THE SPECIAL COMMISSIONERS

SALARIED PERSONS POSTAL LOANS LIMITED
Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS
Respondents

Special Commissioner: DR JOHN F. AVERY JONES CBE

Sitting in public in London on 29 September 2005

Felicity Cullen, counsel, instructed by Auerbach Hope, Chartered Accountants, for the Appellant

Jeff Rodin, HM Revenue and Customs Appeals Unit London, for the Respondents

DECISION

1. This is an appeal by Salaried Persons Postal Loans Limited against the refusal on 2 April 2003 of a claim for small companies relief from corporation tax on the basis that an associated company, Malcolm Muir Limited ("MML"), did carry on a trade or business in the years ended 31 July 1998 to 2001. Mrs Felicity Cullen appeared for the Appellant, and Mr Jeff Rodin appeared for the Respondent.

2. The issues were agreed as follows:

> (1) The Appellant, Salaried Staff London Loan Co Limited ("SSLL"), Managers Limited ("ML") and Malcolm Muir Limited are four companies under the control of Mr. R Selig within the meaning of s 416 of the Taxes Act 1988 which have been treated as associated with one another for the purposes of small companies' relief from corporation tax under s 13 of the Taxes Act 1988 and for the purposes of the payment of corporation tax by instalments within the provisions of Statutory Instrument No. 3175 of 1988.
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> (2) The Appellant, SSLL and ML are private limited companies registered in England and Wales and are resident, for tax purposes, in the United Kingdom. MML is a private limited company registered in Scotland and is resident, for tax purposes, in the United Kingdom.
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> (3) In determining for a company the profit limits for small companies' relief and payment of corporation tax by instalments, the number of companies which are associated with one another is material; but a given company is to be excluded from the number of companies which are associated with one another in any accounting period if the relevant company has not carried on any trade or business at any time in that period: s 13(4) of the Taxes Act 1988.
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> (4) MML has not carried on any trade in any of the accounting periods which are relevant in this case. The issue between the companies and the Respondent is, however, whether MML has carried on any "business", within the ordinary meaning of that word, at any time in any of the accounting periods which are the subject of the present appeals.
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> (5) The outcome of this issue will determine whether MML is to be counted as one of the associated companies referred to above for the purposes of the small companies' relief and payment of corporation tax by instalments.

3. There was an agreed statement of facts as follows:

> (1) For many years until 1966, MML carried on the trade of making personal loans from its premises at West Regent Street, Glasgow. MML owned the Scottish equivalent of the freehold of these premises.

(2) MML's trade of making personal loans was licensed under the Consumer Credit legislation.

(3) In 1966, MML vacated its West Regent Street premises and let them to a tenant, J B & G Forsyth.

(4) At the same time, MML moved to new premises (which it leased) at 111 Union Street, Glasgow and continued to carry on its trade from these new premises. MML shared these premises with the Appellant.

(5) MML carried on its trade of making personal loans from the Union Street premises until 30 November 1995. It then ceased trading.

(6) In the year ended 31 July 1996 MML surrendered its licence under the Consumer Credit Act, and MML and the Appellant vacated the premises at 111 Union Street, Glasgow.

(7) MML has continued to own its premises at West Regent Street, Glasgow from which it receives a net rental income twice a year. A cheque for the full rent payable less commission (i.e. for net rent) is sent directly to ML who acts as banker for the Appellant, MML, and SSLL.

(8) The income from the West Regent Street premises has been MML's sole source of income since it ceased trading on 30 November 1995 in the year ended 31 July 1996.

(9) MML's accounts show that it has received rent since at least 1966 when it vacated and let its West Regent Street premises.

(10) There is a substantial inter-company debt between ML and MML. No interest has been charged to ML in the years which are the subject of the present appeals or at all. The inter-company debt represents monies held by ML for MML in ML's capacity as "group" banker. As at 1 August 1996 the inter-company debt stood at £1,227,342 and included sums arising from the disposals of MML's assets (in years prior to those under consideration). The figure rose to £1,263,637 over the period to 31 July 2003.

(11) In the year ended 31 July 1997, MML incurred expenditure in the form of "rent, rates and service charges" of £3,733. This expenditure was incurred in respect of the Union Street premises which MML had vacated (in the year ended 31 July 1996) but did not immediately dispose of and continued to lease until the expiry of the lease in April 1998. MML incurred accountancy costs of £1,763.

(12) MML's lease of the Union Street premises expired in April 1998.

(13) In the year ended 31 July 1998 MML incurred rent, rates and service charges of £3,854, again in respect of the vacated Union Street premises. MML incurred accountancy costs of £1,763.

(14) In the year ended 31 July 1999 MML incurred agent's fees of £998 in respect of the letting of the West Regent Street premises, and expenses on "repairs" (which were in fact dilapidations) of £3,854 in respect of the

Union Street premises. Though the accounts for this year (and following years) refer to the incurring of agents fees, the agents in fact in all years paid MML rents net of agent's fees (see paragraph 3(7) above). There was no factual change in practice over the years, merely a change of accounting treatment. (Instead of receipts of net rents, gross rent and expenses were shown in MML's accounts). There were no negotiations with regard to the dilapidations of the Union Street premises. An invoice from Richard Ellis (Surveyors) was simply settled. MML incurred accountancy costs of £1,763.

(15) In the year ended 31 July 2000, MML incurred agent's fees of £757 and accountancy costs of £1,763.

(16) In the year ended 31 July 2001 MML incurred agent's fees of £758 and accountancy fees of £1,763.

(17) MML's Memorandum of Association was drawn up in 1927 and permits the letting of property.

(18) The following facts have pertained at all times after MML ceased trading and disposed of all of its assets other than the premises at Union Street and West Regent Street, Glasgow:

(a) MML has not had its own bank account but has maintained an inter-company balance with ML, the group's banker;

(b) MML has had two directors but has had no employees;

(c) MML has not paid any directors' fees or salaries;

(d) MML has not paid any dividends nor made any distributions;

(e) MML has not purchased any assets or disposed of any assets;

(f) MML has neither received nor paid any interest on its inter-company balance with ML; there is a small amount of interest shown in the accounts to 31 July 1998. This was supplement on tax which was paid early;

(g) MML has not negotiated any rent reviews. Rent reviews have taken place automatically by reference to a pre-existing formula providing for 20% increases in rentals at the review dates and there has been no communication with the agents since 1995 other than a short telephone call approximately seven years ago when Mr. Selig simply acceded to a request to proceed with a rent review of the West Regent Street premises;

(h) MML has not sought to let the Regent Street premises or any part of them to a new tenant. MML has, since 1966, let the premises to the same tenant, JB & G Forsyth;

(i) The Appellant, MML, ML, and SSLL have produced accounts.

(19) The shares in MML are held as follows:

Ashington Family Loan Co Ltd	2,990
R B Selig	5
Mrs D Selig	5
	3,000

(20) The shareholding in Ashington Family Loan Co Limited is as follows:

J R Gaba	15 (daughter of R Selig)
Naomi Selig	15 (daughter of R Selig)
Ruth Selig	15 (daughter of R Selig)
Daniel Selig Trust	15 (re son of R Selig)
Mrs D Selig	39 (wife of Mr R Selig)
R Selig	1
	100

(21) The small companies' relief from corporation tax available to the Appellant under section 13 of the Taxes Act 1988 has been restricted by the Inland Revenue under s 13(3) and (4) for each of the accounting periods to which these appeals relate on the grounds that in the respective years to 31 July 1998, 1999, 2000 and 2001 the Appellant had three and not two (as the taxpayer contends) relevant associated companies.

4. I was also given a copy of the lease of the West Regent Street premises. The premises comprise five rooms on the first floor. The lease is from 11 November 1990 to 10 November 2006 and so must be a new lease granted to the same tenant. The rent is £7,000 pa but from 11 November 1992 and every third year thereafter the landlord may give the tenant notice before the review date proposing a fair market rent which, failing agreement, is to be determined by an independent surveyor at the tenant's cost, but which is not to be less than 20 per cent more than the rent for the previous period. The tenant is liable to repair, maintain, renew and if necessary rebuild the premises (but repairs covered by perils insured against are not to cost more than the insurance moneys). The tenant is to paint the outside of premises in every the third year and the inside every sixth year. The landlord insures the premises against a list of perils for the full restatement value (including three years' rent, to include potential rent increases) and collects the premium from the tenant on the next quarter day. MML's accounts show rent receivable in the years to 31 July 1997 £7,761 (net of agent's fee); 1998 £9,441 (net of agent's fee); 1999 £11,186 (gross of agent's fee from here); 2000 and 2001 £12,096. If the rent review was in November 1998 I am not sure why the rent for the years to 31 July 1997 and 1998 are not the same. If the 2000 figure is the post-review figure for a whole year and the 1998 figure the pre-review figure for a whole year and the agents took the same percentage fee of 6.26% as in the later year, the 1998 figure before the agent's fee would have been £10,072 in which case the figures show that the rent increased by the minimum 20 per cent. There was no evidence about compliance with the terms of the lease but I deduce that MML performed its obligations, including therefore insuring and collecting the insurance premiums from the tenant. I will also prefer the description

of the rent review process in the lease to that summarised in paragraph 3(18)(g) above.

5. Mrs Cullen, for the Appellant, contends in outline:

> (1) Whether a business is carried on is a question of fact. Here the facts are extremely unusual involving letting to the same tenant for over 30 years with little activity required by MML.
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> (2) MML was less active than the company in *American Leaf Blending v DG of IR* [1978] 3 All ER 1185 which entered into at least five licences, three of the warehouse, one of the factory following the removal of machinery, and one of both together between April 1964 and October 1968. There is no principle that receipt of rental income must be derived from a business, otherwise *American Leaf* would have been decided on that ground without considering the facts. MML was also less active than the company in *Land Management Limited v Fox* [2002] STC (SCD) 152 which paid for repairs and insurance and in some years professional fees in respect of its let residential property. It was similar to the passive receipt of bank interest on funds derived from former trading in *Jowett v O'Neill & Brennan Construction Ltd* [1998] STC 482.
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> (3) The distinction between individuals and companies made in *American Leaf* was old-fashioned and should not be given weight since there are now entities that are taxed as companies without being companies (unincorporated associations), and entities that are companies but are not taxed as companies (limited liability partnerships).

6. Mr Rodin, for the Respondent, contends in outline:

> (1) MML is not a dormant company. As in *American Leaf* MML was putting its assets to gainful use by letting for rent which for a company was prima facie the carrying on of a business. Activity may be "intermittent with long intervals of quiescence in between" (p.1189e); here in the circumstances of the letting much activity was unnecessary.
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> (2) In letting the property MML was operating under a main object in clause III(2) of its Memorandum of Association: "To purchase or otherwise acquire and to hold, sell, exchange, surrender, lease, mortgage, charge, convert, turn to account, dispose of, and deal with property and rights of all kinds…."

7. In *American Leaf Blending* a company ceased its trade and entered into a total of five licenses of its warehouse and factory. The Malaysian Special Commissioners had decided that as it was acting within one of its objects in its Memorandum of Association it must in law be carrying on a business (p.1189a). This was disapproved by the Privy Council. Lord Diplock said at p 1189d:

> " In the case of a private individual it may well be that the mere receipt of rents from property that he owns raises no presumption that he is carrying on a business. In contrast, in their Lordships' view, in the case of a company

> incorporated for the purpose of making profits for its shareholders any gainful use to which it puts any of its assets prima facie amounts to the carrying on of a business. Where the gainful use to which a company's property is put is letting it out for rent, their Lordships do not find it easy to envisage circumstances that are likely to arise in practice which would displace the prima facie inference that in doing so it was carrying on a business.
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> The carrying on of 'business', no doubt, usually calls for some activity on the part of whoever carries it on, though, depending on the nature of the business, the activity may be intermittent with long intervals of quiescence in between. In the instant case, however, there was evidence before the Special Commissioners of activity in and about the letting of its premises by the company during each of the five years that had elapsed since it closed down its former tobacco business. There were three successive lettings of the warehouse negotiated with different tenants; there was the removal of the machinery from the factory area which made it available for use for storage and a separate letting of that area to a fresh tenant; and as recently as October 1968 there was the negotiation of a letting to a single tenant of both the factory area and the warehouse.
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> As has been mentioned, the question whether the company was carrying on a business of letting out its premises for rent was one of fact for the Special Commissioners;…."

The Privy Council decided that as a matter of fact there was only one decision that the Special Commissioners could have reached if they had applied the correct law, that the company was carrying on a business of letting out its premises. Mrs Cullen asks me to treat the distinction in the first paragraph of the quotation as an old fashioned distinction because there are now unincorporated associations which are not companies but are taxed as companies, and limited liability partnerships, which are companies but are (normally) not taxed as companies. However, it seems to me that the distinction is still valid because a company must act within its objects in its Memorandum of Association, whereas an individual is not so restricted (and nor is a LLP, which has unlimited capacity). A company's objects are therefore available to be used as a guide to the issue of whether a company that is not trading is carrying on business.

8. *Land Management Ltd* is an example of the Special Commissioners examining the facts and concluding that a company that received dividends, interest from an associated company (in two of the years), rent and bank interest and was incorporated for the purpose of undertaking business of an investment nature, did carry on business. Dr Brice examined each activity separately and then looked at the activities as a whole, reaching the same conclusion in each case. In relation to the letting activity the company incurred expenses on repairs and insurance and in two of the years professional fees, presumably on new letting.

9. *Jowett* is an example of the High Court not upsetting a finding of fact by the Special Commissioners that a company that merely put funds that were derived from its former trading on deposit at a bank was not carrying on an investment business. Park J said at p 489:

> "Mr Shirley [the Special Commissioner] has taken it for granted, rightly in my judgment, that if WCL was not carrying on an investment business it was not carrying on any other kind of business. The kinds of activities which our tax law recognises as species of business are trades, professions, vocations and investment. I am not aware of any other, and if another exists I am sure that it does not apply to the facts of WCL in 1995.
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> Mr Furness accepts that WCL was not carrying on an investment business merely by having its money on deposit at the bank. When I asked him what sort of business WCL was carrying on he said: 'It was in the business of gainfully employing its assets while keeping itself in existence pending any trading opportunity which might arise.' That is not a kind of business. It is just a description of the company's profile in the relevant period, stated in the grandest terms that can be managed for facts which amounted to scarcely anything, and then the epithet 'business' is attached.
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> It seems to me that the question which Mr Shirley asked himself, though not couched in the precise words of the statute, was nevertheless the real question to which the statute gave rise on the particular facts of this case. He tacitly assumed that if WCL was not carrying on an investment business, it was not carrying on any business at all. In my judgment he was entirely right, and there is no misstatement of law to be found in his decision."

10. I derive the following principles from the authorities.

> (1) A company need not carry on a business (indeed that is assumed by s 13) but there is a prima facie inference that it does so when it puts its property to gainful use by letting it out for rent (*American Leaf*). The inference is a strong one, see the first paragraph from the quotation from *American Leaf*.
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> (2) It may be relevant that the company was carrying out one of the principal objects stated in its memorandum (*American Leaf* in distinguishing an observation of Pollock MR in *IRC v Westleigh Estates Co Ltd* 12 TC 656); *Land Management Limited* at [24] where the Special Commissioner took into account that the company was incorporated for carrying on a business of an investment nature).
>
> (3) The act of receiving bank deposit interest having ceased one trade before starting another was not the carrying on of a business (*Jowett*).
>
> (4) In a case such as the present the only business that MML might be carrying on is that of investment (*Jowett*)

11. As Lord Diplock said in *Town Investments Ltd v Department of the Environment* [1978] AC 359 at 383 business is "an etymological chameleon; it suits its meaning to the context in which it is found." The context in s 13 of the Taxes Act 1988 is that an associated company is ignored for calculating the small companies' relief if it has not carried on any trade [which it is common ground that it has not] or business at any time in that period. It envisages that a non-trading company can receive income without carrying on a business of investment. This seems to indicate that why it receives income and what it does to receive the income is relevant.

12. The issue is one of fact. It seems to me that the following facts are particularly relevant: (1) MML did not purchase the West Regent Street premises as an investment; it traded from there, then moved in 1966 and traded from other premises until 1995 when it ceased trading, the West Regent Street premises being let during this time. (2) The same tenant has occupied the premises since 1966, although the lease was renewed in 1990 (and possibly on another occasion since 1966). (3) The lease is a tenant's repairing lease. (4) I infer that MML (through the agent) insures and collects the insurance from the tenant in accordance with the lease; although not shown in the accounts it is strictly a receipt and payment by MML. (4) I also infer that MML instigates rent reviews every three years, the one in 1998 being the only time in the relevant years, which was presumably the cause of the phone call from the agent approximately seven years ago mentioned in paragraph 3(18)(g) above. (5) MML employs an agent, at a cost at the end of the relevant periods of £757, who presumably does more than accounting for the rent after the agent's commission twice-yearly direct to ML (the group banking company), for example keeping the insurance current and collecting the insurance premium from the tenant, which activity I should attribute to MML because it is paying someone else to do something that it would have otherwise had to do itself under the terms of the lease. (6) MML used to trade and has objects primarily enabling it to trade; I consider that the renting of the West Regent Street premises was in accordance with object III(18) "to sell, feu, let, lease, or otherwise dispose of, or transfer, or deal with, the business, property, rights, interests, or undertakings of the Company, or any branch or part thereof, in consideration of feu duty, rent…" rather than the main object referred to by Mr Rodin which envisages both purchasing and letting. (7) The rest of MML's assets built up from its trading, amounting to £1.24m at the end of the relevant period, are lent interest-free to another group company ML, and so the premises from which it receives rent, which are in the balance sheet of MML at a director's valuation of £60,000 in the accounts up to 31 July 1999 and £90,000 thereafter, are a small part of MML's assets . (8) The only difference between any of the years under appeal is that in the years ended 31 July 1998 and 1999 MML in addition had expenditure relating to the Union Street premises from which it had formerly traded. Taking all of these factors into account I find as a fact that in each of the relevant years MML did not carry on an investment (or any other) business. The letting was the continuation of the letting of former trading premises, a state of affairs that had continued for nearly 30 years while MML was trading, and which merely continued after the cessation of trading.

13. Accordingly I allow the appeal in principle.