or part to C shall be deemed to have been made by B; and

(d) any incidental costs to A of making the actual disposal to C shall be deemed to be incidental costs to B of making the deemed disposal to C.

(3) No election may be made under subsection (2) above unless section 171(1) would have applied to an actual transfer of the asset or part from A to B.

(4) An election under that subsection must be made before the second anniversary of the end of the accounting period of A in which the disposal to C was made."

11. I have highlighted those words in subsection (1)(b) because they are at the crux of this appeal. The first point which arises is whether when the Loan Notes were repaid by NBNZ (which is 'C' for this purpose) there was a disposal of an asset by A (which is the Appellant) **to** C. The second point is, if there was no disposal of the asset by the Appellant to NBNZ, does that preclude the application of section 171A to this transaction?

12. The Appellant relies on three grounds as establishing that the answers to those questions mean that the election that it and GR3 made pursuant to section 171A(2) was valid:

    a. On its true construction, the satisfaction of a debt is treated for the purposes of section 171A as a disposal of that debt to the debtor (that is NBNZ here) by the creditor (that is the Appellant here). If that is right, there is no difficulty with holding that the transaction was a disposal of the debt by the Appellant to NBNZ for the purposes of section 171A(1)(b) and the Group is entitled to elect to treat it as if in fact GR3 instead of the Appellant had disposed of the debt **to** NBNZ;

    b. If that is wrong, then what happened in this transaction was not – or at least not only – the satisfaction of the debt but also the transfer of the Loan Notes from the Appellant to NBNZ and that was a transfer of an asset (the Loan Notes) to a person (NBNZ) outside the corporate group;

    c. If that is wrong (that is, if the disposal of the debt is not a transfer of the debt to NBNZ and if the Loan Notes were not transferred by the Appellant to NBNZ) then the tribunal should adopt a purposive construction of section 171A on the basis that it was intended to absolve corporate groups from the task of actually moving assets around the group by allowing them to elect to treat assets as having been moved around and the literal construction of the section by HMRC frustrates that intention. The words should therefore be read as if they required only that there is a disposal of the assets outside the group whether or not the assets are disposed of 'to' a person.

13. I will consider each of those arguments in turn.

Is the satisfaction of a debt the disposal of the debt to the debtor by the creditor?

14. The term 'disposal' used in the TCGA is a term of art in that it covers events or transactions which would not be regarded as disposals in the ordinary use of that word, for example where an asset suddenly loses its value or is notionally transferred from the company's trading stock into its capital stock. The disposal of a debt is expressly dealt with in section 251 TCGA, which I discuss further below.

15. If the satisfaction of a debt is clearly a disposal, is it also a disposal *to the debtor* or is it only a disposal *by the creditor*? For the purposes of capital gains charges, it does not usually matter whether the disposal is a disposal to someone else or just a

disposal by the asset owner. But HMRC argue that the wording of section 171A(1)(b) shows that it does matter here.

16. The Appellant's primary submission on this point is reliance on subsections (2)(a) and (4) of section 171. Section 171(2)(a) states that for the purposes of section 171 the satisfaction of a debt owed by Company B **to** Company A is **not** to be treated as a disposal of that debt by Company A to Company B. The Appellant argues that, in the absence of section 171(2)(a) the draftsman clearly thought that such a satisfaction of a debt **would** be a disposal by Company A **to** Company B and therefore expressly excluded it. This provision is closely allied to section 171A and a very similar phrase about disposing of an asset 'to another company' or 'to a person' is used in both provisions. Although the draftsman carved out satisfaction of a debt from the kinds of disposals covered by section 171(1), there is no such carve out from the kinds of disposals covered by section 171A. Therefore satisfaction of a debt **was** intended to be covered by section 171A.

17. Similarly, the Appellant argues that section 171(4) creates an entirely fictitious disposal 'to' someone, namely by treating a damaged or dissipated asset as having been disposed of 'to' the person who pays the compensation for that destruction or dissipation (regardless of who ends up holding the actual asset if it still exists).

18. I do not accept that the absence of a carve out from section 171A in similar terms to the carve out in section 171(2)(a) is an indication that Parliament intended that satisfaction of a debt should be treated as a disposal of the debt to the debtor by the creditor. I agree with the Tribunal's conclusion that it is equally plausible that section 171(2)(a) was placed there for the avoidance of doubt. The Tribunal referred to the speech of Lord Hoffmann in *Walker (Inspector of Taxes) v Centaur Clothes Group Ltd* [2000] 1 WLR 799 where his Lordship was considering whether the reference to unspecified circumstances which could trigger the start of an accounting period for a company would include the circumstance that something happens to create a liability to pay corporation tax. The objection to construing the relevant section as including that as a possible triggering circumstance, was that there was a specific provision elsewhere providing that if a chargeable gain or allowable loss accrued to the company then that triggered the start of an accounting period. It was argued by the Revenue that since a chargeable gain would trigger a liability to pay corporation tax the specific provision was unnecessary if the general wording bore the meaning the taxpayer argued for.

19. Lord Hoffmann said that arguments from redundancy seldom carry great weight, even in Finance Acts: "It is not unusual for Parliament to say expressly what the courts would have inferred anyway". Mr Aaronson pointed out that Lord Hoffmann went on to note that the specific provision would not be entirely redundant because it provided that the creation of an allowable loss, as well as of a chargeable gain, would trigger the commencement of an accounting period. Mr Aaronson also referred me to the many cases where the courts have held that Parliament does not legislate in vain and that one must strive to give some content to statutory provisions.

20. However, taking all those points into account, I do not regard section 171(2)(a) as indicating that Parliament intended that the disposal of a debt by satisfaction of the debt was to be regarded as a disposal of an asset to the debtor even though it has been expressly excluded from the similar phrase used in section 171(1). On the contrary, I would have expected the draftsman to make clear in section 171A that

disposals of debts effected by satisfying the debt **were** intended to be included in section 171A(1)(b) even though they were plainly not covered by section 171(1).

21. Section 171(4) does not assist the Appellant. Again, I consider that this shows the importance for the operation of section 171 of being able to identify the person to whom the asset has been disposed of in order to bring the transaction within the provision. Here it is not possible to identify someone to whom the debt is disposed of when it is satisfied.

Was there a transfer of the Loan Notes from the Appellant to NBNZ?

22. The Appellant's alternative case is that the gain which HMRC is seeking to tax here is not in fact a profit arising from the transaction that occurred in 2003 but the held-over gain from the sale of the Countrywide shares in 1998. The reason why that gain was held over, rather than brought into charge in 1998, was because the consideration for the Countrywide shares was not cash but the Loan Notes and those Loan Notes count as qualifying corporate bonds for the purposes of the TCGA. When analysing the 2003 transaction for the purposes of section 171A, the proper focus is, the Appellant submits, the Loan Notes and not the underlying debt. On their face, the Loan Notes contemplate that when the debt is satisfied the Loan Notes are transferred by the holder (that is the Appellant) to the debtor (that is NBNZ) even if only for a moment, before being cancelled by the debtor. This transaction does, therefore, involve the disposal of an asset, namely the Loan Notes, from Company A (that is the Appellant) to a person who is not a member of the group (that is NBNZ) for the purposes of section 171A(1)(b).

23. To consider this point it is necessary to back track a little to examine the provisions under which the gain arising on the sale of the Countrywide shares in 1998 came to be held over and brought into charge only when the 2003 transaction took place.

24. The starting point is the provision in section 115 TCGA which provides as follows:

> "115 **Exemptions for gilt-edged securities and qualifying corporate bonds etc**
>
> (1) A gain which accrues on the disposal by any person of—
>
> (a) gilt-edged securities or qualifying corporate bonds, or
>
> (b) any option or contract to acquire or dispose of gilt-edged securities or qualifying corporate bonds,
>
> shall not be a chargeable gain.
>
> (2) In subsection (1) above the reference to the disposal of a contract to acquire or dispose of gilt-edged securities or qualifying corporate bonds is a reference to the disposal of the outstanding obligations under such a contract.
>
> (3) Without prejudice to section 143(5), where a person who has entered into any such contract as is referred to in subsection (1)(b) above closes out that contract by entering into another contract with obligations which are reciprocal to those of the first-mentioned contract, that transaction shall for the purposes of this section constitute the disposal of an asset, namely, his outstanding obligations under the first-mentioned contract."

25. Because, as is common ground, the Loan Notes are qualifying corporate bonds, the disposal of them by the Appellant in 2003 as a result of the satisfaction of the debt by NBNZ could not of itself give rise to a capital gain in the hands of the Appellant.

26. Section 116 TCGA deals with a situation where in the course of a company reorganisation or reconstruction, shares are exchanged for qualifying corporate bonds. What it provides broadly is that, where such an exchange takes place in the circumstances to which section 116 applies, the transaction shall not be treated as a disposal of the shares at that point, but that one does at that point calculate the gain that would have arisen if the shares had been sold for cash and then treats that gain as accruing on the subsequent disposal of the bonds.

27. The key provision is section 116(10) which provides:

> "116(10)-- Except in a case falling within subsection (9) above, so far as it relates to the old asset and the new asset, the relevant transaction shall be treated for the purposes of this Act as not involving any disposal of the old asset but—
>
> (a) there shall be calculated the chargeable gain or allowable loss that would have accrued if, at the time of the relevant transaction, the old asset had been disposed of for a consideration equal to its market value immediately before that transaction; and
>
> (b) subject to subsections (12) to (14) below, the whole or a corresponding part of the chargeable gain or allowable loss mentioned in paragraph (a) above shall be deemed to accrue on a subsequent disposal of the whole or part of the new asset (in addition to any gain or loss that actually accrues on that disposal); and
>
> (c) on that subsequent disposal, section 115 shall have effect only in relation to any gain or loss that actually accrues and not in relation to any gain or loss which is deemed to accrue by virtue of paragraph (b) above."

28. The effect of section 116(10)(c) is that although section 115 serves to prevent any chargeable gain arising for the Appellant on the disposal in 2003 of the Loan Notes, it does not prevent that transaction from being the trigger for bringing into charge the held-over gain arising from the 1998 sale of the Countrywide shares.

29. Ms Yang for the Appellant demonstrated that section 116 applies to the sale of the Countrywide shares because of section 135 TCGA. That provides that where a company (Company B, in this case NBNZ) issues shares or debentures (in this case the Loan Notes) to a person in exchange for shares or debentures of another company, (Company A, in this case Countrywide) and Company B will hold more than 25 per cent of the shares in Company A, then section 127 to 131 apply with necessary adaptations as if Company A and Company B were the same company and the exchange were a reorganisation of its share capital.

30. This means that the 1998 transaction has to be treated as if it were a reorganisation of the entire share capital of a single company and sections 127 to 131 apply to that reorganisation.

31. Turning then to the provisions about reorganisations of share capital, section 127 provides that a reorganisation shall not be treated as involving any disposal of 'original shares' or any acquisition of a 'new holding' but rather the original shares and the new holding are treated as the same asset and as having been acquired 'as the original shares were acquired'. Section 126 then defines the terms 'original shares' and 'new holding' as follows:

“126 **Application of sections 127 to 131**

(1) For the purposes of this section and sections 127 to 131 “reorganisation” means a reorganisation or reduction of a company’s share capital, and in relation to the reorganisation—

(a) “original shares” means shares held before and concerned in the reorganisation,

(b) “new holding” means, in relation to any original shares, the shares in and debentures of the company which as a result of the reorganisation represent the original shares (including such, if any, of the original shares as remain).”

32. Thus, the Appellant sayS, it is clear that the ‘new holding’ for the purpose of applying sections 127 to 131 to the 1998 transaction is the debentures (that is the Loan Notes) and the ‘original shares’ are the shares in Countrywide.

33. Turning back to section 116, this deals with how sections 127 – 131 apply where either the new holding or the original shares comprise qualifying corporate bonds, as is the case here. First, section 116(1) makes clear that those terms bear the same meaning in section 116 as they bear for the purposes of sections 127 – 131:

“116 **Reorganisations, conversions and reconstructions**

(1) This section shall have effect in any case where a transaction occurs of such a description that, apart from the provisions of this section—

(a) sections 127 to 130 would apply by virtue of any provision of Chapter II of this Part; and

(b) either the original shares would consist of or include a qualifying corporate bond and the new holding would not, or the original shares would not and the new holding would consist of or include such a bond;

and in paragraph (b) above “the original shares” and “the new holding” have the same meaning as they have for the purposes of sections 127 to 130.”

34. Subsection (4) of section 116 then introduces two new tags: ‘the new asset’ and ‘the old asset’ for the purpose of applying the remaining subsections:

“116(4)— Where the qualifying corporate bond referred to in subsection (1)(b) above would constitute the new holding for the purposes of sections 127 to 130, it is in this section referred to as “the new asset” and the shares or securities which would constitute the original shares for those purposes are referred to as “the old asset”.”

35. Subsections (5) and (6) of section 116 then disapply the provisions that relate to corporate reorganisations in sectionS 127 – 130 so that those provisions can be replaced by the remaining provisions of section 116:

“(5)— So far as the relevant transaction relates to the old asset and the new asset, sections 127 to 130 shall not apply in relation to it.

(6)— In accordance with subsection (5) above, the new asset shall not be treated as having been acquired on any date other than the date of the relevant transaction or, subject to subsections (7) and (8) below, for any consideration other than the market value of the old asset as determined immediately before that transaction.”

36. Subsection (9) of section 116 then deals with the situation (which is not the situation here) where the old asset is the qualifying corporate bond and the new asset is the shares. Subsection (10) which I have set out earlier deals with the situation (which is the situation here) where the old asset is the shares and the new asset is the qualifying corporate bond. As I have already explained, subsection (10) provides that the relevant transaction shall not be treated as a disposal of the shares in Countrywide but that a gain is calculated as if those shares had been sold for cash at market value; that gain is then deemed to accrue on the subsequent disposal of the whole or part of ‘the new asset’ and on that subsequent disposal, if it is a disposal of a qualifying corporate bond, the exemption in section 115 does not prevent that held-over gain from being brought into charge.

37. The Appellant argues that the disposal which triggers the bringing into charge of the held-over gain is, according to section 116(10) the disposal of the whole or part of the ‘new asset’ and the ‘new asset’ for these purposes is, according to section 116(4), the qualifying corporate bond which constitutes the ‘new holding’ for the purposes of section 116(1) and sections 127 to 130. The Appellant submits that HMRC and the First-tier Tribunal were therefore wrong to say that the relevant asset disposal for the purposes of section 171A(1)(b) TCGA was the satisfaction of the debt and the Tribunal should have accepted that the asset disposal was the disposal of the qualifying corporate bonds.

38. The Appellant supports this submission by showing that the legislative context of these provisions does recognise that the qualifying corporate bond is a distinct asset from the underlying debt. The Loan Notes are an intangible asset constituted in this case by a deed poll. The separate existence of the Loan Notes is, the Appellant says, confirmed not only by the provisions of section 115 and 116 to which I have already referred but by section 251 TCGA. Section 251 deals with the situations in which a chargeable gain (or loss) can arise on the satisfaction of a debt:

> “**251 General provisions**
>
> (1) Where a person incurs a debt to another, whether in sterling or in some other currency, no chargeable gain shall accrue to that (that is the original) creditor … on a disposal of the debt, except in the case of the debt on a security (as defined in section 132).
>
> (2) Subject to the provisions of sections 132 and 135 and subject to subsection (1) above, the satisfaction of a debt or part of it (including a debt on a security as defined in section 132) shall be treated as a disposal of the debt or of that part by the creditor made at the time when the debt or that part is satisfied.”

39. Section 132(3)(b) defines a ‘security’:

> “‘security” includes any loan stock or similar security whether of the Government of the United Kingdom or of any other government, or of any public or local authority in the United Kingdom or elsewhere, or of any company, and whether secured or unsecured.”

40. Mr Aaronson explained the policy behind section 251 as intended to prevent companies from claiming that they have suffered a capital loss when they write off a bad debt so that the disposal of a debt only generates a gain or loss for this purpose when the debt is effectively traded. The term ‘debt on a security’ was considered by Lord Wilberforce in *Aberdeen Construction v IRC* [1978] STC 127 when construing the predecessor provisions which were in identical terms to section

132 TCGA. He noted that since a security can be 'secured or unsecured' according to what is now section 132, the term 'the debt on a security' could not be a synonym for a secured debt. As to which unsecured debts came within the exclusion in the final clause of what is now section 251(1), Lord Wilberforce found it impossible to discover any principle on which to state a discrimen. Having considered provisions about corporate debts in other contexts he concluded:

> "the only basis on which a distinction can be drawn is between a pure unsecured debt as between the original borrower and lender on the one hand and a debt (which may be unsecured) which has, if not a marketable character, at least such characteristics as enable it to be dealt in and if necessary converted into shares or other securities."

41. He held that the debt in question in those proceedings had no quality or characteristic which brought it within whatever special category is meant by 'debt on a security'.

42. The definition of a qualifying corporate bond in section 117 TCGA also indicates that the bond is something different from or additional to the underlying debt. In fact, section 117 provides two definitions of qualifying corporate bond; one for the purposes of corporation tax (which is the purpose relevant in this case) and one for any other purpose.

43. For the purpose of corporation tax, section 117(A1) provides:

> "117(A1)— For the purposes of corporation tax, "qualifying corporate bond" means any asset representing a loan relationship of a company; …."

44. For other purposes the definition is more complicated but includes the provision in section 117(1) that:

> "117(1)— For the purposes of this section, a "corporate bond" is a security, as defined in section 132(3)(b)—
>
> (a) the debt on which represents and has at all times represented a normal commercial loan; and
>
> (b) which is expressed in sterling and in respect of which no provision is made for conversion into, or redemption in, a currency other than sterling, …"

45. Again, the Appellant says, the definition in section 117(1), though not the governing definition in this case, shows that the security is something different from the debt.

46. The phrase 'loan relationship of a company' in section 117(A1) is defined in section 81 of the Finance Act 1996 which deals with the taxation of loan relationships. I will need to refer to that later.

47. The First-tier Tribunal accepted HMRC's submission that the capital gains tax legislation 'is concerned with the underlying debts, even when they are in the form of a debenture' and held that it is the debt that is the asset for CGT purposes: see paragraphs 32 and 33 of the decision.

48. In the light of the Appellant's analysis of the relevant statutory provisions I do not agree with the Tribunal's conclusion on this point. In my judgment, assuming that one can draw a distinction between the Loan Notes and the debt, the relevant statutory provisions clearly focus on the former and not the latter. I agree with the

Appellant that the reason why HMRC is bringing this gain into charge now, and not in 1998, is because the consideration for the sale of the Countrywide shares involved the acquisition by the Appellant of qualifying corporate bonds and because those bonds, or part of them, have now been disposed of.

49. I accept therefore the Appellant's submission that the right question to ask in this aspect of the case is not whether the debt has been disposed of 'to' NBNZ but whether the Loan Notes were disposed of 'to' them.

50. Having shown that the disposal that took place in the transaction in 2003 between NBNZ and the Appellant was not (or not only) the disposal of the debt by satisfaction of the debt but also the disposal of the separate and distinct Loan Notes, the Appellant moves to the next necessary step, that is to establish that the Loan Notes were disposed of **to** NBNZ for the purposes of section 171A of the TCGA.

51. HMRC, as I understood Mr Gibbon's submissions, did not rule out that the Loan Notes for some purposes could be treated as a separate asset from the debt. What they disputed was, first, the idea that it was the disposal of the Loan Notes rather than the debt that was relevant for the purposes of section 171A and secondly that the Loan Notes could continue in existence once the debt had been satisfied in order to be capable of being disposed of to NBNZ. The First-tier Tribunal, having agreed with HMRC on the first point, did not decide whether the Loan Notes continue in existence after the debt is satisfied.

52. I now turn to consider whether as a matter of fact and law, the Loan Notes were transferred to NBNZ when the debt was satisfied in 2003. The Appellant argues that the terms of the deed poll which comprises the terms of the loan clearly contemplate such a transfer. The deed poll dated 10 September 1998 made by NBNZ provides as follows.

    a. The Issuer must keep a register showing the names and other details of the holders of the Notes for the time being.

    b. Each Noteholder (defined as a person for the time being entered on the Register as the holder of Notes) is entitled without charge to certificates for the notes registered in its name with each certificate representing Notes in denominations of NZ$10 million or multiples thereof.

    c. The payment of the Notes is guaranteed by Lloyds Bank plc.

53. As far as repayment, purchase or redemption of the Loan Notes is concerned:

    a. paragraph 1.1. of the Second Schedule to the Loan Notes provided that each Noteholder was entitled to require the Issuer (that is NBNZ) to repay the whole or any part of the Loan Notes. To exercise that entitlement the Noteholder must complete the Notice of Repayment in the terms set out in the Schedule, stating the amount required to be repaid and the date for repayment and lodge that Notice at the registered office of the Issuer not less than 30 days prior to the date on which repayment is required.

    b. Paragraph 4.1 of the Second Schedule provided that every Noteholder whose Notes were due to be repaid must, at least five business days before the due date for repayment, deliver up to the Issuer the Certificate for its Notes which are due to be repaid and upon the delivery of that Certificate the Issuer repays the amount required on the due date.

c. Paragraph 5 then states (emphasis added):

"CANCELLATION

All Notes repaid, redeemed or purchased by the Issuer **shall be cancelled forthwith thereafter** and the Issuer shall not be at liberty to keep the same of the purposes of re-issue or to re-issue the same".

54. The Appellant submits that the Loan Notes contemplate therefore that, even if only for a moment, the Loan Notes are transferred to the Issuer because it is the Issuer who then cancels them 'forthwith thereafter' in accordance with paragraph 5. There must be a period of time between the moment of repayment and the moment of cancellation of the Loan Notes and that means that the Loan Notes are indeed disposed of by the Appellant to NBNZ so that NBNZ can forthwith thereafter cancel them.

55. The Appellant says that there is nothing unusual about the idea of the Loan Notes surviving the repayment of the underlying debt. They point to section 194 of the Companies Act 1985 which was in force at the relevant time and which deals with a company's power to re-issue debentures that have previously been redeemed. This provides:

"**194 Power to re-issue redeemed debentures**

(1) Where (at any time) a company has redeemed debentures previously issued, then –

(a) unless provision to the contrary, whether express or implied, is contained in the articles or in any contract entered into by the company; or

(b) unless the company has, by passing a resolution to that effect or by some other act, manifested its intention that the debentures shall be cancelled,

the company has, and is deemed always to have had, power to re-issue the debentures, either by re-issuing the same debentures or by issuing other debentures in their place."

56. The reference in the full out of the subsection there to 're-issuing the same debentures' after the debentures have been redeemed is relied on by the Appellant as showing that debentures continue in existence even after they have been redeemed because the company has the choice either to cancel them or to 're-issue' them.

57. The Appellant further relies on the decision of the House of Lords in *City of Edinburgh v British Linen Bank* [1913] AC 133 where Viscount Haldane referred to the City's power to raise money by issuing perpetual annuities "redeemable in the sense of being repurchasable' upon certain terms. It does not appear to me, however, that the point being considered in that case was at all similar to the point at issue here, since it involved the construction of statutory provisions to determine whether the City had an obligation as well as a right to redeem certain stocks at a particular date.

58. HMRC argue that where the debt is repaid, there is no disposal of the note to the issuer or acquisition of the note by the issuer; the note simply ceases to exist. The mechanics of cancellation (such as they are) are merely the physical demonstration

that the bundle of rights comprising the Loan Note has come to an end. Mr Gibbon points out that the statutory provisions dealing with qualifying corporate bonds are all predicated on the existence of a subsisting debt. Thus:

a. Section 117(1) defines the bond (albeit for purposes other than corporation tax) as a security 'the debt on which represents and has at all times represented' a normal commercial loan. This is in the present tense indicating that there must be a debt in existence which the bond represents;

b. Section 117(A1) defines the bond for the purposes of corporation tax by reference to the concept of the 'loan relationship' and that is itself defined in section 81(1) and (2) of the Finance Act 1996 as arising where the company 'stands… in the position of a creditor or debtor as respects any money debt' and where the debt is one arising from a transaction for the lending of the money.

59. On this point I accept the submissions of Mr Gibbon that the qualifying corporate bonds cannot outlive the existence of the debt which they represent. Thus, even if, during the currency of the Loan Notes, they can be regarded as existing separately from the debt for certain purposes, they cannot have any existence after the debt is redeemed, not even for a moment. I do not accept either that the wording of paragraph 5 of the Second Schedule of the Loan Notes or section 194 of the Companies Act 1985 indicates to the contrary. The Loan Notes comprise the terms on which the debt falls to be repaid. It is true that these terms may be more or less complicated and may involve a third party such as the guarantor. The debt on the terms set out in the Loan Notes can be bought and sold whilst some of the money is still owed. But as soon as the debt is repaid, the parties are released from those obligations and those obligations are not transferred from one to the other. If rights have accrued because of some default by a party, then the Loan Note terms may still be relevant in working out what those rights are. But those rights are different from the rights under the Loan Notes themselves and are certainly not transferred as between the parties. A company may decide to 're-issue' a debenture rather than cancel it but that says no more than that it has decided to enter into a fresh loan relationship once the old one has come to an end, albeit on the same terms as the old debenture.

60. I therefore reject the submission that there is a period in time between the debt being repaid and the Loan Notes being 'cancelled' when the Loan Notes continue in existence and are transferred by the Appellant to NBNZ. The Loan Notes came to an end at the moment that the debt was repaid and were not transferred to NBNZ by the Appellant. There may thereafter have been some action on the part of NBNZ that constituted 'cancelling' Loan Notes. It cannot be suggested that the handing over of the physical certificates is the transfer of the Loan Notes (assuming that such a handing over actually happens) because that must occur five days before repayment. The mechanism of that early hand over of the Certificates and the 'cancellation' of the Notes 'forthwith' on the repayment of the debt was a procedure most likely designed to forestall any attempt by the Noteholder to sell the Note shortly before repayment. What is actually involved now in fulfilling the obligations to 'deliver up' the Certificates or 'cancel' the Loan Notes is not at all clear, now that the world of unique, physical documents and red ink pads and stamps has receded into the past. Whatever it may mean in a world of electronic

communications, I find that it does not mean that the Loan Notes survive the repayment of the debt.

61. I therefore hold that there was nothing transferred by the Appellant to NBNZ when the Loan Notes were repaid on 28 November 2003 and hence that there was no disposal of either the debt or the Loan Notes ‘to’ NBNZ for the purposes of section 171A of the TCGA.

A purposive construction of section 171A TCGA

62. The Appellant’s final ground of appeal is that the First-tier Tribunal erred in refusing to adopt a purposive construction of section 171A TCGA and in refusing to recognise that the ‘hyper-literal’ construction argued for by HMRC went against the clear Parliamentary intention in enacting the provision. The Appellant and HMRC are agreed as to the principles that must be applied to construing legislation, including tax legislation. The Tribunal referred to the speech of Lord Nicholls in *Barclays Mercantile Business Finance Ltd v Mawson* [2004] UKHL 51 where he cited Ribeiro PJ in *Collector of Stamp Revenue v Arrowtown Assets Ltd* [2003] HKCFA 46 who said:

> “[T]he driving principle in the *Ramsay* line of cases continues to involve a general rule of statutory construction and an unblinkered approach to the analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically."

63. The Tribunal went on cite extensively from the key authorities on statutory construction including *R v Environment Secretary ex parte Spath Homes Ltd* [2001] 2 AC 349, *Chevron UK Ltd v IRC* [1995] STC 712 and *Bibby v Prudential Assurance Co Ltd* [2000] STC 459. There is no issue between the parties about the authorities on which the Tribunal relied in directing itself as to the proper approach to construction. However, the Appellant submits that the Tribunal was wrong to ignore materials that were directly relevant to the proper construction of section 171A, including an extract from Hansard, the Budget Notes and the Explanatory Notes relating to clause 100 of the Finance Bill (which became section 101 of the Finance Act 2000 and which introduced section 171A into the TCGA).

64. I can deal with this point shortly since I am entirely in agreement with the conclusion that the First-tier Tribunal reached, namely that the extra-statutory materials relied on by the Appellant do not require or permit me to construe section 171A as widely as the Appellant wishes.

65. The material relied on by the Appellant shows that the purpose of section 171A was to enable corporate groups to match chargeable gains and allowable losses between sister companies without having to transfer asset ownership within the group. What those materials do not show was that Parliament intended to achieve that goal in respect of *all* disposals by sister companies. The materials explain why section 171A was enacted but they do not say anything about the scope of section 171A and it is the scope that is at issue in this appeal. The high point of the Appellant’s submissions is a reference in the Budget Notes referring to the effect of the new section 171A as being that two members of the group may jointly elect that an asset ‘which has been disposed of outside of the group’ can be treated as having been transferred immediately before that disposal. This is simply a paraphrase of the

provision as enacted and cannot justify ignoring the clear words of section 171A(1)(b) in requiring that there be a disposal to another person outside the group.

66. Both sides accept that there were various kinds of disposals that could give rise to losses but which were not covered by the wording of section 171A because of its apparent requirement that there be not only a disposal but a disposal to someone outside the group. For example, there may be a loss where a non-trading asset is appropriated to trading stock (see section 161 TCGA 1992) or where a company ceases to be resident in the United Kingdom (see section 185 TCGA 1992). In such cases there is no change in either the physical nature or the ownership of the asset.

67. It is also accepted by both sides that the new wording of section 171A, introduced by section 31 of the Finance Act 2009, would allow a valid joint election by the Appellant and GR3 in the present circumstances because it refers to the transfer of gains and losses between members of the same group rather than to the transfer of assets to a person outside the group.

68. The Appellant criticises the decision of the First-tier Tribunal in so far as the Tribunal relied on the judgment of Oliver LJ in *Finch v IRC* [1985] 1 Ch 1. The Tribunal referred to that case as establishing that it is only where earlier legislation is ambiguous, in the sense that there are two perfectly clear and plain constructions possible, that recourse may be had to subsequent legislation as an aid to construction. The Tribunal accepted HMRC's submission that there was nothing ambiguous about the wording of section 171A as it stood in 2003 so that the Tribunal was not entitled to rely on the 2009 amendment of the provision in order to construe it. The Appellant submits that the requirement that there be an ambiguity in the earlier legislation before subsequent legislation can be used as an aid to interpretation had been overturned by the House of Lords in *R v Environment Secretary ex parte Spath Holme Ltd* [2001] 2 AC 349. Lord Bingham of Cornhill and Lord Cooke of Thorndon in *Spath Holme* referred to a less demanding level of ambiguity than appears to have been contemplated by Oliver LJ in *Finch* in that Lord Bingham described words as being 'ambiguous' if they were fairly susceptible of bearing more than one meaning and Lord Cooke stated that a provision is ambiguous 'if reasonably open on orthodox rules of construction to more than one meaning'.

69. I am prepared to accept for present purposes that it is permissible to consider the revision of section 171A in 2009 as an aid to construing the earlier provision. However, there is nothing in the new version which enables me to conclude that Parliament's intention in revising the section was not to extend the previous ambit of section 171A but merely to clarify its already wide scope. The change to section 171A took effect in relation to chargeable gains and allowable losses accruing on or after 21 July 2009: see Schedule 12 to the Finance Act 2009. That Schedule not only substituted the new section 171A but added in sections 171B and 171C as well as making certain consequential amendments to other provisions in other legislation. This suggests that Parliament was making a significant change to the effect of the pre-2009 provisions. I do not accept that the re-casting of section 171A in 2009 permits me to construe the earlier provision as covering the same broad ground as is now covered. The recasting of section 171A in order to achieve that result was substantial, not a few minor amendments to the wording.

70. I therefore reject the Appellants' submission that a purposive construction of section 171A entitles or requires me to ignore the reference in section 171A(1)(b) to the disposal being to a person outside the group.

Disposition

71. I therefore conclude for the reasons set out above that the appeal must be dismissed.

Signed

Mrs Justice Rose

RELEASE DATE: 3 March 2014