[2016] UKFTT 492 (TC)

TC05242

Appeal number:TC/2011/08164

INCOME TAX – capital allowances – ss286-296 Capital Allowances Act 2001 – purchase of building sold unused by a developer – developer holding headlease – sale completed by means of a long sub-lease and not an assignment of headlease – whether sale of relevant interest – appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

DAVID WELLSTEAD **Appellant**

- and -

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

TRIBUNAL: JUDGE JONATHAN CANNAN
MR ROLAND PRESHO

Sitting in public in Manchester on 8 February 2016

Mr Rory Mullan of counsel for the Appellant

Mr Simon Bracegirdle of HM Revenue & Customs for the Respondents

DECISION

Background

1. In 2001 Hillford Construction Limited ("HCL") purchased a long lease of land at New York Industrial Park, North Tyneside ("the Land"). It developed two industrial units on the Land. In 2004 HCL granted an underlease of one of the units to Mr Wellstead, the Appellant, who was a director of HCL. The underlease was for the same term as HCL's long lease less 5 days. Mr Wellstead paid a premium of £1m for the underlease and expected to be entitled to claim industrial buildings allowances ("IBAs") on the purchase price.

2. The Respondents have refused Mr Wellstead's claim to IBAs on the basis that the relevant statutory provisions only permit IBAs to be claimed where the purchaser purchases the same interest as was held by the developer at the time the buildings were built. In other words Mr Wellstead would only be entitled to claim IBAs if he had taken an assignment of the lease. The Respondents say that he is not entitled to IBAs because he took an underlease.

3. We must determine whether the Respondents' have correctly construed the relevant statutory provisions. Mr Wellstead argues that in all the circumstances he did purchase HCL's interest and is entitled to relief.

4. Mr Rory Mullan was instructed by the Appellant on a pro bono basis arranged by the Revenue Bar Association. We are extremely grateful that he agreed to act on that basis. If the Appellant had been unrepresented it is unlikely that the submissions made on his behalf would have been put forward so cogently and forcefully. We are also grateful to Mr Bracegirdle for the fair and measured way in which he put forward the Respondents' case.

Findings of Fact

5. There was no dispute in relation to the facts. We heard no oral evidence, but we were referred to all relevant documents from which we make the following findings of fact.

6. On 24 August 2001 HCL acquired a 125 year lease of the Land ("the Lease"). It paid a premium of £760,000 plus VAT. On the same date HCL entered into a building agreement with the freehold owner for the construction and development of two industrial units on the Land ("Unit 1" and "Unit 2"). Most of the Land was in a qualifying enterprise zone, with a small part being outside the enterprise zone.

7. At all material times Mr Wellstead was a director of HCL.

8. HCL employed a construction company to develop Unit 1 and Unit 2, incurring construction costs between September 2001 and April 2002. Practical completion of the development took place on 8 April 2002.

9. On 27 February 2004 HCL entered into a sale agreement with Mr Wellstead ("the Sale Agreement") pursuant to which it agreed to sell Unit 2 to Mr Wellstead. The Sale Agreement provided that HCL would either grant an underlease to Mr Wellstead of Unit 2 or assign the Lease to Mr Wellstead, subject to an underlease of Unit 1 if granted. The method of completion of the Sale Agreement effectively depended upon whether HCL had completed a sale by way of underlease of Unit 1 by the time of completion. Whatever the method of completion the consideration payable by Mr Wellstead was to be £1m excluding VAT. A deposit of £39,000 was payable on the date of the Sale Agreement with the balance due on completion.

10. The Sale Agreement provided that HCL would use all reasonable endeavours to obtain consent of the superior landlord to the grant of the underlease or the assignment, as the case may be. HCL also agreed that it had not and would not make any claim for IBAs in respect of expenditure it had incurred on Unit 2 and would provide all reasonable assistance to Mr Wellstead to enable him to claim IBAs.

11. Completion of the Sale Agreement was to take place on a date between 6 April 2004 and 31 May 2004. In the event the Sale Agreement was completed by way of an underlease of Unit 2 to Mr Wellstead dated 24 May 2004 ("the Underlease"). By that date HCL had not managed to sell Unit 1. The Underlease was for a term of 125 years less 5 days from 24 August 2001.

12. HCL subsequently sold Unit 1 to Silverlink NewYork LLP ("Silverlink") of which Mr Wellstead was a member. That sale was completed on 23 November 2005 by way of an assignment of the Lease by HCL to Silverlink, subject to the Underlease.

13. We understand that neither Unit 1 nor Unit 2 had been brought into first use as at the dates they were sold.

14. The Lease reserved a peppercorn rent payable by HCL. Sums were also reserved as further rent in respect of various expenses of the landlord in connection with the Land. HCL gave standard tenant's covenants including covenants to keep buildings in good repair and as to user. There were also standard covenants against assigning or underletting the whole or any part of the premises save with the written consent of the landlord. The Lease also contained various standard covenants by the superior landlord, the freeholder in favour of HCL as the tenant.

15. The Underlease demised Unit 2 together with various rights exercisable in common with the landlord and other tenants and subject to various rights reserved to the landlord and other tenants. It reserved a peppercorn rent together with other sums payable by HCL to the superior landlord which were also reserved as rent. A service charge was also payable to HCL as landlord. Mr Wellstead as tenant gave standard tenant's covenants which broadly replicated HCL's covenants in the Lease. He also covenanted to observe and perform all the tenant's covenants in the Lease. HCL as landlord gave standard landlord's covenants including using reasonable endeavours to procure performance by the superior landlord of its covenants in the Lease.

16. On 26 July 2004 HCL and Mr Wellstead made an election under section 290 Capital Allowances Act 2001 ("CAA 2001"). That election, if effective, would have meant that Mr Wellstead was entitled to IBA's on a large part of the premium he had paid for Unit 2. However both parties now accept that the purported election was not effective because HCL and Mr Wellstead were connected persons.

17. Mr Wellstead claimed capital allowances of £840,880 in his self-assessment return for 2004-05 on the understanding that the election was effective. The sum claimed reflected the fact that only part of Unit 2 was in an enterprise zone and also excluded part of the premium attributable to the land rather than the building. On 18 January 2006 the Respondents opened an enquiry into Mr Wellstead's return. A closure notice was issued on 18 March 2011 in which the Respondents refused Mr Wellstead's claim for IBAs.

18. Mr Wellstead subsequently pursued a claim against his former accountants for professional negligence. In the event however that claim was statute barred. It is right to record that the stress and strain of dealing with the enquiry, the financial implications of that enquiry and the potential professional negligence proceedings has taken its toll on Mr Wellstead's health.

The Statutory Provisions

19. All references are to CAA 2001 save where otherwise stated.

20. Section 271 provides that IBAs will be available in relation to qualifying expenditure incurred on a commercial building or structure in a qualifying enterprise zone.

21. Section 296 applies where expenditure is incurred by a developer on the construction of a building and the "relevant interest" is sold by the developer before the building is first used. It provides that a capital sum paid by the purchaser for the relevant interest is qualifying expenditure for the purpose of IBAs. The qualifying expenditure is to be treated as incurred by the purchaser at the time the capital sum became payable. The terms of section 296 are as follows:

> " ***296 Purchase of building which has been sold unused by developer***
>
> *(1) This section applies if—*
>
> *(a) expenditure is incurred by a developer on the construction of a building, and*
>
> *(b) the relevant interest in the building is sold by the developer in the course of the development trade before the building is first used.*
>
> *(2) If—*
>
> *(a) the sale of the relevant interest by the developer was the only sale of that interest before the building is used, and*

(b) a capital sum is paid by the purchaser for the relevant interest,

the capital sum is qualifying expenditure.

(3) …

(4) The qualifying expenditure is to be treated as incurred by the purchaser when the capital sum referred to in subsection (2)(b) or (3)(b) became payable."

22. Provisions for identifying the "relevant interest" are contained in sections 286-291 which in so far as relevant provide as follows:

" ***286 General rule as to what is the relevant interest***

(1) The relevant interest in relation to any qualifying expenditure is the interest in the building to which the person who incurred the expenditure on the construction of the building was entitled when the expenditure was incurred.

(2) Subsection (1) is subject to the following provisions of this Chapter and to sections 342 (highway undertakings) and 359 (provisions applying on termination of lease).

(3) If—

(a) the person who incurred the expenditure on the construction of the building was entitled to more than one interest in the building when the expenditure was incurred, and

(b) one of those interests was reversionary on all the others,

the reversionary interest is the relevant interest.

287 Interest acquired on completion of construction

For the purposes of determining the relevant interest, a person who—

(a) incurs expenditure on the construction of a building, and

(b) is entitled to an interest in the building on or as a result of the completion of the construction,

is treated as having had that interest when the expenditure was incurred.

288 Effect of creation of subordinate interest

(1) An interest does not cease to be the relevant interest merely because of the creation of a lease or other interest to which that interest is subject.

(2) This is subject to any election under section 290.

289 Merger of leasehold interest

If the relevant interest is a leasehold interest which is extinguished on—

(a) being surrendered, or

(b) the person entitled to the interest acquiring the interest which is reversionary on it,

the interest into which the leasehold interest merges becomes the relevant interest when the leasehold interest is extinguished.

290 Election to treat grant of lease exceeding 50 years as sale

(1) Subsection (2) applies if—

(a) expenditure has been incurred on the construction of a building,

(b) a lease of the building is granted out of the interest which is the relevant interest in relation to the expenditure,

(c) the duration of the lease exceeds 50 years, and

(d) the lessor and the lessee elect for subsection (2) to apply.

(2) This Part applies as if—

(a) the grant of the lease were a sale of the relevant interest by the lessor to the lessee at the time when the lease takes effect,

(b) any capital sum paid by the lessee in consideration for the grant of the lease were the purchase price on the sale, and

(c) the interest out of which the lease was granted had at that time ceased to be, and the interest granted by the lease had at that time become, the relevant interest.

(3) The election has effect in relation to all the expenditure—

(a) in relation to which the interest out of which the lease is granted is the relevant interest, and

(b) which relates to the building (or buildings) that is (or are) the subject of the lease.

291 Supplementary provisions with respect to elections

(1) No election may be made under section 290 by a lessor and lessee who are connected persons unless—

(a) the lessor is a body discharging statutory functions, and

(b) the lessee is a company of which it has control.

(2) No election may be made under section 290 if it appears that the sole or main benefit which may be expected to accrue to the lessor from the grant of the lease and the making of an election is obtaining a balancing allowance.

(3) Whether the duration of a lease exceeds 50 years is to be determined—

(a) in accordance with section 38(1) to (4) and (6) of ICTA, and

(b) without regard to section 359(3) (new lease granted as a result of the exercise of an option treated as continuation of old lease).

(4) An election under section 290 must be made by notice to the Inland Revenue within 2 years after the date on which the lease takes effect.

(5) All such adjustments, by discharge or repayment of tax or otherwise, are to be made as are necessary to give effect to the election."

23. To summarise the effect of these provisions, where a developer sells the relevant interest before first use the purchaser is entitled to IBAs on the purchase price. The relevant interest is the interest in the building to which the developer was entitled when the expenditure was incurred. There are provisions for identifying the relevant interest where subordinate interests are created and where leasehold interests are surrendered or merge with reversionary interests. Similarly, where a long lease is granted out of a relevant interest and the parties elect under section 290, IBAs are available to the purchaser as if the grant of the long lease were a sale of the relevant interest. However no election may be made under section 290 where the parties are connected persons.

Reasons and Decision

24. The issue on this appeal is essentially a short point of construction. Mr Mullan argues that the Underlease from HCL to Mr Wellstead was the sale of a relevant interest for the purposes of section 296. Mr Bracegirdle argues that what was sold was not a relevant interest.

25. Mr Mullan had originally pursued a further ground of appeal, namely that Mr Wellstead and HCL were not connected persons so that the election under section 290 had been valid. Shortly prior to the hearing that further ground of appeal was abandoned and it was accepted that Mr Wellstead and HCL were connected persons.

26. Before addressing the detailed submissions of the parties we must first consider some authorities as to the approach we should take to the construction of statutes. Mr

Mullan reminded us that a purposive approach is required in construing all statutes, not just taxing statutes. In *R (otao Quintavalle) v Secretary of State for Health [2003] 2 AC 687* Lord Bingham described the task of construing statutory provisions at [8]:

> " *8. The basic task of the court is to ascertain and give effect to the true meaning of what Parliament has said in the enactment to be construed. But that is not to say that attention should be confined and a literal interpretation given to the particular provisions which give rise to difficulty. Such an approach not only encourages immense prolixity in drafting, since the draftsman will feel obliged to provide expressly for every contingency which may possibly arise. It may also (under the banner of loyalty to the will of Parliament) lead to the frustration of that will, because undue concentration on the minutiae of the enactment may lead the court to neglect the purpose which Parliament intended to achieve when it enacted the statute. Every statute other than a pure consolidating statute is, after all, enacted to make some change, or address some problem, or remove some blemish, or effect some improvement in the national life. The court's task, within the permissible bounds of interpretation, is to give effect to Parliament's purpose. So the controversial provisions should be read in the context of the statute as a whole, and the statute as a whole should be read in the historical context of the situation which led to its enactment.*"

27. Both parties referred us to the decision of Lewison J (as he then was) sitting in the Upper Tribunal in *Berry v Revenue & Customs Commissioners [2011] UKUT 81 (TCC)*. Whilst we are not concerned in the present case with tax avoidance the description of the approach to construction is helpful. At [31] he said as follows:

> " *31. In my judgment:*
>
> *i) The Ramsay principle is a general principle of statutory construction (Collector of Stamp Revenue v Arrowtown Assets Ltd (2004) ITLR 454 (§ 35); Barclays Mercantile Business Finance Ltd v Mawson [2005] STC 1 (§ 36)).*
>
> *ii) The principle is twofold; and it applies to the interpretation of any statutory provision:*
>
> *a) To decide on a purposive construction exactly what transaction will answer to the statutory description; and*
>
> *b) To decide whether the transaction in question does so (Barclays Mercantile Business Finance Ltd v Mawson (§ 36)).*
>
> *iii) It does not matter in which order these two steps are taken; and it may be that the whole process is an iterative process (Barclays Mercantile Business Finance Ltd v Mawson (§ 32); Astall v HMRC [2010] STC 137 (§ 44)).*
>
> *iv) Although the interpreter should assume that a statutory provision has some purpose, the purpose must be found in the words of the statute itself. The court must not infer a purpose without a proper foundation for doing so (Astall v HMRC (§ 44)).*

v) In seeking the purpose of a statutory provision, the interpreter is not confined to a literal interpretation of the words, but must have regard to the context and scheme of the relevant Act as a whole (WT Ramsay Ltd v Commissioners of Inland Revenue (1981) 54 TC 101, 184; Barclays Mercantile Business Finance Ltd v Mawson (§ 29)).

vi) However, the more comprehensively Parliament sets out the scope of a statutory provision or description, the less room there will be for an appeal to a purpose which is not the literal meaning of the words. (This, I think, is what Arden LJ meant in Astall v HMRC (§ 34). As Lord Hoffmann put it in an article on Tax Avoidance: "It is one thing to give a statute a purposive construction. It is another to rectify the terms of highly prescriptive legislation in order to include provisions which might have been included but are not actually there": See Mayes v HMRC [2010] STC 1 (§ 30)).

vii) In looking at particular words that Parliament uses what the interpreter is looking for is the relevant fiscal concept: (MacNiven v Westmoreland Investments Ltd [2001] STC 237 (§§ 48, 49)).

viii) Although one cannot classify all concepts a priori as "commercial" or "legal", it is not an unreasonable generalisation to say that if Parliament refers to some commercial concept such as a gain or loss it is likely to mean a real gain or a real loss rather than one that is illusory in the sense of not changing the overall economic position of the parties to a transaction: WT Ramsay Ltd v Commissioners of Inland Revenue (1981) 54 TC 101, 187; Inland Revenue Commissioners v Burmah Oil Co Ltd (1981) 54 TC 200, 221; Ensign Tankers Ltd v Stokes [1992] 1 AC 655, 673, 676, 683; MacNiven v Westmoreland Investments Ltd (§§ 5, 32); Barclays Mercantile Business Finance Ltd v Mawson (§ 38).

ix) A provision granting relief from tax is generally (though not universally) to be taken to refer to transactions undertaken for a commercial purpose and not solely for the purpose of complying with the statutory requirements of tax relief: (Collector of Stamp Revenue v Arrowtown Assets Ltd (§ 149)). However, even if a transaction is carried out in order to avoid tax it may still be one that answers the statutory description: (Barclays Mercantile Business Finance Ltd v Mawson (§ 37). In other words, tax avoidance schemes sometimes work.

x) In approaching the factual question whether the transaction in question answers the statutory description the facts must be viewed realistically. (Barclays Mercantile Business Finance Ltd v Mawson (§ 36).

…"

28. Mr Mullan submitted that what Lewison J said at (vi) was not relevant here because the relevant provisions are not highly prescriptive. He relied in particular on what was said at (viii), (ix) and (x). In contrast Mr Bracegirdle relied in particular on what was said at (vi) because he submitted that the relevant provisions were highly prescriptive.

29. We were also referred to the Supreme Court decision in *Forde and McHugh Ltd v Revenue & Customs Commissioners [2014] UKSC 14* at [14]-[16] as an example of the court taking a realistic approach to statutory construction.

30. Similar principles were applied by the Court of Appeal in *Pollen Estate Trustee Company Ltd v Revenue & Customs Commissioners [2013] EWCA Civ 753*. Mr Mullan submitted that there were a number of parallels between the present appeal and that case. In particular he submitted that it was difficult to see how relief could have been available on a literal construction, but that the Court of Appeal took a broad purposive approach in circumstances where there was no policy reason for Parliament to have intended relief to be refused.

31. Pollen Estate concerned liability to stamp duty land tax ("SDLT"). In the ordinary course a charity which acquires property in furtherance of its charitable purposes is entitled to relief from SDLT on the purchase price. The same applies if a non-charity purchases property as bare trustee for a charity. The issue in Pollen Estate involved a non-charity also acquiring a beneficial interest in the property. The question was whether the charity was entitled to any relief at all in respect of its purchase of a share of the beneficial interest?

32. Paragraph 1(1) Schedule 8 Finance Act 2003 provided relief from SDLT for charities as follows:

> " *1(1) A land transaction is exempt from the charge if the purchaser is a charity and the following conditions are met …*"

33. The Court of Appeal considered what policy reason there might be for denying relief to a charity where it purchased jointly with a non-charity. The court found that there was no policy reason to deny relief. It then referred to a number of authorities defining the boundaries between the role of a court in construing legislation and the power of Parliament to legislate. In particular in *Inco Europe Ltd v First Choice Distribution* [2000] 1 WLR 586 at 592 where Lord Nicholls said:

> " *It has long been established that the role of the courts in construing legislation is not confined to resolving ambiguities in statutory language. The court must be able to correct obvious drafting errors. In suitable cases, in discharging its interpretative function the court will add words, or omit words or substitute words … This power is confined to plain cases of drafting mistakes. The courts are ever mindful that their constitutional role in this field is interpretative. They must abstain from any course which might have the appearance of judicial legislation. A statute is expressed in language approved and enacted by the legislature. So the courts exercise considerable caution before adding or omitting or substituting words. Before interpreting a statute in this way the court must be abundantly sure of three matters: (1) the intended purpose of the statute or provision in question; (2) that by inadvertence the draftsman and Parliament failed to give effect to that purpose in the provision in question; and (3) the substance of the provision Parliament would have*

made, although not necessarily the precise words Parliament would have used, had the error in the Bill been noticed. The third of these conditions is of crucial importance. Otherwise any attempt to determine the meaning of the enactment would cross the boundary between construction and legislation."

34. The court in Pollen Estate also referred to the words of Lord Reid in *Luke v IRC [1963] AC 557* at 577:

> " *To apply the words literally is to defeat the obvious intention of the legislation and to produce a wholly unreasonable result. To achieve the obvious intention and produce a reasonable result we must do some violence to the words. This is not a new problem, though our standard of drafting is such that it rarely emerges. The general principle is well settled. It is only where the words are absolutely incapable of a construction which will accord with the apparent intention of the provision and will avoid a wholly unreasonable result, that the words of the enactment must prevail.*"

35. The court then went on to construe paragraph 1(1) adding the highlighted words as follows: "A land transaction is exempt from the charge ***to the extent that*** the purchaser is a charity and the following conditions are met …". The court considered that "*… there is sufficient 'policy imperative' to justify the reading… Not to afford a charity relief in such circumstances would, in my judgment, be capricious*".

36. In the present case Mr Mullan effectively submitted that the ambiguity in the statutory provisions could be resolved without the need to add, omit or substitute any words. He did not rely on any obvious drafting error nor did he accept that is was necessary to do any violence to the words used in CAA 2001. The underlying policy of IBAs could be respected and what would otherwise be an unreasonable result could be avoided with a purposive construction of the words used. To that extent therefore he did not suggest that we were in the realms of Inco Europe or Luke v IRC.

37. At first sight the interest of HCL when it built Unit 2 was the Lease. It was not the same interest that was transferred by HCL to Mr Wellstead, namely the Underlease. The issue before us is really whether a purposive construction of the provisions, in particular section 286, gives a different result.

38. Mr Mullan submitted that the legislation for IBAs was designed amongst other things to encourage expenditure in enterprise zones. In the context of that overriding purpose there was no policy reason or rationale for a distinction between the Lease and the Underlease on the present facts. The term "interest in the building" in section 286 should not be construed in a narrow technical sense. Regard should be had to the nature of the rights enjoyed by the person incurring the expenditure. In the case of HCL it had a right to use and occupy the building for a period of 125 years from 24 August 2001. The intention of the parties had been to put Mr Wellstead in the same position. Because of conveyancing technicalities the Lease could not simply be assigned, because it was a lease of both Unit 1 and Unit 2, and Unit 1 had not yet been sold. The reality however was that in a practical sense all HCL's right and interest in Unit 2 was sold to Mr Wellstead by way of the Underlease. All that HCL retained was

the right to use and occupy the premises for 5 days at the end of the 125 year period. There was therefore a sale of the relevant interest by HCL to Mr Wellstead.

39. That result was consistent, said Mr Mullan, with a realistic and purposive construction of the provisions. Any other result would be inconsistent with the purpose of the legislation which was to grant IBAs to those incurring expenditure on buildings in enterprise zones. Mr Wellstead had incurred such expenditure.

40. If that was the extent of Mr Mullan's submissions we think he would have been in some difficulty persuading us that the provisions could be given such a purposive construction. Importantly however Mr Mullan relied on the terms of section 288(1) set out above. For the sake of convenience we repeat them here:

> "*288(1) An interest does not cease to be the relevant interest merely because of the creation of a lease or other interest to which that interest is subject.*
>
> *(2) This is subject to any election under section 290.*"

41. Mr Mullan emphasised use of the word "merely" in that sub-section. Section 288(1) refers to the position where a lease or other subordinate interest is created, to which the relevant interest is subject. He submitted that the effect of section 288(1) was that the grant of a subordinate interest will not "*on its own*" cause an interest to cease to be a relevant interest. The implication was that depending on the circumstances the grant of a subordinate interest could cause an interest to cease to be a relevant interest.

42. Mr Mullan submitted that the question whether the grant of a sub-lease causes a lease to cease to be a relevant interest would involve consideration of the terms of the sub-lease. In particular the grant of a sub-lease where the lessor did not retain any valuable interest in a building might cause a lease to cease to be a relevant interest. It was implicit in Mr Mullan's submissions that if in those circumstances the lease ceased to be a relevant interest, the purposive construction of section 286 meant that the granting of a sub-lease would be treated as the sale of a relevant interest. If the grant of a sub-lease could never amount to the sale of a relevant interest then section 288(1) would be unnecessary. On that basis Mr Mullan submitted that it was not necessary to omit, add or substitute any words in the legislation to arrive at a result consistent with the policy intention of Parliament. Nor was it necessary to do violence to the words of the statute.

43. We were also referred to the decision of Megarry J in *Sargaison v Roberts [1969] 1 WLR 951* as support for the proposition that niceties of English land law should not affect the availability of capital allowances. In that case the taxpayer was a farmer who acquired freehold property in 1957 and incurred considerable capital expenditure that qualified for allowances. In 1964 he settled the freehold on trust for the benefit of his family, and the trustees immediately granted a 40 year lease to the taxpayer so that he could continue farming. The Inland Revenue refused a capital allowances claim in 1965-66 on the basis that the taxpayer had transferred the whole

of his interest in the land to some other person, namely the trustees within section 314(4) Income Tax Act 1952.

44. The general commissioners allowed the taxpayer's appeal and Megarry J dismissed an appeal by the inspector of taxes. He held that whilst there was a notional instant during which the taxpayer had no interest in the land, the reality was that his interest had been reduced from freehold ownership to a long lease and he had not transferred the whole of his interest in the land. He was supported in that conclusion by his view that the Act was not drafted in terms of English property law but in broader and less technical language. He concluded that the statutory provision was intended to operate broadly, without fine technical distinctions.

45. We do not consider that Sargaison v Roberts provides much if any real support for Mr Mullan's arguments in the context of the provisions we are asked to construe. More important are the words used by Parliament in the statute, together with the broad context and policy which underpin IBAs.

46. Mr Bracegirdle submitted that the legislation made specific provision for circumstances where there was more than one interest in a building. On the facts of the present case there were three interests in Unit 2 – the freehold, the Lease and the Underlease. The possibility of more than one interest in a building made it important to define precisely the interest which was relevant for IBA purposes. He relied on the express wording of section 286(3) which makes provision for more than one interest in a building. Where one of the interests is reversionary on the other it is the reversionary interest which is the relevant interest.

47. Mr Bracegirdle also relied on section 359(5). Section 286(1) which sets out the general rule as to what is the relevant interest, is expressly subject to section 359. Section 359 makes provision for new leases arising on the termination of a lease to be treated as a continuation of the original lease. Section 359(5) provides as follows:

> "*359(5) If on the termination [of a lease] –*
>
> *(a) another lease is granted to a different lessee, and*
>
> *(b) in connection with the transaction that lessee pays a sum to the person who was the lessee under the first lease,*
>
> *the two leases are to be treated as if they were the same lease which had been assigned by the lessee under the first lease to the lessee under the second lease in consideration of the payment.*"

48. Section 359(5) could apply in the circumstances of the present appeal if there had been a surrender of the Lease together with a re-grant of a lease by the freeholder to Mr Wellstead. Obviously that would require a willingness on the part of the freeholder to grant a new lease directly to Mr Wellstead, which it may or may not have been willing to do. It might also apply to some form of partition of the Lease.

49. Mr Mullan accepted that in theory it might have been possible for there to have been some form of partition of the lease and an assignment of that part relating to Unit 2. We do not know whether HMRC would have maintained an argument that a partitioned lease of Unit 2 would not be the same interest as the relevant interest which was a lease of both units.

50. Mr Bracegirdle submitted that if Parliament had intended to treat the grant of a long lease as a sale of the relevant interest then it could easily have done so. However it restricted relief in such circumstances to sub-leases exceeding 50 years between non-connected persons and where an election was made. It did not intend IBAs to be available generally in the case of sub-leases outside sections 290 and 291. He submitted that was the only qualification to the general rule in section 288(1) that an interest does not cease to be a relevant interest because of the creation of a subordinate interest.

51. The difficulty with Mr Bracegirdle's construction of section 288 is that the word "merely" in section 288(1) is rendered unnecessary. It is not necessary to include that word simply, as Mr Bracegirdle suggested, to lead the reader to sub-section (2). Sub-section (2) naturally follows from and qualifies sub-section (1) without any need for the word "merely". Mr Bracegirdle did acknowledge that on his construction if the word was not simply introducing the qualification in sub-section (2) then it served no useful purpose.

52. Mr Bracegirdle maintained that the legislation was highly prescriptive about the meaning of relevant interest, in particular the circumstances where the grant of a lease exceeding 50 years could be treated as a sale of the relevant interest. It was therefore hard to see why the statute would not have set out more detail as to the circumstances in which the grant of a lease generally might be treated as the sale of the relevant interest.

53. We agree with Mr Mullan's submissions in relation to section 288. As a matter of law the grant of a lease or a sub-lease does not affect the nature of the interest out of which it is granted, whether it is a freehold or a leasehold interest. The leaseholder owns the same interest in the property before and after the grant of a sub-lease. However these provisions introduce the concept of a relevant interest, which governs entitlement to IBAs. It seems to us that Parliament, in enacting section 288(1), anticipated that there may be circumstances where the grant of a lease might cause a relevant interest to cease to exist for the purposes of the scheme of the legislation. However the grant of a sub-lease would not, on its own, cause a headlease to cease to be a relevant interest. Adopting that construction the legislation begs the following questions:

(1) In what circumstances might the grant of a sub-lease mean that the lease will cease to be a relevant interest, and

(2) What is the effect of a lease ceasing to be a relevant interest as the result of the grant of a sub-lease. In particular, does the granting of the sub-lease amount to a sale of the relevant interest.

54. As to the first question we agree with Mr Mullan that the legislation does not specify in what circumstances the granting of a sub-lease might cause the relevant interest to cease to exist because it is inevitably a matter of degree. As Mr Mullan said, a sub-lease could come in all shapes and sizes. It would be difficult for Parliament to prescribe all the circumstances in which the grant of a sub-lease might amount to the transfer of a relevant interest and therefore the matter is left for interpretation on the particular facts of the case. To that extent we do not consider that the legislation is highly prescriptive. What is prescriptive is the circumstances in which the grant of any lease of more than 50 years will amount to a sale of the relevant interest.

55. It is certainly the case from the scheme of the legislation that there can only be one relevant interest. The granting of a sub-lease does not automatically cause the headlease to cease to be the relevant interest. One specific situation in which the grant of a sub-lease will cause a headlease to cease to be the relevant interest is in section 290. That is where the sub-lease is for more than 50 years, it is granted to a non-connected person and the appropriate election is made. However the legislation does not say that that is the only circumstance in which the grant of a sub-lease will amount to a sale of the relevant interest.

56. Section 290(2) expressly provides that IBAs will be available for cases falling within section 290(1) "as if" the grant of the sub-lease were a sale of the relevant interest. It seems to us that the provisions of section 290 provide an opportunity for certainty in the case of a sub-lease of more than 50 years, regardless of the length of the reversionary interest. It is not however inconsistent with making IBAs available to the purchaser of a sub-lease generally where the question of whether there has been a sale of the relevant interest will be a matter of degree.

57. Section 290(2) implicitly provides the answer to the second question as to the effect of an interest ceasing to be a relevant interest following the grant of a sub-lease. The provisions are to apply as if the grant of the sub-lease were a sale of the relevant interest. Mr Bracegirdle did not suggest that the effect of a relevant interest ceasing to be a relevant interest by virtue of section 288(1) would be anything other than a sale of the relevant interest.

58. Mr Bracegirdle pointed to the strict qualifying conditions for IBAs including qualifying expenditure on a qualifying building. The construction contended for by the Respondents produced what he described as an entirely reasonable result. It was entirely reasonable to treat separate interests in a different way. However he could not identify any policy reason why IBA's should be available to a purchaser by way of assignment of a headlease but not available to a purchaser of a sub-lease for the whole term of the headlease, save a few days. In particular if the economic effect of a sub-lease is the same as an assignment then there is no policy reason why IBAs should not be available. It was not suggested that there was any policy connected with tax avoidance or abuse of the provisions which should distinguish those situations. Certainly there is no suggestion that the transactions between HCL and Mr Wellstead were in any way connected with tax avoidance.

59. It is notable in this context that the Sale Agreement anticipated two methods of completion. Either the grant of a sub-lease of Unit 2 or, if Unit 1 had previously been sold by way of sub-lease, an assignment of the Lease. Whatever method of completion was adopted the consideration payable by Mr Wellstead was £1m. That serves to highlight the fact that there was no commercial difference between the Lease in so far as it affected Unit 2 and the Underlease. Mr Bracegirdle had submitted that on the facts of the present case the Lease continued to have value in relation to Unit 1 which was not affected by the Underlease of Unit 2. However the provisions for IBAs are concerned with the relevant interest in the building. Plainly if Mr Wellstead had taken an assignment of the Lease before Unit 1 had been sold it would have cost him considerably more than the £1m he paid. There is no policy reason why he should not be entitled to IBAs on a purchase of only Unit 2.

60. Mr Mullan's overarching submission was that the grant of the Underlease answered the statutory description of a sale of the relevant interest with the result that the purchase price paid by Mr Wellstead qualified for IBAs. For the reasons given above we accept that submission.

Conclusion

61. In all the circumstances we allow the appeal.

62. 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.

JONATHAN CANNAN
TRIBUNAL JUDGE

RELEASE DATE: 13 JULY 2016