TC02851

Appeal number: TC/2010/5874, 5872, 5867, 5869, 5864, 5865 & 5858

Corporation Tax – capital gains- pre entry losses: Sch 7A TCGA- successive takeovers*-Prizedome-** ***appeals dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

(1) GREATHEY INVESTMENTS LIMITED **Appellant**
(2) HELICONIA LIMITED
(3) PEEL AIRPORTS (AESPL) LIMITED
(4) PEEL PORTS (BIHL) LIMITED
(5) PEEL PROPERTY (SDL) LIMITED

- and -

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

TRIBUNAL: JUDGE CHARLES HELLIER
JOHN CHERRY

Sitting in public at 45 Bedford Square WC1B 3DN on 29, 30 and 31 May 2013

David Goldberg QC instructed by Travers Smith LLP for the Appellants

Akash Nawbatt, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

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DECISION

Introduction.

1. These appeals concern the application of the restrictions on the use of "pre-entry losses" - that is to say losses realised by a company before it joins a group - in Schedule 7A TCGA 1992. There has been only one other set of reported appeals which reached the higher courts on the application of these provisions. Those were in the combined cases of *Revenue and Customs Commissioners v Prizedome* and *Revenue and Customs Commissioners v Limitgood*. Those appeals are reported at [2009] STC 1980 (Court of Appeal) and [2008] STC 361 (High Court).

2. Those appeals, like the present ones, related to the provisions of Schedule 7A which applied when one group of companies (we shall call it the Target group) became part of another group (which we shall call the Acquiring group) as the result of what we shall call a "takeover" in which the principal company of the Target group was acquired by the Acquiring group. In a nutshell in the present appeals Mr Nawbatt says that the reasoning of the courts in *Prizedome* applies in these appeals; Mr Goldberg suggests that the reasoning in those was misguided and that in any event it is not applicable to the circumstances of these appellants.

3. When the hearing started there was a second set of appellants whose facts differed from those of the remaining appellants. On the morning of the second day HMRC withdrew their challenge to their appeals. In those appeals a loss company had been acquired by a group, which after some intervening transactions became part of another group. But whereas in the remaining appeals all changes of group had been as the result of a takeover of the principal company of the group by another group, in the situation of the second set of appellants the intervening transactions had involved the disposal of part of a group (containing the loss companies) to another group.

The facts.

4. The facts were agreed. They may be summarised thus:

5. (A) Transactions in relation to Peel subsidiaries

(1) In 1987 Largs limited (a non-UK resident company) owned 100% of Greathey Investments Limited (the 1st Appellant) to which it transferred the shares of Higham Limited. Largs was not at that time a 75% subsidiary of any other company.

(2) In 1988 Greathey sold Higham and realised a capital loss of some £27 million. This is the “Greathey loss”. By this time Greathey had other UK resident 75% subsidiaries (together “the Greathey group”).

(3) In 1991 Peel Holdings plc (“PH”), a UK resident company which was not a 75% subsidiary of any other company and had

existing 75% subsidiaries (forming the “PH group”), acquired 100% of Largs.

(4) In 2000 PH realised a capital loss on the sale of shares in Eleco Holdings plc of some £629K. This is the "Eleco loss".

(5) In March 2004 three of PH’s wholly owned subsidiaries each acquired a company with existing capital losses. These capital loss companies we shall call the "2004 loss companies" and are the 3rd, 4th and 5th Appellants..

(6) In August 2004 Peel Acquisitions Limited (PAL), a newly formed company, acquired 100% of PH.

(7) In the years ended 31 March 2005, 2006, and 2008, gains were made by companies within the PAL group (we understood that these gains arose from assets held by PH group members before PH was taken over by PAL at step (5) and did not arise from assets held by members of the Greathey group at the time it was taken over by the PH group) in respect of which elections were made under section 171A and 179A TCGA that they be treated as disposals by the 1st, 3rd, 4th and 5th Appellants so that those gains might be reduced by the losses which are the subject of these appeals.

6. (B) The Heliconia transactions

(a) In March 2005, Cronkdean, a company wholly owned by Tokenhouse Holdings Limited (the majority shareholder in PAL) acquired 100% of Heliconia Ltd (the 2nd Appellant), a company without subsidiaries which had existing realised capital losses.

(b) In October 2005 (in the following accounting period of Heliconia) TIGL (a Guernsey resident company) acquired 100% of the share capital of Tokenhouse Holdings.

(c) On 14 October 2005 (we assume after (b)) Cronkdean realised a capital gain. It elected under section 171A TCGA to treat the disposal as having been made by Heliconia so that the gains might be reduced by Heliconia’s losses.

Commentary.

7. Section 170 TCGA defines the meaning of "group" for purposes of Chapter 1 Part VI TCGA 1994. A group is defined by its principal holding company. Prior to March 2000 a non-resident company could not be the principal company of a group although ownership could be traced through non-resident companies for the purposes of determining whether the ownership test for membership of a group was satisfied.

8. As a result of the relevant group definitions (leaving aside for the moment any affect section 170(10) TCGA might have) it was uncontentious that:

(1) Before Greathey acquired Highams in 1987, Greathey was not a member of a group. On the acquisition at step (A)(1) Greathey became the principal company of the Greathey group. The Greathey loss of £27 million arose when it was a member of that group.

(2) At step (A)(3), when PH acquired Largs, the Greathey group joined the PH group, and Greathey and its subsidiaries were thereafter part of the PH group.

(3) The Eleco loss was realised at step (A)(4) by PH when it was the principal company of the PH group.

(4) The 2004 loss companies joined the PH group in March 2004 at step (A)(5).

(5) In August 2004 PH and its subsidiaries became members of the PAL group

(6) Heliconia joined the Tokenhouse group in 2005 at step (B)(a).

(7) Heliconia became part of the TIGL group at step (B)(b).

9. There are some other facts to record which relate to the provisions of paragraphs 1 (7) and 9(6) of Schedule 7A and mean that those paragraphs do not have any direct application in relation to this appeal.

10. Immediately before step (A)(3) when Greathey became a member of the PH group, the persons who owned its share capital were not the same as those who owned the share capital of PH. The time when Greathey became the principal company of the Greathey group was not in the same accounting period as that in which Greathey became a member of the PH group. Greathey was not, immediately before it became a member of the PH group controlled by a company which was a member of the PH group.

11. The same statements apply appropriately modified to PAL's takeover of PH and the takeover of the Tokenhouse group by TIGL.

The legislation.

12. Schedule 7A TCGA is given effect by section 177A TCGA which itself lies in Chapter 1 of Part VI of that Act. That Chapter deals with the gains and losses of groups of companies. Those provisions include those: for the no gain/no loss intragroup transfer of assets in section 171, for the notional transfer of assets intragroup, so that a gain made by one group company can be treated as realised by another group company in section 171A (and also 179A); and, in section 179, for the imposition of an exit charge – a deemed disposal and reacquisition – if a company leaves a group holding assets acquired from other group members.

13. The chapter begins with section 170 which provides definitions and interpretation for the purposes of sections 171 to 181. It defines a group to be a principal company and those of its 75% subsidiaries which are effective 51% subsidiaries. Subsection (10) deals with one group being taken over by another. It applies "for the interpretation of sections 171 to 181" and provides:

"(10) For the purposes of this section and sections 171 to 181 [which thus includes schedule 7A], a group remains the same group so long as the same company remains the principal company of the group, and if at any time the principal company of a group becomes a member of another group, the first group and the other group shall be regarded as the same and the question whether or not a company has ceased to be a member of a group shall be determined accordingly."

14. Section 177A describes Schedule 7A as making provision for losses (later defined as pre entry losses) accruing to a company before the time it becomes a member of a group of companies and losses accruing on assets held by a company at such a time (which are later defined as pre entry assets). Much of the Schedule is taken up with matters relating to pre entry assets. This appeal related to the effect of the provisions related to pre entry losses.

15. Paragraph 1 of the Schedule contains provision for the application and construction of the Schedule including a definition of “pre entry loss”. So far as relevant to this appeal it provides:

"1 (1) This Schedule shall have effect, in the case of a company which is or has been a member of a group of companies ("the relevant group"), in relation to any pre-entry losses of that company.
(2) In this Schedule "pre-entry loss", in relation to any company, means-
(a) any allowable loss that accrued to that company at a time before it became a member of the relevant group; or
(b) the pre-entry proportion of any allowable loss accruing to that company on the disposal of any pre-entry asset.
……..
[(3), (4) and (5) relate to "pre-entry assets"]

(6) Subject to so much of sub-paragraph (6) of paragraph 9 below as requires groups of companies to be treated as separate groups for the purposes of that paragraph, if-
(a) the principal company of a group of companies ("the first group") has at any time become a member of another group ("the second group") so that the two groups are treated as the same by virtue of subsection (10) of section 170, and
(b) the second group, together in pursuance of that subsection with the first group, is the relevant group,
then, except where subparagraph (7) below applies, the members of the first group shall be treated for the purposes of this Schedule as having become members of the relevant group at that time and not by virtue of that subsection at the times when they became members of the first group".

(7) [applies where the takeover was by a new non group holding company with the same shareholders and whose assets after the takeover were almost entirely the Target group].

……..

16. When referring to a group to which particular provisions are relevant it is easy to refer to it as "the relevant group". In the context of these provisions "the relevant group" is used in a particular way. We shall endeavour to limit our use of the phrase to that used in the Schedule.

17. Paragraphs 2, 3, 4 and 5 are taken up with pre entry assets. Paragraph 6 provides for how much of a pre entry loss may be set against a chargeable gain, providing that if paragraph 7 permits the deduction of a pre entry loss from a gain that may be done, but the reminder of the pre entry loss is to be carried forward and not used against other gains.

18. Paragraph 7(1) provides:

> "(1)A pre entry loss that accrued to a company before it became a member of the relevant group shall be deductible from a chargeable gain …if that gain is one accruing:
>
> (a) on a disposal made by that company before the date on which it became a member of the relevant group (the "entry date");
>
> (b) on the disposal of an asset which was held by that company immediately before the entry date; or
>
> (c) on the disposal [of a trading asset acquired from a third party]."

19. Paragraph 7(3) provides that: "Where two or more companies become members of the relevant group at the same time and those companies were all members of the same group of companies immediately before they became members of the relevant group, then" an asset held by one on the entry date may be treated as held by another so that for the purposes of the offsetting rule in para 7(1) they are effectively treated as a single company.

20. It is by virtue of this provision and elections made under section 171A and 179A that in these appeals gains made by companies other than the loss making companies are said to be eligible for the offset of pre entry losses of other group companies. The key issue is the date on which the companies became members of "the relevant group". For the paragraph 7(1) offset to be permitted the asset must be or be treated as having been held by the company making the loss on the date the company joined the relevant group.

21. Paragraph 8 is irrelevant. Paragraph 9 is headed: "Identification of 'the relevant group' and application of Schedule to every connected group" and provides:

> 9. (1) This paragraph shall apply where there is more than one group of companies which would be the relevant group in relation to any company.

(2) Where any loss has accrued on the disposal by any company of any asset, this Schedule shall not apply by reference to any group of companies in relation to any loss accruing on that disposal unless-

(a) that group is a group in relation to which that loss is a pre-entry loss by virtue of paragraph 1(2)(a) above or, if there is more than one such group, the one of which that company most recently became a member;

(b) that group, in a case where there is no group falling within paragraph (a) above, is either-

(i) the group of which that company is a member at the time of the disposal, or

(ii) if it is not a member of a group of companies at that time, the group of which that company was last a member before that time;

(c) that group, in a case where there is a group falling within paragraph (a) or (b) above, is a group of which that company was a member at any time in the accounting period of that company in which it became a member of the group falling within that paragraph;

[(d) and (e) provide other cases];

and subparagraphs (3) to (5) below shall apply in the case of any loss accruing on the disposal of any asset where, by virtue of this subparagraph, there are two or more groups (“connected groups”) by reference to which this schedule applies.

[(3), (4) and (5) provide for the separate application of the schedule in relation to each of the connected groups and broadly for (none or) the smallest amount of any loss to be deductible in respect of any gain as such amount arises by virtue of the separate application of the schedule to each connected group]

(6) Notwithstanding that the principal company of one group ("the first group") has become a member of another group ("the second group"), those two groups shall not by virtue of section 170(10) be treated in relation to any company that is or has become a member of the second group ("the relevant company") as the same group for the purposes of this paragraph if-

(a) the time at which the relevant company became a member of the first group is a time in the same accounting period as that in which the principal company of the first group became a member of the second group ; or

(b) the principal company of the first group was under the control, immediately before it became a member of the second group, of a company which at that time was already a member of the second group.

Mr Goldberg's arguments.

22. Mr Goldberg says that these provisions apply in relation to realised losses in the following manner.

> (1) Identify a company (company A),
>
> (2) Identify all the groups of which A is or has ever been a member. Each of these groups is a relevant group for the purposes of paragraph 1.
>
> (3) Determine the time A entered each such relevant group.
>
> (4) Consider whether A made a capital loss which accrued before A became a member of any of those relevant groups. If so that loss is a pre-entry loss.
>
> (5) Determine in relation to each relevant group in accordance with paragraph 7, the gains against which that loss may be offset.
>
> (6) If there is more than one relevant group then apply paragraph 9. This, in the case of a pre entry loss, will either determine to which relevant group the Schedule is to be applied by reference to a selection made by that paragraph from a set of relevant groups, or limit the amount deductible by reference to only one member of the set.

23. Key to this approach is the premise that paragraph 1(1) does not identify only one group but makes any group of which A has been a member a "relevant group". Mr Goldberg says that this approach is indicated by the language of paragraph 1(1) which, in speaking of:

> "a company which is or has been a member of a group of companies ("the relevant group")",

indicates that there may be many groups of which it may have been a member and that the tests in the Schedule are to be applied in respect of each of them. By using "the relevant group" the language of the paragraph indicates that only those groups of which the company has been a member are to be party to the test. The language invites you to choose one of the groups and to set out on a voyage of discovery with it in your hand, but to repeat the process for all other relevant groups. While journeying with a particular group in hand, that group is the “relevant group” for the purposes of the Schedule. Whatever else is express or implicit in paragraph 1(1), it does not say that the relevant group is the earliest one the company joined by reference to which the loss would be a pre-entry loss.

24. Mr Goldberg finds support in paragraph 9(1) which acknowledges that there may be more than one company which "would" be the relevant group: "would", he says, is the subjunctive, indicating the world of possibilities opened by paragraph 1(1), but potentially limited by the following subparagraphs of paragraph 9.

25. He finds further support in:

(1) paragraph 9(2)(a) which expressly recognises that there may be "more than one ... group" in relation to which a particular loss is a pre-entry loss by virtue of paragraph 1(2)(a);

(2) in paragraph 9(2)(c) which expressly acknowledges that a group of which the company was a member before or after it was a member of the group chosen by paragraph 9(2)(a) is not only a relevant group but will be a (relevant) group to which the Schedule applies. That group could not be made a relevant group by the language of paragraph 9(2) and so will have been already made a relevant group by paragraph 1(1); and

(3) in paragraph 9(3)'s requirement to apply the Schedule separately to each such group

26. Finally Mr Goldberg notes that in relation to pre-entry assets, the object of the Schedule can be seen from paragraph 9 as to treat as a pre-entry loss the portion of the loss which pro rata temporis accrued before the company holding the asset joins a group of which it is a member when the disposal takes place. Thus the type of limitation which would have to be made to the language of paragraph 1(1) to make it have the effect of selecting only one group as the relevant group for a pre-entry loss would be startlingly different from that which would apply in the selection of the group relevant to a pre-entry asset.

27. Now, in order to determine whether a loss accrued before a company became a member of a particular relevant group, it is necessary to know when the company became a member of the group. This is step (3). This date, the "entry date", is also needed for the application of paragraph 7 to determine whether a pre-entry loss may be set against a gain. That is because paragraph 7 provides that a loss may be set against a gain only on a disposal made before, or assets held on, the entry date (or of assets which are third party acquired "trade" assets).

28. Mr Goldberg says that the entry date is determined thus:

(1) when a company which is not part of a group is taken over by an acquirer, it becomes a member of the group on the date on which that happens. That is the entry date.

(2) In the absence of any provision to the contrary, the same rule applies when a Target group is taken over - every company in the Target group becomes a member of the Acquiring group on the takeover.

(3) Section 170 (10), which provides:

> "For the purposes of this section [and Schedule 7A], a group remains the same group so long as the same company remains the principal company of the group, and if at any time the principal company of a group becomes a member of another group, the first group and the other group shall be regarded as the same, and the question whether or not a company has ceased to be a member of a group shall be determined accordingly.",

does not alter the general rule; it merely makes sure that the target companies are not treated as leaving a group by virtue only of a takeover.

(4) Paragraph 1(6), rather than altering the position, confirms that where the conditions of that subparagraph are satisfied (and paragraph 1(7) does not apply), the entry date remains the date of the takeover. When the conditions are not satisfied or paragraph 1(7) applies, the entry date is the date the target subsidiaries joined the Target group.

29. We shall return to the arguments in relation to section 170(10) and paragraph 1(6) after we have discussed *Prizedome* in which the effects of section 170(10) and paragraph 1(6) were crucial to the judgements.

30. Thus, having determined the entry date in relation to any particular group, Mr Goldberg says that one is now in a position to apply paragraph 7 and paragraph 9.

31. On the facts Mr Goldberg says that Schedule 7A applies thus:

(A) The Eleco loss

32. This loss was used by PH in accounting periods ended 31 March 2006 and 2007. It appeared that no challenge had been made to its use. It was not therefore part of the appeal but, as we shall explain later, Mr Goldberg argues that the existence of this loss was a distinguishing feature of the facts of the appeals of the 1st, 3rd, 4th and 5th from the facts in *Prizedome*.

(B) The Greathey loss

33. This was realised at step (A)(2) when Greathey was the principal company of the Greathey group. Greathey became part of the PH group at step (A)(3), and PH was taken over by PAL at step (A)(5). The losses were sought to be set against gains arising after step (A)(5) on assets held by the PH group companies before step (A)(5).

34. On Mr Goldberg's analysis there are three groups: the Greathey group, the PH group, and the PAL group. By virtue of section 170(10) they are to be treated as the same. Thus the PAL group is the only relevant group. (Alternatively by virtue of paragraph 9(2) the PAL group is the only group to which the Schedule applies because it is the group of which the company most recently became the member. There were no groups falling within subparagraphs (c) to (e) of paragraph 9(2) so that the only group to which Schedule 7A applied was the PAL group.)

35. The natural meaning of section 170(10) required Greathey to be treated as joining that group at the time of the takeover. That was confirmed by paragraph 1(6). Thus the entry date of the Greathey companies into the PAL group was at the time of the PAL takeover, at step (A)(5). Paragraph 7(1)(a) permitted pre-entry losses to be set against a gain:

(1) on a disposal before the entry date or

(2) on the disposal of an asset held immediately before the entry date.

36. The assets disposed of were not held by Greathey itself at the time of step (A)(5), but the effect of paragraph 7(3) was to treat the assets held by other members of the PH group as held by Greathey before it became a member of the PAL group, and the deeming of section 171A treated the gain as rising in Greathey. Thus the loss could be set against the gains.

(C) The 2004 loss companies.

37. These were acquired by the PH group at step (A)(4). PH was taken over by PAL at step (A)(5).

38. There were two potentially relevant groups: the PH group and PAL group. On the PAL takeover they fell to be treated as the same group. The losses accrued before the 2004 loss companies joined either group.

39. The only relevant group was the PAL group either because that was to be treated as the same as the PH group (or because the effect of paragraph 9(2) in this case was that the only relevant group by reference to which Schedule applies was the one of the which the company most recently became a member. Neither paragraph 9(6) nor any of the other subparagraphs of paragraph 9(2) applied). Thus PAL was the only group by reference to which the Schedule was to be applied.

40. The loss companies joined the PAL group at step (A)(5), the time of the takeover. That conclusion was permitted by section 170(10) and confirmed by paragraph 1(6). The entry date was thus the time of step (A)(5). Thus, as with the Greathey loss, the losses of these companies could be set against the assets held by members of the PH group at the time of step (A)(5).

(D) The Helliconia losses.

41. The legislation applied in the same was as it did for the 2004 loss companies.

(E) The basis of this analysis

42. These analyses were dependent upon the following propositions.

(1) "relevant group" is not, before the application of paragraph 9, limited to any one group of which the company has been a member, and in particular is not limited to the first group by reference to which the loss was a pre-entry loss;

(2) Paragraph 1(6) has the effect that on a takeover the entry date is the date of joining the Acquiring group; and

(3) Either the only relevant group is the most recent acquiring group by virtue of section 170(10) or paragraph 9(2)(a) has the effect of making the relevant group that which is most recent to the disposal giving rise to the gain, or the accounting period in which the gain arose.

Prizedome

43. Before turning to Mr Nawbatt's submissions we should discuss the judgements in *Prizedome*.

44. In *Prizedome* P and L had realised capital losses. They were acquired by GL; GL was then taken over by GH. Gains were made on the disposal of assets which had been held by other GL group companies prior to the GH takeover. The assets were disposed of by those companies after the takeover. The gains were treated under section 171A elections as gains made by P and L; P and L then sought to offset their capital losses against those gains. The argument for the companies was that the entry date into the GH group was the date of the GH takeover, that para 7(3) permitted the assets to be treated as held by L and P at the date they joined the GH group, and accordingly that the losses could be set under para 7(1) against the gains on the assets.

45. The Special Commissioners said:

> "[41] The deductibility of the losses from the gains depends on the date or dates on which the appellants became members of the "the relevant group" within Sch 7A in relation to each gain. This depends upon the identification of "the relevant group" which in turn depends upon the applicability or otherwise of para 1(6)(b) and para 9(2)(a)."

They said that if "the relevant group" in para 1(6) referred to the "second" group, i.e. the GH group, then paragraph 1(6) would not have any effect and the losses would be pre-entry to the "relevant group" and not usable against the gains because the assets would not have been (treated as) held by L and P immediately before they entered the relevant group; if by contrast it referred to the GH group combined with the GL group, then paragraph 1(6) would apply and the assets disposed of by GL group companies would be treated as held by P and L before they entered the GH group so that the losses could be offset against those gains.

46. Dr Avery Jones, whose dissenting view was later endorsed by the Court of Appeal, regarded section 170(10) as treating the GL group and the GH group as a single group but paragraph 1(6)(b) as referring to the separate components of that group so that since the loss was realised before P and L became members of the GL group (the first group), that group was the relevant group and the GH group (the second group) was not the relevant group with the effect that the condition in paragraph 1(6)(b) was not satisfied, and the time of entry of P and L to the relevant group was not the time of the GH takeover but the time they entered the GL group.

47. In the High Court, Blackburne J said [25] that the resolution of the question turned, as the parties accepted, on the true meaning of paragraph 1(6): whether or not it applied to treat P and L as joining the GH group at the time of the GH takeover. HMRC argued that the identity of "the relevant group" to which the Schedule referred depended on the loss identified as pre-entry in respect of which the Schedule had effect [36].

48. The appellant had argued [48] that there was no need to consider paragraph 9 in that appeal since the GH group was the only contender for "the relevant group", and even if paragraph 9 were relevant, subparagraph 9(2)(a) would identify the GH group as the relevant group. It was wrong, it said, to link the identity of the relevant group to a particular pre-entry loss.

49. Blackburne J identified the object of the Schedule, being to restrict the use of losses, as being achieved [55] by limiting the use of losses to reduce chargeable gains of any members of a group which the company had joined. He said that:

> "[56] ... the legislation takes care to ensure that a relevant group, once identified as such, does not cease to be the relevant group merely because (a) other companies may join or leave it or (b) the group is acquired by another group. That requires two things: (a) a clear definition of what is meant by 'a group of companies', a matter dealt with by section 170(3) to (6); and (b) a mechanism to ensure that the scope of the restriction against deductibility is not undermined by alterations in the make up of the relevant group. This is achieved by section 170(10) providing (a) that the 'group remains the same group so long as the same company remains the principal company of the group' and (b) that 'if at any time the principal company of the group becomes a member of another group, the first group and the other group shall be regarded as the same'. The subsection then states 'and the question whether or not a company has ceased to be a member of a group shall be determined accordingly'. The effect of this provision, so far as it is made to apply to Schedule 7A (as by s177A it is), is therefore to ensure that once the loss has been identified as pre-entry in respect of a group of companies identified as 'the relevant group' it remains a pre-entry loss in respect of that group, notwithstanding changes in the composition of the group or the takeover of the group by another group."

50. We note that the reasoning in this paragraph proceeds in part on the basis that if a loss had been identified as pre entry to a particular group it would, absent the effect of section 170(10) cease to be pre entry in relation to any group if the make up of the group changed on a takeover. On Mr Goldberg's approach to the Schedule if there was ever a group by reference to which a loss was pre entry it would for ever thereafter be a pre entry loss (subject to the application of paragraph 9) no matter what changes there were to the composition of the group, so that section 170(10) is not needed to preserve the operation of the Schedule.

51. Blackburne J continued:

> "[57] Unless modified, however, s170(10) would operate to enable losses realised by a company in one group ("the first group") to be set against gains realised by members of another group ("the second group") where the second group has later taken over the first group. This is because the members of the first group would, by force of s170(10), be treated as having joined the merged group not at the time of the merger but at the time that they each became members of the first group. The losses in question would not therefore be pre-entry in relation to the merged group with the result that, as regards those losses,

the merged group would not qualify as "the relevant group" and the losses would not be subject to any restrictions against deductibility."

52. Again we note that on Mr Goldberg's approach section 170(10) would not have the effect which Blackburne J contemplates because the members of the first group would not be treated by that section as having joined the merged group at the time they became members of the first group. Blackburne J continued:

> "[58] It is to avoid this consequence that, in my judgement, para 1(6) was enacted. For the effect of the paragraph, where it applies, is to treat the members of the first group as having joined the merged group at a time of the merger "and not by virtue of that subsection [i.e. section 170(10)] at the time when they became members of the first group." The consequence of so doing is to treat the losses of members of the first group as pre-entry to the merged group and thus to subject them to the operation of the Schedule, i.e. as subject to restrictions on deductibility set out in paras 6 and 7.
>
> ...
>
> "[61] Paragraph 1(6) requires two separate conditions to be fulfilled if it is to apply and the operation of section 170(10) is to be modified. The first, set out in subparagraph (a), is that there has at some time been a takeover of the first group by the second group so that the two groups are treated as the same by virtue of s170 (10). The second, set out in subparagraph (b), is that "the second group, together in pursuance of section 170 (10) with the first group, is the relevant group." The assumption underlying both subparagraphs is that s170 (10) operates so that the two groups are, in the words of that subsection, "regarded as the same". Subparagraph (b) is intended in my view, to add something to subparagraph (a): it is not enough that one group has been acquired by another in the circumstances set out in subparagraph (a). The addition, required by subparagraph (b), is that "the second group, together in pursuance of that subsection [s170(10)] with the first group, is the relevant group". But the relevant group in relation to what?

53. Mr Goldberg points to the assumption here and in para [63] that subparagraph (b) would not otherwise add anything to subparagraph (a). We discuss that later.

54. Blackburne J continued:

> "[62] It is to be noted that the condition to be fulfilled by subparagraph (b) is that it is "the second group" that is to be the relevant group. It is not that the first group is to be that group. In adding the words "together in pursuance of that subsection with the first group" the draftsman is doing no more, in my view, than acknowledging - in line with the assumption that underlies the paragraph - that as a consequence of the operation of section 170(10) the first group and the second group are, following the takeover of the former by the latter, the same group. The effect of the paragraph is to negate the operation of that subsection so that, as regards the particular losses which are in point, the members of the first group are to be treated as having joined the relevant group at the time of the merger and not before.

"[63] What then are the losses to which the paragraph is directed? In my judgement they are the losses which are pre-entry in relation to the second group; they are not the losses which are pre-entry in relation to the first group. I reach that conclusion because, if it were the latter, there would be no need to disapply the operation of section 170(10); paragraph 1(6) would add nothing to the scheme of the Schedule. It is precisely because, as regards losses which have accrued to members of the group while members of that group, there is a need, if the aim of the Schedule - to subject pre-entry losses to restrictions on set off - is to be achieved, to disapply section 170(10) that, in my judgement, paragraph 1(6) was enacted. So regarded, it operates to put losses accruing to companies in a group which is subsequently taken over by another group on the same footing as losses accruing to a single company which is subsequently taken over by a group. That being, as I see it, the purpose of the provision, I see no reason, unless compelled by the words to do so, to construe it as having an effect which goes beyond that purpose. I consider that purpose can be achieved - and the surprising results avoided which I have described paragraph 60 above – by construing the reference to "the relevant group" and subparagraph (b) as confined to losses of the acquired (the first) group which are not pre-entry losses in relation to that group immediately before its acquisition by the acquiring (second) group."

55. We note the assumption in this reasoning that because section 170(10) treats the two groups as the same they cannot later be regarded as having been separate at earlier times.

56. In the Court of Appeal the same approach was adopted. Paragraph [63] of the judgement in the High Court was expressly approved. The argument was fought over the provisions of paragraph 1(6):

> "[4]… the particular point in this case arises where a company joins a group of companies (the first group) which is later taken over by another group (the second group). It then becomes necessary to determine which is "the relevant group" in relation to the pre-entry losses. It is common ground that the appellants are entitled to set off the losses against the gains to the extent claimed in this case if, but only if, para 1(6) of Sch 7A applies to the facts of this case. The construction of para 1(6) is at the heart of the dispute.

57. This passage shows that the Court of Appeal appeared to regard paragraph 1 as requiring the identification of a single group to be "the relevant group" in relation to any loss. Mr Goldberg says that this usurps the function of paragraph 9. Although the function of paragraph 9 was mentioned no part of the Court's conclusions depended upon its terms although the appellant is recorded as having argued that the proper approach was:

> "[25] ... first to identify every group of which the loss-making company is, or has been a member. Then you apply the rules in paragraph 9 Schedule 7A to identify "the relevant group" and ask when the loss-making company became a member of "the relevant group". If the relevant group is a merged group, you change the normal time of entry to the time of the merger. Having identified the

relevant group and the time of entry you can then identify whether under paragraph 1(2), the losses are pre-entry loss in relation to the relevant group."

58. In the Court of Appeal, Mummery LJ agreed with Blackburn J, and accepted the following summary of HMRC's submission as correctly stating the law:

> "[29] The company starts off on the basis that it has realised a loss. By reference to the loss it can identify the relevant group and when the company becomes a member of the group by reference to which it is a pre-entry loss. In a case to which section 170(10) applies this will identify a single group as the relevant group, notwithstanding the merger. From the perspective of a company within the GL group before the merger with the GH group the relevant group will be the GL group. From that perspective the loss-making companies have already identified the pre-entry losses by reference to the date of entry into the GL group.
>
> "[30] Against that background ... paragraph 1(6) is a provision in which the draftsman deconstructed in condition (a) the merged group into its constituent elements of "the first group" and "the second group". Then in condition (b) the draftsman treated the second group as "the relevant group" in order to see whether any of the companies' losses can be identified as pre-entry losses from the perspective of their membership of the second group. The perspective is reversed from the first group to the second group for the purpose of identifying the losses of the first group companies which have not previously been identified as pre-entry losses under paragraph 1(2)(a). They will be losses in respect of which the second group is the relevant group. But the second group is not the relevant group for *all* the purposes of Schedule 7A. It is for the more limited and precise purpose of seeing whether any losses of the companies in question are pre-entry losses, which have not already been identified as pre-entry losses of the relevant group.
>
> "[31] Thus, the purpose and effect of condition (b) was to identify and bring within the scope of Schedule 7A losses of the first group of companies that have not previously been identified as pre-entry losses, as defined in paragraph 1(2)(a) of Schedule 7A. In respect of those losses, but only those losses, the second group is "the relevant group".

59. Mr Goldberg made a number of criticisms of this reasoning:

(1) he says that paragraph 1 permits any group of which a company has been a member to be a relevant group. The paragraph does not identify a single relevant group by reference to any pre-entry loss. Even HMRC in this appeal accepted that there could be situations in which there was more than one relevant group. Any restriction on the operation is the province of paragraph 9 only, and that paragraph, which is critical to the operation of the Schedule was not properly considered in the Courts' reasoning. There was in particular no consideration therein of paragraph 9(6) which appeared to conflict with the Courts' conclusions;

(2) the reasoning assumes that section 170(10) has the effect of treating the entry date of the Target group companies to the Acquiring group as being the date on

which the companies joined the Target group. That was not its effect, and the contrary did not seem to have been argued;

(3) the reasoning is (as suspected by Dr Avery Jones) circular: paragraph 1(6) can apply only to a relevant group; on the Court of Appeal's reasoning a group is a relevant group only if there is a loss which is pre entry in relation to it; to know if a loss is pre entry to a group you need to know when the company with the loss joined the group; but in order to determine that you need to apply paragraph1(6)!

(4) it assumes (see Blackburne J quoted at [63] above) that unless in paragraph 1(6)(b), the "second group" means "the group in relation to a loss by reference to which the second group is the relevant group", the condition in (b) has no meaning. That was wrong.

60. In relation to the first three of these criticisms we are unable to say that the relevant provisions were not before the Courts. Paragraph 9(6) was one of the few provisions cited by Mummery LJ; whilst it is true that no argument appears to have been addressed to the effect of section 170(10), it was plainly in view and plainly considered; and the circularity concern was alluded to by Dr Avery Jones. It seems to us that we cannot say on this basis that the judgements were per incuriam

61. We should say a little more about the last of these criticisms. Mr Goldberg says (b) was there to deal with a situation in which a member of the Target group could cease to be a member of such a group by virtue of a takeover. This situation arises because of the requirement in section 170 that no company can be a member of the group unless it is an effective 51% subsidiary of the principal company of the group. A group is defined to be a principal company, its 75% subsidiaries, the 75% subsidiaries of those subsidiaries and so on (section 170(3)(a)), but not any company which (by virtue for example of the attenuation of ownership in serial 75% holdings) is not an effective 51% subsidiary of the principal company (section 170(3)(b)).

62. If Target holds 75% of T1, which holds 75% of T2, which in turn holds 75% of T3, then the group will be formed of T, T1, and T2, but not T3 (which would only be effectively 42% owned by T, leaving aside other complexities). If A then acquired 75% of T, then the group would be A, T and T1; and T2 would by virtue of the takeover cease to be a member of the T group (and not join the A group). Section 179(5) specifically addresses this situation providing for a deferral of the group exit charge which would otherwise occur where, by virtue of the takeover, T2 left the group.

63. This is the situation which Mr Goldberg says (b) is intended to address. Its object is to ensure that whilst T and T1 are treated as joining the A group at the time of the takeover - because for them the second (A) group together with the first group (T) is the relevant group - T2 will not be so treated because, for it, A is not a relevant group because it is never a member of it. Thus T2 will not satisfy (b).

64. But it seems to us that this relies upon treating the tailpiece of paragraph 1(6) as having the effect, not simply of determining the time at which a company became a member of the group, but also as prescribing that it became a member of the group of which it would not otherwise be treated as having been a member. If all the operative

provision does is to determine the entry date into the A group then, since T2 never becomes a member of the A group, the tailpiece can never have any effect in relation to its entry date into that group: in other words if the tailpiece is limited in its effect to timing there is no need for the exception for T2 identified by Mr Goldberg. But to our minds the tailpiece is concerned only with timing: the words "and not ... at the times they become members of the first group" make that clear. Thus even though (b) might theoretically encompass the condition which would exclude T2 from the operation of the paragraph, that would serve no practical purpose. Thus (b) would remain otiose. Accordingly it does not seem to us that this is the proper way of giving meaning to paragraph 1(6)(b).

Mr Nawbatt's arguments.

65. Mr Nawbatt says:

(1) schedule 7A operates loss by loss;

(2) in relation to any particular loss its purpose is to limit and identify the gains against which it may be deducted;

(3) in relation to any particular loss paragraph 1 requires the identification of any group to which it is pre-entry. The identity of the relevant group depends upon the loss;

(4) if there is more than one such group paragraph 9 may limit the application of the schedule to only one or to some only of those groups;

(5) but in these appeals there was only one relevant group. That was because of the effect of section 170(10). Therefore paragraph 9 had no direct effect on the outcome;

(6) section 170(10) had the effect that when Acquiring group took over Target group, the companies in the target group did not leave that group (for section 179 reasons); and if they did not leave the target group they could not be said to have joined the Acquiring group;

(7) that section 170(10) had this effect was confirmed rather than denied by paragraph 1(6) – see in particular the words " and not by reason of [section 170(10)] at the times they became members of the first group";

(8) the only qualifications to section 170(10) were paragraph 1(6) and paragraph 9(6);

(9) paragraph 9(6) was not applicable because paragraph 9 dealt only with the situations in which there was more than one relevant group or because it was not applicable on the facts of this case;

(10) paragraph 1(6) affected only the time of entry into a group;

(11) as Blackburne J and the Court of Appeal had held sub paragraph 1(6)(b) applied to identify the Acquiring group as the relevant group for the particular purpose of considering whether losses arising in an intervening period – between joining the Target group and the Target group being taken over by the Acquiring

group - were to be identified as pre entry losses. It did not apply for any other purpose;

(12) this construction was plainly consistent with the purpose of the schedule to restrict the use of pre entry losses – the evident purpose of the regime which was not to free up losses on a change of group structure (as Mr Goldberg had suggested);

(13) the issues which arose from paragraph 9 had been debated before the Court of Appeal in *Prizedome*. The reasoning in that case was binding on this tribunal.

66. As a result, on the facts of these appeals Mr Nawbatt says that Schedule 7A applies thus:

(1) The Eleco loss is irrelevant to the analysis. Its use is not the subject of any appeal and its existence does not affect the loss by loss operation of Schedule 7A.

(2) Helliconia's situation is indistinguishable from that of *Prizedome.* Its losses are not usable against the Cronkdean gains

(3) When the 2004 loss companies joined the PH group they had losses. Those losses were pre-entry to the PH group. That, by section 170(10) is the same group as the PAL group. Those losses are therefore pre-entry to the PAL group unless paragraph 1(6) changes the date on which those companies joined that group. On the Court of Appeal's interpretation of paragraph 1(6) does not have any effect in relation to those losses since the losses were already pre-entry to that group. Thus the losses may be set only against gains arising before the entry date to the PH group or on assets held by the 2004 loss companies before their entry into the PH group. That precludes their use against the gains on the PAL group assets against which the Appellants sought to set them.

(4) The Greathey group joined the PH group and then the PAL group. Section 170(10) applies at each takeover. There is therefore only one relevant group, the PAL group. The date the loss making Greathey companies joined that group is therefore the date they joined the Greathey group unless paragraph 1(6) applies. The losses did not arise after Greathey joined the PH group or the PAL group. Therefore paragraph 1(6) does not apply to them. That means that in respect of those losses, the date Greathey joined the PAL group is unaffected and remains the date Greathey joined that group. The assets whose disposal gave rise to the gains against which the Greathey losses were sought to be set were not held by Greathey companies at that time. The losses are therefore not offsetable against gains on their disposal.

Our Analysis

Free from authority we would conclude as follows:

1. Loss by Loss

67. The schedule is to be applied loss by loss to determine how much of that loss is offsetable against gains. Its effect in relation to one loss does not affect its application in relation to another loss. This followed from the operation of paragraph 7.

2. The relevant group.

68. It seems to us that the natural reading of paragraph 1 is that it invites the reader to consider all the groups of which a company is or has been a member and then to apply the rest of the Schedule to each of those groups in relation to any loss made by the company. We agree with Mr Goldberg that paragraphs 9(2)(a) and 9(2)(c) are inconsistent with the idea that as respects any one loss there can only be one potential relevant group. The requirement in paragraph 9(5) in relation to "separate applications of [paragraph 7] in relation to each group" reinforces the point.

69. The use of "the" in "the relevant group" is simply intended to indicate the group under consideration. It need not be the group which identifies a loss as pre-entry.

70. In particular the identification in relation to a company of a relevant group is not dependent upon the identification of a loss. Instead, once a relevant group has been identified, the question posed in paragraph 1(2) by reference to that group is "is the loss a pre-entry one by reference to that group?"

71. Where more than one relevant group has been identified in relation to a particular loss paragraph 9 may limit the relevant groups to which the schedule applies, and the amount of the loss which is deductible against any gain.

72. This approach has the effect that paragraph 1(6) does not introduce the infinite regress in the construction of the Schedule to which the Court of Appeal's reasoning appears to give rise (see Mr Goldberg's third criticism thereof above).

3. Section 170(10)

73. For the reasons which follow, we believe that section 170(10) did not *on its own* have the clear effect of requiring the date on which a company in the Target group entered the Acquiring group to be the date on which it joined the Target group, although such treatment would not be inconsistent with the subsection. In particular the prescription that a company is to be treated as not leaving a group does not mean that it should be treated as not joining another.

74. First, the section is prospective in effect: it does not treat the two groups as the same before the takeover. If the effect of the section had been retrospective so that the Target group company was to be treated as having entered the Acquiring group before the merger, then transfers of assets between the two groups prior to the takeover would retrospectively benefit from the intergroup no gain/no loss provisions of section 173. That seems to us a ridiculous conclusion.

75. Second, Chapter 1 Part VI TCGA (which starts with section 170) as it was before the enactment of Schedule 7A contained no provision which related to when the company entered into a group. It was thus not necessary for section 170(10) to say

anything about that. There were provisions in that chapter, such as sections 178 and 179, which applied when a company left a group, but none which related to the time of entry into a group. Thus section 179 provides that if company A:

> "acquires an asset from another company (company B) at a time when company B is a member of a group, and ...
>
> company A ceases to be a member of that group within ... six years after the time of the acquisition"

then company A is to be regarded as having immediately after its acquisition of the assets sold at market value.

76. This provision requires the identification of "that group"- the one B was a member of when A acquired the asset - and the time when the company A left that group: when it ceased to be a member of "that group". Section 170(10) provides the answer to the first of these questions when there has been a takeover – when, after the takeover, company A leaves the Acquiring group it is treated as if it left "that group" i.e. the one it was a member of at the time it acquired the assets because that is treated as the same group . The closing words of section 170(10) – " and the question whether or not a company has ceased to be a member of a group shall be determined accordingly" - add to this by making clear that section 179 applies when company A later leaves the Acquiring group.

77. Third, section 170 is an interpretation section, not a deeming one. This is not a case where one must follow the logical consequences of a deeming provision until one's mind boggles (*East End Dwellings v Finsbury* [1952] AC 109). Even if it were a deeming provision the deeming is for the purposes of the provision for which it operates (see "if I were your age" per Lord Hope at [40] in *DCC Holdings (UK) Limited* [2010] UKSC 109).

78. But Schedule 7A was inserted in 1993 as part of Chapter 1, relying therefore on the definitions and concepts of that chapter. On its insertion the question of when a company became a member of a group became relevant.

79. It seems clear that the draftsman of Schedule 7A considered that section 170(10) did have some consequence in relation to the question of when a company joined a group. Whilst the draftsman cannot have understood section 170(10) to mean that the Target group and the Acquiring group had always been the same, he or she must have thought that if a company joined Target group before the takeover then, although it was a member of Target and not Acquiring group before the takeover, nevertheless it was to be treated as joining Acquiring group when it joined the Target group. That understanding seems to us evident in the following provisions:

> (1) paragraph 1(6) in its exception for circumstances within 1(7).
>
> It is clear that a different rule is intended for circumstances falling within 1(7) as compared to 1(6). If the draftsman had understood section 170(10) as having no effect on when the company joined the group then the exception of 1(7) circumstances from 1(6) would have been nugatory.

Put another way, if he understood that the general rule was that specified in 1(6) he provided no rule for the circumstances of 1(7): making express a general rule whilst leaving the position undefined for an exception to that rule makes no sense;

(2) the words at the end of 1(6) "and not by virtue of that section at the times when they became members of that group" indicate the understanding of that subsection;

(3) the provisions of paragraph 9(6).

80. Whilst a later inserted provision will generally not affect the meaning of an existing provision in an Act, it seems to us that where the existing provision is able to bear an extended meaning, it may, for the purposes of the inserted provision, be treated as having the meaning ascribed to it by the inserted provision, even if that meaning is not made express in that later provision. We therefore conclude that *for the purposes of Schedule 7A* section 170(10) is to be taken as meaning that the date on which a member of Target group joined Acquiring group is the date on which it entered the Target group.

81. We have explained that prior to the insertion of Schedule 7A section 170(10) did two things: (1) it prevented a takeover occasioning a section 179 charge, and (2) it ensured that when a company left the Acquiring group, it is treated as leaving the group it was in when it acquired the asset to which the exit charge may apply. Both those are forward looking. In the context of Schedule 7A we accept that the effect of the subsection must be to treat the company as joining the Acquiring group when it joined the Target group. But we do not believe that the section requires history to be rewritten: it does not require the Target group to be treated as if before the takeover it had been the Acquiring group. As a result when one asks the question: of what groups "has" a company been a member, one can answer that it "has been" a member of two groups, namely Target group and Acquiring group. In other words both Target and Acquiring groups can, before the application of paragraph 9, be relevant groups to which the Schedule can apply.

82. It does not seem to us that the fact that Target group ceases to exist on the takeover affects this. In the same way if A Ltd was owned and then sold by X Ltd, and X Ltd was later wound up and ceased to exist, that would not prevent the X Ltd group being a relevant group and one to which paragraph 9 could permit the Schedule to apply.

83. Whilst, on this approach to the effect of section 170(10) in Schedule 7A, subparagraph (6) on its own would appear to be a (limited) duplication, that subparagraph appears to apply only for the purposes of paragraph 9 and not the Schedule as a whole, redundancy in tax legislation is not always a sure guide, and the satisfaction of the particular conditions in that subparagraph is necessary for the separate operation of (7) which has a wider effect.

4. Paragraph 1(6).

84. Free from authority we would read paragraph 1(6)(b) as meaning "the second group is the particular (i.e. relevant) group to which the Schedule is being applied at the moment", i.e. as confining the application of the tailpiece to the considerations required by the Schedule in relation to that group rather than giving it more general application, for example so as to treat for all purposes Target's members as joining the Acquiring group on the takeover.

85. This construction follows in particular from the fact that subparagraph (a) is of completely general form: it refers to "a" company becoming a member of "another" group: it thus relates to any takeover whether or not relevant to a company or a loss.

5. Paragraph 9(2)(a) "most recently become a member"

86. We asked Mr Goldberg about this phrase. He submitted that it referred to the group of which the company was most recently a member by reference to the disposal giving rise to the gain against which it was sought to set the loss, or to the accounting period of that disposal.

87. We reached a different conclusion. That was for the following reasons:

(1) paragraph 9 makes no mention of any gain or any disposal; it is concerned with losses;

(2) subparagraph (2) starts by referring to a loss accruing on a disposal, and its opening words indicate that it relates to the application of the Schedule "in relation to any loss accruing on that disposal"; and

(3) the emphasis on the disposal - or the time of the disposal - is continued in subparagraph (2)(b).

88. It thus seems to us that "most recently" refers to the disposal giving rise to the loss: it refers to the first (most recent) possible (relevant) group by reference to which the loss is pre-entry.

89. This approach does not render the other provisions of paragraph 9 nugatory:

(1) the remaining subparagraphs of (2) permit other groups also to be relevant groups;

(2) subparagraph (3) may apply where (2)(c) makes another group also a relevant group;

(3) subparagraphs (4) and (5) apply in particular to the determination of the relevant group in relation to pre-entry assets.

90. We therefore conclude that the single group identified by subparagraph 9(2)(a) is the one most recently after the disposal giving rise to the loss of which the relevant company became a member.

6. The result

91. Free from authority we would therefore reach the following conclusions in a case where a loss company joins Target group which is subsequently taken over by Acquiring group where losses which accrued before entry to the Target group are sought to be set against gains made by Target group companies which did not join the Target group with the loss company:

(1) "relevant group" means any group of which the loss-making company is or at any time has been a member;

(2) once a relevant group has been identified in relation to which a loss accrued before the entry date that loss is for purposes of the Schedule a pre-entry loss;

(3) for the purposes of the Schedule, absent the effect of paragraph 1(6), section 170(10) is to be treated as having the effect that the date on which a company is to be treated as joining Acquiring group is the date it joined Target group, but does not treat the two groups as having always been indistinguishable;

(4) as a result it is possible to say that a company "has been" a member of Target group and that it is or has been a member of Acquiring group, and thus to treat both Target and Acquiring group as relevant groups even though after the takeover they are the same;

(5) the effect of paragraph 1(6) is that, in considering the date on which the loss company joined Acquiring group (i.e. when considering Acquiring group as the relevant group), a Target subsidiary is to be treated as joining the group on the day of the takeover. Thus when applying the Schedule to Acquiring group the relevant group loss company would be considered as joining Acquiring group at the time of the takeover. But it has no application to the date on which the company joined the Target group: the condition in (a) is not satisfied when considering Target group as the relevant group;

(6) paragraph 9(2)(a) limits the application of the Schedule to the group which the loss company joined most recently after the loss. That is Target group. Thus in relation to that loss the Schedule is not to be applied to Acquiring group.

(7) paragraph 1(6) has effect only when one is considering the Acquiring group as the relevant group, and such consideration has been ruled out by paragraph 9(2)(a).

(8) as a result paragraph 7 has effect only in relation to the Target group. The losses may be set against gains only if the related assets were held by companies in the Target group which were part of the loss making company's group before it joined the Target group.

92. The Court of Appeal regarded paragraph 1(6) as being limited in its effect to losses which were not pre-entry to the Target group. Our conclusion is that, because of paragraph 9(2)(a), paragraph 1(6) is not called upon by the Schedule to have effect other than in relation to such losses.

93. In relation to such intermediate losses - losses incurred by a Target group company after entry into Target group and before the takeover by Acquiring group:

(1) Target and Acquiring groups are both relevant groups;

(2) in relation to Acquiring group only, paragraph 1(6) has the effect of changing the entry date of the loss making companies into the Acquiring group to the date of the takeover;

(3) having identified the Acquiring group as a relevant group in relation to which (by virtue of paragraph 1(6)) the losses are pre-entry, that group falls within paragraph 9(2)(a) so that Schedule 7A applies to Acquiring group and that loss – since it is the most recent group;

(4) but paragraph 9(2)(c) permits Target group also to be a relevant group (because the takeover would have been in an accounting period in which the company would have been a member of Target group) to which the Schedule applies;

(5) thus Target and Acquiring groups are connected groups;

(6) at this stage paragraph 9(4)(b) has effect and, since the loss is a pre-entry loss by reference to paragraph 1(2)(a) and the Acquiring group, the loss is treated as pre-entry for the purposes of paragraph 6;

(7) thus the restrictions in paragraph 7 will apply to its use;

(8) that has the result that the losses are usable only against gains arising, and on gains on assets held by Target group companies, before the takeover (or "trade" assets).

94. During the course of the hearing Mr Goldberg considered the example of a singleton company which had incurred a loss, and which was then acquired in different accounting periods: first by group A, then by a consortium, and then by group B. He said that if the company acquired an asset whilst owned by group A the loss would not be offsetable against a gain on that asset whilst the company was owned by group A, nor whilst owned by the consortium, but when it joins the B group the loss would be offsetable since the B group is the group of which the company had most recently become a member and the loss and the asset were both pre-entry to that group. He said that this was not affected by the *Prizedome* judgment since that related to 1(6) which was not relevant in the case of a singleton company. He then asks why a greater restriction should apply if the loss company were a group.

95. It seems to us that if we are right about the meaning of paragraph 9(2)(a), then in his example the only relevant group in relation to the loss company to which the Schedule could be applied in relation to the loss would be group A. If that is right then the loss could not be set against a gain on an asset acquired after joining A unless it was a trading asset acquired from a third party (paragraph 7(1)(c)). The asset acquired from group A could not be such an asset, thus the loss could never be offset against the gain on its disposal whether realised when a member of group A or group B. That

was the same result as that which would apply if the loss company (X Ltd) were the principal company of a group[1]. This seemed to support our approach.

96. Our analysis in [91] above covers the Heliconia losses and the 2004 loss companies. In relation to the Greathey loss there are, on our analysis, three potentially relevant groups (groups which, although later treated for some purposes as the same, had been groups of which Greathey had been a member): Greathey, PH and PAL. The loss arose before Greathey was taken over by the PH group. Paragraph 1(6) potentially has effect in relation to the PH group and the PAL group; it is not relevant to date of entry of Greathey into the Greathey group since there was no relevant takeover by it. In considering the PH group in relation to Greathey's loss that paragraph treats Greathey as joining it at the date of the takeover: that makes the loss pre-entry to the PH group. In relation to the PAL group the paragraph similarly applies to make the date Greathey joined that group the date of the PAL takeover, thus losses are similarly made pre-entry. At this stage in relation to the Greathey loss there are three relevant groups in relation to each of which Greathey has different entry dates. But paragraph 9(2)(a) applies to permit the only group to which the Schedule may apply to be the PH grou. By reference to that group the date of entry in respect of that loss is the date of the PH takeover. The later entry into the PAL group becomes irrelevant. Although paragraph 9(2)(c) permits the schedule to apply to the Greathey group (since Greathey was a member of it in the accounting period of the takeover by PH), by paragraph 9(4)(b) the loss is to be treated as pre-entry for the purposes of paragraph 6 since it it is pre-entry to the PH group within paragraph 9(2)(a). Thus paragraph 6 applies and the effect of paragraph 7 is that since the gains made in 2005, 2006 and 2008 were not made before the date of entry into the PH group nor were the assets which were disposed of held before that date by Greathey group companies), the paragraph does not permit the Greathey losses to be set against them.

97. On this basis we would dismiss the appeals.

The applicability of the *Prizedome* reasoning

98. We are constrained by authority. We have discussed Mr Goldberg's criticisms of the *Prizedome* judgments and concluded that we could not say that they were per incuriam.

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1. [1] Because, on our analysis, (i) the relevant groups are the X group, the A group and the B group but so that *after* the takeovers the X group is treated as the same as the A group and the B group; (ii) in relation to the A group – i.e. when considering it as the relevant group – paragraph 1(6) treats X as joining it on the A takeover; (iii) para 9(2)(a) permits the application of Sch7A by reference to the A group – the group by reference to which the loss is most recently pre-entry, but not the B group; (iv) paragraph 9(2)(c) permits the application of the schedule to the X group, (iv) but by para 9(4)(b) the loss is to be treated as pre-entry for paragraph 6 purposes because it is pre-entry to the A group (iv) thus the restrictions in paragraph 6 apply and because of the limitations on use in paragraph 7, the losses are usable only against assets held by X group companies at the time of entry (or "trading assets") .

99. It seems clear that the High Court's and the Court of Appeal's conclusions were dependant on the following reasoning:

(1) The particular loss identifies whether or not a group is a relevant group.

This finding by Blackburne J was the subject of specific criticism by the Appellant in the Court of Appeal. It seems to us that Balckburne J was expressly upheld.

(2) Because section 170(10) treats Target and Acquiring group as the same, there is only one relevant group to be considered, that is Acquiring group;

(3) Section 170(10) means that the date a Target group company joins Acquiring group is the date on which it joined Target group.

(4) Paragraph 1(6):

(i) requires the identification of a loss which in turn determines the relevant group

(ii) does not apply if Target group is the relevant group because that would defeat the object of the provisions or because the draftsman's language deconstructs the merged group in to its constituent parts so the target group does not fall within (b); and

(iii) applies only to a loss which is pre-entry to the Acquiring group but not pre-entry to Target group

it thus applies only to losses incurred by companies in what was Target group after they had become a member of that group. In relation to those losses it treats the date of entry into the Acquiring group as the date of the takeover.

100. Mr Goldberg says that we are not bound by the reasoning in *Prizedome* because in the case of the 2004 loss companies and Greathey the facts are different*;* in these appeals there is the Eleco loss - there was no equivalent in *Prizedome* - he says that its existence affects the reasoning.

101. Mr Goldberg seeks to apply *Prizedome* in the following way. He says that *Prizedome* decides that, where a group has a loss which is not pre-entry to that group, and Target group is then taken over by Acquiring group (so that 170(10) applies to require the two groups to be regarded as the same), then paragraph 1(6) does apply to change the entry date into the Acquiring group. And paragraph 1(6) apples for all purposes not limited ones. That he says is the case in relation to the Eleco loss. That loss arose to PH when it was the principal company of the PH group: therefore it was not a pre-entry loss to the PH group. Thus on the Court of Appeal's reasoning paragraph 1(6) applies and so all the members of the PH group are treated as becoming members of the PAL group at the time of the PAL takeover. Thus the 2004 loss companies are also treated as becoming members of the PAL group at that time together with the PH group companies. As a result gains made by the PH group companies before the PAL takeover may be offset by those losses.

102. We do not think that this reflects the reasoning of the Court of Appeal. It did not treat the existence of the loss incurred within a target group prior to its takeover as switching on paragraph 1(6) for all purposes. That is most clearly seen at [31] of Mummery LJ's judgement:

> "Thus the purpose and effect of condition (b) was to identify and bring within the scope of Schedule 7A losses of the first group that have not previously been identified as pre-entry losses ... In respect of those losses *but only those losses*, the second group is "the relevant group"". [Our italics]

103. In the same way the approved passage quoted from Blackburne J's judgement begins "What then are the losses to which [paragraph 9(6)] is directed…"

104. Thus the Court of Appeal saw paragraph 1(6) as requiring losses to be divided into those which were pre-entry to Target group and those which were not; and as applying only to those *losses* which were not. Rather than applying group by group, or loss company by loss company, they regarded the paragraphs as applying loss by loss and only to particular losses. That was an essential part of its reasoning for holding that subparagraph (b) was not satisfied in the case of the G and L losses.

105. Thus the fact that the Eleco loss existed and was not pre-entry to the PH (Target) group would not switch on paragraph 1(6) in respect of any other losses - and in particular would not switch it on in respect of the 2004 company losses.

106. Mr Goldberg also says that capital gains taxation is not an annual tax: *Taylor v MEPC* Holdings [2004] STC 123. If a company enters a group owning an asset it will be essential to know when it entered the group. If paragraph 1(6) is not of general application then the time of entry – which could be affected by paragraph 1(6) would not be known until the sale of the asset because it would depend on whether the sale was at a profit or a loss. It can hardly have been intended that the time of entry into a group would depend upon whether an asset was realised at a loss or a gain.

107. It seems to us that this is the result of the *Prrizedome* reasoning – but only as regards that particular loss. The reasoning requires each loss to be put through the mincing machine of Schedule 7A separately, and, while it is in that machine for paragraph 1(6) to be applied, so that if the asset is disposed of in the intervening period between its joining one group and its being taken over by another, the asset owning company is taken as joining the relevant group when Acquiring group acquires Target. But the internal mechanism of that machine operates specifically on that loss after it has arisen by reference to when it arises.

108. Mr Goldberg also puts his case this way. He says that in *Prizedome* it was common ground that the appellants (L and P) could succeed only if they could rely on paragraph 1(6). That is not the position in this appeal, since here he submits that the Appellants may rely on the general proposition that they entered the Acquiring group at the time they actually joined it – the time of the takeover – because paragraph 1(6) does not change the time of entry but confirms it.

109. We have set out below our conclusions in relation to paragraph 170(10). But it seems to us that the conclusion that, absent paragraph 1(6), section 170(10) had the effect of treating a company as joining the Acquiring group when it joined the Target group was a necessary part of the Courts' reasoning in *Prizedome* and is binding on us. We accept that the question does not appear to have been expressly argued in that appeal. But that it was a basis for the Court of Appeal's reasoning is clear where at [21] Mummery LJ says: "Further the date of entry of L and P into the GL group was not changed by the GL group becoming a member of the GH group. As explained in the second step the pre entry losses of L and P were in relation to the GL group and are identified as losses incurred before the date of entry into the GL group. That remains the case after the GL group was taken over by the GH group, unless altered by the deeming provisions of paragraph 1(6)". The same point is made by Blackburne J at [57].

110. As a result we remain of the view that we should apply the *Prizedome* reasoning. We now apply that reasoning.

Applying the *Prizedome* reasoning

The 2004 loss companies

111. These joined the PH group in March 2004. In August 2004 PAL took over PH.

112. The losses were, prior to that takeover, pre-entry to the PH group.

113. In relation to the losses of each company, the only relevant group is the PAL group. Absent paragraph 1(6) each company joined that group on the day it joined the PH group. Paragraph 1(6) does not change this entry date since it applies only to losses which have not already been identified as pre-entry losses by reference to the group taken over. Thus by paragraphs 6 and 7 those losses may be used only against gains arising, or on assets held by the loss companies before the date they entered the PH group. The gains did not so arise and the losses may not be used against them.

The Greathey loss.

114. The Greathey loss accrued when the Greathey group was a separate group. It then became subsumed into the PH group which in turn was taken over by the PAL group.

115. Mr Goldberg says that the Greathey loss can only have been a pre-entry loss if Greathey is taken to have joined the PH group at the time of the PH takeover. Thus he says it is pre-entry only if paragraph 1 (6) applied.

116. On the approach of the Court of Appeal, the Greathey, PH and PAL groups are to be regarded as one. In relation to the Greathey loss: (i) the only relevant group is the PAL group; (ii) Greathey joined that group when Greathey became the principal company of its own group; (iii) when Greathey joined the PH group paragraph 1(6) applied to treat it as joining that group at the time of that takeover; (iv) when PH joined the PAL group the Greathey loss had already been identified as pre-entry to the

PH group, therefore paragraph 1(6) did not apply; (v) thus Greathey remains treated as joining the PAL group at the time of its takeover by PH ; (vi) as a result those losses cannot, under paragraph 7 be set against gains made by PH group companies after that time because those assets were not held by Greathey group companies at the time of the PH acquisition of Greathey .

117. For the reasons we have given in relation to the Eleco loss it does not seem to us that the existence of that loss affects the application of paragraph 1(6).

The Heleconia losses

118. The appeals in relation to the Heliconia losses fail for the same reasons.

Result

119. We conclude that Schedule 7A applies to prohibit the offset of: (i) the Greathey loss and the 2004 company losses against the PAL group gains, and (ii) the Heliconia losses against the Cronkdean gains.

120. We dismiss the appeals.

Rights of Appeal

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

CHARLES HELLIER
TRIBUNAL JUDGE

RELEASE DATE: 28 August 2013