TC01823

Appeal numbers: TC/2010/6363, 6364, 6743 and 6744

Corporation tax – receipts of payments in respect of overpaid VAT and statutory interest – whether VAT repayments trading receipts – whether payments in respect of supplies made in discontinued trades chargeable to tax as post-cessation receipts – ICTA 1988, ss 103 and 106(2) – whether payments in respect of interest taxable under Sch D, Case III – loan relationships rules – whether a "money debt" – FA 1996, s 100

FIRST-TIER TRIBUNAL
TAX

(1) SHOP DIRECT GROUP
(2) SHOP DIRECT HOME SHOPPING LIMITED
(3) REALITY GROUP LIMITED
(4) LITTLEWOODS RETAIL LIMITED **Appellants**

- and -

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

TRIBUNAL: JUDGE ROGER BERNER
MISS SANDI O'NEILL (Member)

Sitting in public at 45 Bedford Square, London WC1 on 12 -14 December 2011

David Goldberg QC and Michael Jones, instructed by Weil, Gotshall & Manges, for the Appellant

Malcolm Gammie QC and Elizabeth Wilson, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. These are the appeals of the Appellants against amendments made by HMRC to the corporation tax self assessments of the Appellants for various accounting periods. The amounts of tax at issue are very considerable, but there is no dispute on the figures. The issues before us are accordingly issues of principle only.

2. All the appeals raise common issues, although the facts on which those issues arise are different in each case. What is common is that the issues concern the correct tax treatment of amounts received by each of the Appellants which derived from the determination or settlement of a number of long-running disputes between HMRC and companies that were at the material times representative members of the relevant VAT groups, as a result of which those representative members received repayments of amounts that had been wrongly accounted for as VAT, and – in most cases – statutory interest on those amounts.

3. There are two issues. The first is whether, as HMRC contend, the repayments of amounts wrongly paid as VAT (which, for shorthand, we shall describe as VAT repayments or VRPs) are liable to corporation tax as receipts taxable under Schedule D Case I or Case VI. The second issue is whether the amounts received in relation to statutory interest paid by HMRC on the repayments are liable to corporation tax as loan relationship credits or otherwise. These we describe as interest payments or IPs.

4. In essence, the Appellants say that neither the VRPs nor the IPs can be brought into account as receipts in the computation of any of the Appellants' profits because they are not from a taxable source. In particular, but without limitation, they do not arise from the carrying on of a trade and they are not from any form of debt obligation. As regards all the Appellants other than Reality Group Limited ("RGL") the Appellants say that they had no entitlement, as against HMRC or anyone else, to the VRPs or the IPs, and that those receipts were therefore by way of gift. As regards RGL, which received a VAT repayment as representative member, this was simply due to the fact that it was the relevant representative member entitled to the repayment from HMRC, and its retention of the payment was a matter of its own choice.

5. The Appellants were represented by David Goldberg QC with Michael Jones. Malcolm Gammie appeared for HMRC with Elizabeth Wilson.

Statement of Agreed Facts

6. We had a helpful statement of agreed facts, which we reproduce below. The statement refers to various appendices, which we have appended to this decision. The footnotes and annotations to the statement are those of the parties and not the Tribunal.

7. The statement includes a helpful glossary of abbreviations, which we have also adopted.

A. The VAT Repayments and Interest Payments

1. An agreed schedule of payments to which the appeals relate is set out at Appendix 1. The payments are labelled in this document as VAT Repayments 1 to 8 and Interest Payments 1 to 8. The facts stated in Appendix 1 are agreed so that, for example but without limitation, the identity of the entities referred to in columns 3, 5, 7 and 8 of the Schedule of VAT Repayments within Appendix 1 and the cash movements described in column 8 are agreed facts, as are the similar facts appearing in the Schedule of Interest Payments contained within Appendix 1.

2. Appendices 2 and 3 show the trade transfers which occurred within the Littlewoods and GUS sides of the group respectively. Appendix 4 sets out details (including any previous names) of the main companies involved in the factual background to the appeal.

3. A glossary of abbreviations is appended to this Agreed Statement of Facts.

B. The Assessments

The First Appellant, SDG

4. SDG appeals against amendments to its corporation tax returns

   (i) for the period 1 April 2004 to 31 March 2005;

   (ii) for the period 1 April 2005 to 30 April 2005;

   (iii) for the period 31 January 2007 to 30 January 2008.

5. SDG's appeal relates to a repayment in respect of overpaid VAT[1] in the sum of £15,686,929 ("VAT Repayment 1") and a payment of statutory interest in the sum of £1,328,993 ("Interest Payment 1")[2] made between February 2005 and 1 June 2005. Sums equal in amount to VAT Repayment 1 and Interest Payment 1[3] were accounted for as part of a £25,300,000 exceptional item within operating expenses in SDG's profit and loss account for the 13 month period ending 30 April 2005. The item is described as "VAT Recovery" in the 2005 accounts and Note 3 to the accounts states: "*The company has also reclaimed VAT following a successful claim brought against HM Customs and Excise regarding the treatment of commission payments to agents*".

[1] That is sums overpaid as VAT

[2] The Appellants say for the first time in their SOC at para 9.1 that no part of this sum is taxable. Previously, and as recorded in the Respondents' SOC at para 9, the Appellants accepted that £811,504 of this sum was taxable.

[3] In this Agreed Statement of Facts the reference to "sums equal in amount to" a VAT Repayment or an Interest Payment indicate that the Appellant in question contends that it has not brought into account the actual VAT Repayment or Interest Payment mentioned while accepting that it has recognised an amount equal to the Repayment or Payment in question in its accounts.

6. Its appeal also concerns a repayment in respect of overpaid VAT in the sum of £124,963,600 ("VAT Repayment 2") made on or about 19 September 2007 and a payment of statutory interest in the sum of £174,828,209 ("Interest Payment 2")[4] made on 19 September 2007. Sums equal in amount to VAT Repayment 2 and Interest Payment 2 were accounted for as an exceptional item of £299,791,000 in SDG's profit and loss account for the period ended 30 January 2008. Note 2 to the financial statements for 2008 states *"The current year exceptional item is in relation to a repayment in respect of VAT output tax and related interest. The funds were received by LW Corporation Limited and have been added to the parent undertaking debtor (see note 5)"*.

7. SDG is assessed in respect of the periods 1 April 2004 to 31 March 2005 and 1 April 2005 to 30 April 2005 on the basis that VAT Repayment 1 and Interest Payment 1 should be apportioned between those periods and brought into account so as to increase SDG's taxable profits for those periods by sums equal to the aggregate of VAT Repayment 1 and Interest Payment 1.

8. SDG is assessed in respect of the period 31 January 2007 to 30 January 2008 on the basis that VAT Repayment 2 and Interest Payment 2 should be brought into account in that period so as to increase SDG's taxable profits for that period by an amount equal to VAT Repayment 2 and Interest Payment 2.

The Second Appellant, SDHSL

9. SDHSL appeals against amendments to its corporation tax returns:

(i) for the period 1 May 2004 to 30 April 2005;

(ii) for the period 1 May 2006 to 30 April 2007;

(iii) for the period 1 May 2007 to 30 April 2008.

10. SDHSL's appeal relates to a repayment in respect of overpaid VAT in the sum of £7,740,298 ("VAT Repayment 3") paid on 24 January 2005. Sums equal in amount to VAT Repayment 3 were brought into account in SDHSL's profit and loss account for the period ended 30 April 2005. Also, statutory interest in the sum of £832,628 ("Interest Payment 3")[5] [was] paid in two instalments in February 2005. Sums equal to that amount were brought into the profit and loss account of SDHSL for the period ended 30 April 2005.

11. Its appeal also concerns a repayment in respect of overpaid VAT in the sum of £52,141,416 ("VAT Repayment 4") and statutory interest in the sum of £78,395,858

[4] The Appellants say for the first time in their SOC at para 10.1 that no part of this sum is taxable. Previously, and as recorded in the Respondents' SOC at para 10, the Appellants accepted that £11,239,877 of this sum was taxable.

[5] The Appellants say for the first time in their SOC at para 13.1 that no part of this sum is taxable. Previously, and as recorded in the Respondents' SOC at para 13, the Appellants accepted that £192,728 of this sum was taxable.

("Interest Repayment 4") paid in August 2007. Sums equal in amount to VAT Repayment 4 and to £77,654,202 of Interest Payment 4 were brought into account as an exceptional item of £129,796,000 in SDHSL's profit and loss account for the period ended 30 April 2007 in the way shown at Note 3 on page 14 of the accounts. A sum equal in amount to the remaining £741,656 of Interest Payment 4 was brought into account in the profit and loss account of SDHSL for the period ended 30 April 2008.

12. Note 3(a) to SDHSL's statutory accounts for the year ended 30 April 2007 and dated 12 July 2007 states:

"*The VAT claim of £129.8m arose from the incorrect treatment by HMRC of commission earned by agents on orders placed for third parties. Previously, the commission was treated as consideration for the provision of services by the agent but following litigation in 2004 it was accepted as a discount off the selling price of the goods, thereby reducing the company's VAT liability. HMRC had previously refused payment of the claim on the basis that it was caught by the 3 year cap on refunds introduced in 1996 but two Court of Appeal decisions in 2006 decided that the cap was introduced unlawfully and therefore claims for earlier years were effectively unrestricted. HMRC implemented the Court of Appeal decisions by issuing a Business Brief in August 2006 inviting companies to seek repayment of claims previously rejected under the three year cap.*

The repayment is subject to the company giving an undertaking that the monies will be repaid to HMRC with interest should HMRC ultimately be successful in having the Court of Appeal decisions overturned by the House of Lords. The case is due to be heard in the House of Lords in November 2007 with a decision expected early 2008. In addition to the undertaking, HMRC has sought a bank guarantee that the money will be repaid in the event of their appeal being successful."

13. SDHSL is assessed in respect of the period 1 May 2004 to 30 April 2005 on the basis that VAT Repayment 3 and Interest Payment 3 should be brought into account in that period so as to increase SDHSL's taxable profits for that period by an amount equal to VAT Repayment 3 and Interest Payment 3.

14. SDHSL is assessed in respect of the period ending 30 April 2007 on the basis that VAT Repayment 4 and Interest Payment 4 should be brought into account in that period so as to reduce its brought forward trading losses and to increase its non-trade financial profits. HMRC claims that, consequently, for the period ended 30 April 2008, the brought forward trading losses of SDHSL should be reduced.

The Third Appellant, RGL

15. RGL appeals against assessments made on it:

(i) for the period 1 April 1997 to 31 March 1998;

(ii) for the period 1 April 1998 to 31 March 1999.

16. RGL's appeal relates to a repayment in respect of overpaid VAT in the sum of £83,604,357 ("VAT Repayment 5") made in May 1998. RGL brought VAT Repayment 5 into account for the period ended 31 March 1998 as part of an exceptional item of £70,312,000 within cost of sales in the profit and loss account. The £70,312,000 was a composite figure made up of the £83,604,357 less a £25,900,000 provision (net £57,704,357) and several other items. The £25,900,000 provision was released in the following year of account (ending 31 March 1999) as part of a £23,700,000 exceptional item within cost of sales in the profit and loss account, the difference relating to 'professional fees'. Note 4 to the 1998 accounts describes the item as "*VAT refund (see Note 15)*". Note 15 to the 1998 accounts states: *"Following a decision of the Court of Appeal, these monies were repaid to the company by Customs and Excise in May 1998, together with appropriate interest."* Note 3 to the 1999 accounts describes the exceptional item as "*VAT refund*" and notes that "*Customs and Excise have now confirmed that they will not seek repayment of those refunds relating to the 1979 and 1991 VAT rate increases and the relevant provisions amounting to £23,700,000 net of professional fees, have been released*".

17. RGL is assessed in respect of both periods on the basis that VAT Repayment 5 should be brought into account for those periods, so increasing the taxable profits for the period ended 31 March 1998 by £57,704,357 and the profits for the period ended 31 March 1999 by £25,900,000.

18. For the avoidance of doubt there is no Interest Payment 5 (there being no interest at issue in relation to VAT Repayment 5).

The Fourth Appellant, LRL

19. LRL appeals against assessments made on it or amendments to its corporation tax returns:

(i) for the period 1 January 1995 to 31 December 1995;

(ii) for the period 1 May 1997 to 30 April 1998;

(iii) for the period 1 May 1998 to 30 April 1999; and

(iv) for the period 1 May 2001 to 30 April 2002.

20. LRL's appeal relates to repayment of VAT in the sum of £14,782,382 ("VAT Repayment 6") paid in two instalments on 22 November 1995 and 20 December 1995 and statutory interest of £20,527,859 ("Interest Payment 6")[6] paid in two instalments on 27 December 1995 and 12 January 1996. Sums equal in amount to VAT Repayment 6 and Interest Payment 6 were accounted for by way of a £35,310,000 credit entry shown in 'cost of sales' in LRL's profit and loss account for the period

[6] The Appellants say for the first time in their SOC at para 19.1 that no part of this sum is taxable. Previously, and as recorded in the Respondents' SOC at para 21, the Appellants accepted that the whole £20,527,859 was taxable.

ended 31 December 1995. Note 2 to the 1995 accounts states: *"Exceptional item – Recovery of value added tax payments made in earlier years (including interest)"*.

21. Its appeal also concerns a repayment in respect of overpaid VAT in the sum of £55,902,362 ("VAT Repayment 7") made on 12 May 1998 and statutory interest in the sum of £1,978,225 ("Interest Payment 7")[7] made on 12 May 1998. These sums were not disclosed in the consolidated statutory accounts of the Fourth Appellant for the year ended 30 April 1998, but the tax computation showed that £20,623,228 was included as a credit in its profit and loss account with a note that £56,091,540 was credited to the accounts but reduced by a £35,468,312 provision against possible action by HMRC to recover the earlier *Grattan* repayment. This provision was released in the following period ended 30 April 1999 by a corresponding credit to cost of sales.

22. Also, a repayment in respect of overpaid VAT in the sum of £596,457 ("VAT Repayment 8") made in two instalments on 28 January 2002 and 17 April 2002, and statutory interest of £46,730 ("Interest Payment 8") made on 1 August 2002. VAT Repayment 8 was not disclosed separately in the company's statutory accounts, but an amount equal to it is described as an 'income adjustment' in its tax computation.

23. LRL is assessed in respect of the period ended 31 December 1995 on the basis that VAT Repayment 6 and Interest Payment 6 should be brought into account in that period so as to increase LRL's taxable profits.

24. LRL is assessed in respect of the period ended 30 April 1998 and the period ended 30 April 1999 on the basis that VAT Repayment 7 and Interest Payment 7 should be brought into account in those periods so as to increase its taxable profits for the period ended 30 April 1998 by £22,490,938 and its taxable profits for the period ended 30 April 1999 by £35,279,134.

25. LRL is assessed in respect of the period ended 30 April 2002 on the basis that VAT Repayment 8 and Interest Payment 8 should be brought into account in that period so as to increase its taxable profits for that period by sums equal to the aggregate of VAT Repayment 8 and Interest Payment 8.

C. Trade transfers and VAT groups

SDHSL and LRL

26. The trade transfers relevant to SDHSL and the LRL are set out in diagrammatic form at Appendix 2 and are as follows:-

[7] The Appellants say for the first time in their SOC at para 20.1 that no part of this sum is taxable. Previously, and as recorded in the Respondents' SOC at para 22, the Appellants accepted that £110,515 of this sum was taxable.

1 January 1993 – the trades of Brian Mills Limited, Burlington Warehouses Limited, Janet Frazer Limited, John Moores Home Shopping Service Limited, Littlewoods Warehouses Limited and Peter Craig Limited (the "**Six Companies**") were each transferred to LRL. Copies of the six agreements are at [bundle: C/tabs 1-6] of the Agreed Bundle. At the time of the sale LRL was known as the International Import & Export Company Limited. Following the sale it became known as Littlewoods Home Shopping Group Ltd. From 25 January 1999 it became known as LRL.

1 November 2002 –LL and its subsidiary companies were acquired by LW Investments Ltd, the company of that name registered in England and Wales under number 04502467. "**LL**" means Littlewoods Limited, the company of that name registered in England and Wales under number 00262152, the previous names of which include The Littlewoods Organisation plc, in the period from 5 February 1982 to 16 October 2000, and Littlewoods plc, in the period from 17 October 2000 to 31 October 2002.

30 April 2003 – The trade of LRL was transferred to SDHSL. A copy of the Intra Group Reorganisation Agreement – Sale of Business, dated 30 April 2003 is at [bundle: C/tab 11/p68] of the Agreed Bundle. The effective date of the transfer was 4 May 2003.

27. Prior to 4 January 1987 the Six Companies were separately registered for VAT. This affects a portion of VAT Repayments 4 and 6. Between 4 January 1987 and 27 May 2003 the Six Companies were members of the LL VAT group 163 7696 28. LL was the representative member of the LL VAT group. LRL and SDHSL were also members of this VAT group.

28. Save where otherwise stated, the above matters relate to all or some of VAT Repayments and Interest Payments 3, 4, 6, 7 and 8.

SDG and RGL

29. The trade transfers relevant to SDG and RGL are set out in diagrammatic form at Appendix 3 and are as follows:-

As at **1 June 1991** SDG, the first Appellant, the unlimited company of that name registered in England and Wales under number 00039708 was a limited company registered under number 00039708 and known as John Noble Limited.

1 June 1991 – The trade of SDG (then known as John Noble Ltd) was transferred to RGL, the third Appellant, the company of that name registered in England and Wales under number 00739600. RGL was known as GUS

Home Shopping Ltd[8] until 28 November 2000. No document recording the terms of the transfer has been found.

1 April 1996 – GUS plc transferred part of its business relating to the Great Universal Catalogue trade to RGL (then known as GUS Home Shopping Ltd). "**GUS plc**" is the company of that name registered in England and Wales under number 00146575[9]. A copy of the sale agreement is at [bundle: C/tab7/p44] of the Agreed Bundle.

1 April 1997 – The trade of Abound Ltd (then known as Family Hampers Ltd) was transferred to RGL (then known as GUS Home Shopping Ltd). No document recording the terms of the transfer has been found.

1 April 1997 - The trade of Kay and Company Ltd was transferred to RGL (then known as GUS Home Shopping Ltd). A copy of the agreement dated 10 October 1997 is at [bundle: C/tab 8/p52] of the Agreed Bundle.

25 November 2000 – RGL transferred its trade to SDG (then known as John Noble Ltd). No document recording the terms of the transfer has been found.

28 November 2000 - SDG changed its name from John Noble Ltd to GUS Home Shopping Ltd.

22 July 2002 - Abound Ltd changed its name from Family Hampers to Abound Ltd.

25 October 2002 - SDG changed its name from GUS Home Shopping Ltd to Arg Equation Ltd[10].

27 May 2003 –March UK Limited acquired various companies including RGL, Kay & Co Ltd, Abound Ltd, and SDG from GUS plc. A copy of the share purchase agreement between GUS plc and March UK dated 27 May 2003 is at [bundle: C/tab12/p96] of the Agreed Bundle. "**March UK**" means the company registered in England and Wales under number 04730752 (now called Shop Direct Limited)

23 June 2003 – SDG changed its name from Arg Equation Ltd to Shop Direct Group Ltd

28 October 2005 – SDG transferred its trade to SDHSL. A copy of the Intra Group Reorganisation Agreement – Sale of Business dated 28 October 2005 is at [bundle: C/tab 15/p 254] of the Agreed Bundle. SDG sold "Assets… as reflected in the management accounts of the Vendor for the period ended 28

[8] Known as GUS Catalogue Order Ltd until 01/04/1996. From that date until 28/11/00 it was known as GUS Home Shopping Limited

[9] GUS plc is now known as Experian Finance plc.

[10] See e.g., [bundle: C/tab 12/p 147] of the Agreed Bundle

October 2005 excluding for the avoidance of doubt the Excluded Assets" ([bundle: C/tab15/p 255-256] of the Agreed Bundle).

On **25 October 2006** LW Corporation acquired SDG from March UK Ltd.

On **30 January 2007** SDG became an unlimited company.

30. The GUS VAT group 145 8990 25 included John Noble Ltd (joined 1 April 1973), Kay & Co (joined 1 April 1973), Abound Ltd (then known as Family Hampers Ltd) (joined 1 December 1977), and RGL (then known as Gus Home Shopping Ltd). The representative members of GUS VAT group were as follows:

GUS Merchandise Corporation Ltd[11] (CRN 00872776) from 1973 to 11 February 1992

Kay & Co Ltd from 12 February 1992 to 6 August 1997

RGL (then known as GUS Home Shopping Ltd) from 7 August 1997 to 19 May 2003.

31. Abound Ltd (then known as Family Hampers Ltd) left the GUS VAT group on 5 July 2002. It changed its name to Abound Ltd on 22 July 2002.

32. From 20 May 2003 GUS plc (now known as Experian Finance plc) became representative member of GUS VAT group 145 8990 25 and was replaced as representative member by Argos Ltd on 9 October 2006.

33. On 27 May 2003 March UK Ltd acquired RGL and SDG under a share purchase agreement of that date. A copy of the Agreement is at [bundle: C/tab 12/p 96] of the Agreed Bundle.

34. Abound Ltd was deregistered on or before 27 May 2003.

35. March UK Ltd had its own VAT group 813 0438 64. RGL, SDG, and Kay & Co Ltd joined the March UK VAT group following the share purchase. March UK Ltd was representative member of the March UK Ltd VAT group between 27 May 2003 and 25 June 2004.

36. March UK Ltd deregistered on 26 June 2004. March UK Ltd, RGL and SDG, joined the LL VAT group 163 7696 28 as from that date. LL was the representative member of the LL VAT group.

37. Kay & Co Ltd ceased to be registered for VAT purposes as from 26 June 2004.

38. The above matters are relevant to all or some of VAT Repayments 1, 2 and 5 and Interest Payments 1 and 2.

[11] Now known as Home Retail Group Holdings (Overseas) Ltd

Glossary of abbreviations

"**ACR**" (for "agents commission repayments") means a repayment in respect of overpaid VAT by HMRC attributable to the wrong calculation of VAT when goods were sold to agents of the supplier with a discount for commission (see *CCE v Littlewoods Organisation PLC* [2001] STC 1568);

"**Argos Ltd**" is the company of that name registered in England and Wales under number 01081551;

"Next/Grattan Repayment" or "**Grattan Repayment**" means a repayment in respect of overpaid VAT by HMRC attributable to the wrongful charging of VAT by HMRC on debtor balances, outstanding in respect of credit sales, when: (i) the increase in the rate of VAT from 8% to 15% occurred in 1979; and (ii) the increase in the rate of VAT from 15% to 17.5% occurred on 1 April 1991 (see *CCE v Grattan* [1995] STC 651);

"**GUS plc**" is the company of that name registered in England and Wales under number 00146575 which was named GUS plc as at 27 May 2003, but is now called Experian Finance plc;

"**HMRC**" means H.M. Revenue & Customs;

"**LL**" means Littlewoods Limited, the company of that name registered in England and Wales under number 00262152, the previous names of which include The Littlewoods Organisation plc, in the period from 5 February 1982 to 16 October 2000, and Littlewoods plc, in the period from 17 October 2000 to 31 October 2002;

"**LRL**" means the fourth Appellant, the company of that name registered in England and Wales under number 00421258;

"**LW Corporation**" means the company named LW Corporation Limited registered in Jersey under the number 0079696J;

"**LW Investments Ltd**" means LW Investments Limited, the company of that name registered in England and Wales under number 04502467;

"**March UK Ltd**" means the company registered in England and Wales under number 04730752 (which was named March UK Limited as at 27 May 2003, but is now called Shop Direct Limited);

"**RGL**" means the third Appellant, the company of that name registered in England and Wales under number 00739600;

"**SDG**" means the first Appellant, the unlimited company of that name registered in England and Wales under number 00039708;

"**SDHSL**" means the second Appellant, the company of that name registered in England and Wales under number 04663281;

the "**Six Companies**" means each of Brian Mills Limited, Burlington Warehouses Limited, Janet Frazer Limited, John Moores Home Shopping Service Limited, Littlewoods Warehouses Limited and Peter Craig Limited;

"**SMGT**" (for "the standard method of calculating gross takings") means a repayment in respect of overpaid VAT by HMRC attributable to the wrongful charging of VAT on a supplier's debtor balances as at 28 February 1997, when the standard method of calculating gross takings was withdrawn (see *R v HMRC ex parte Littlewoods Home Shopping Group Limited* [1998] STC 445);

"**VAT**" means value added tax;

"**WGM**" means Weil, Gotshal & Manges.

[End of Statement of Agreed Facts]

Other evidence

8. We also had a number of bundles of documents. All the documents were agreed. In light of that, and the agreed facts, Mr Goldberg informed us at the outset of the hearing that he did not intend to call any witnesses. The witness statements that had been served and filed were accordingly withdrawn, and we have not considered them.

Further findings of fact

9. The statement of agreed facts and the agreed documents take us only so far. We have to make findings as to the nature of the amounts received by each of the Appellants. In this connection we have regard to the fact that the burden of proof lies on the Appellants. We think it is most convenient for us to take each Appellant in turn. Our discussion of the underlying facts may involve some repetition of facts that are included in the agreed statement or in tabular or diagrammatic form elsewhere in this decision, but we consider that this is necessary if we are to provide a coherent picture.

Shop Direct Group ("SDG")

10. SDG received two VAT repayments (VRP 1 and 2) and two associated interest payments (IP 1 and 2).

VRP1 and IP 1

11. VRP 1 was paid by HMRC[12] to GUS plc, March UK and LL in February and May 2005. That repayment was an ACR, namely a repayment in respect of VAT overpaid when goods were sold to agents of the supplier with a discount for commission. The overpaid VAT had been paid by RGL, March UK and LL (as the relevant representative members) in respect of supplies made by RGL and SDG. IP 1 was paid to GUS plc, March UK and LL in several instalments between 15 March 2005 and 1 June 2005.

12. The trade of RGL was transferred to SDG on 25 November 2000. No document recording the terms of this transfer was available to us, and we had no evidence in that respect. We infer, and consequently find as a fact, that the whole of the trade was transferred, together with all rights and entitlements.

13. GUS plc and LL each paid the relevant amounts (including the amounts which appear to have been paid by HMRC to March UK) to SDG.

14. The background to the repayment being made to GUS plc is the sale, by agreement dated 27 May 2003, by GUS plc to March UK of a number of companies, including RGL and SDG (then called ARG Equation Limited). In that agreement the parties addressed the VAT issues that would arise on the sale and acquisition of the companies. Relevant extracts are as follows;

> (1) By clause 11 GUS plc agreed to procure that an application be made for the relevant companies, including RGL and SDG, to be excluded from the GUS plc VAT group with effect from completion, or at the earliest date following completion, in the latter case with corresponding payments between the new representative member of the GUS plc group and the relevant company to replicate so far as possible the position if the exclusion had taken effect on completion. There was agreed to be an information exchange to enable both the old and new VAT groups to make the necessary returns.
>
> (2) Schedule 5 to the Agreement contained a Tax Covenant. Under clause 11.7 of that Schedule it was provided that to the extent that they were not Accounts Reliefs (that is, according to clause S of Schedule 4 – Warranties, reliefs taken into account in computing and so reducing or eliminating any provision for tax in the balance sheet in the Final Completion Statement or which was taken into account in the Final Completion Statement as an asset), March UK was to pay to GUS plc VAT repayment amounts recovered from HMRC and interest in two specific cases:
>
> (a) catalogue charging; and
>
> (b) merchant charges.

[12] We refer throughout to HMRC, although at the material times certain of the payments were made by the formerly separate HM Customs & Excise.

(3) Clause 12 of Schedule 5 made provision for certain payments between GUS plc and March UK, and for March UK to procure certain payments from the relevant companies to GUS plc in respect of excesses of input tax and output tax respectively related to supplies made before completion.

15. No specific provision was made in relation to repayments of VAT that might fall to be made in respect of VAT overpaid on supplies made by the relevant companies, including RGL and SDG. That issue was subsequently raised in correspondence between March UK and GUS plc. Responding to letters of 1 and 15 April 2004 from Paul Atkinson, Head of Group Tax at GUS plc, in respect of Tax Covenant claims, VAT errors and agents' commission, Michael Seal, director of March UK, in a letter dated 20 May 2004, gave the following reply in relation to rights to VAT repayments:

> "Where there is any right to repayment of VAT, this should be claimed by ARG Equation Limited, (now Shop Direct Group Limited), in respect of any claim relating to the Shop Direct companies, or by GUS Plc in respect of any claim relating to the retained GUS companies. The only exceptions to this will be for any repayments relating to the claims in respect of catalogue charging and merchant charges, which can be paid direct to GUS Plc to the extent they are not provided for in the Final Completion Statement. You will recall these were the only two matters which you and I negotiated should be for the benefit of GUS Plc."

In that respect, Mr Seal continued:

> "… we would be happy to write a joint letter to Customs confirming this process, and agreeing to the relevant repayments for non-acquired companies being made to the new representative member, GUS Plc, despite the fact that Shop Direct Group Limited is due the refund under the provisions of section 80 VATA 1994."

16. It appears that, and there was no dispute on this, Mr Seal's statement regarding the entitlement under s 80 VATA of SDG to the repayment was incorrect. SDG had made no payment to HMRC in respect of the relevant VAT, and so could not have been due a refund under s 80.

17. The issue of entitlement to repayments of VAT in respect of agents' commission was dealt with by Mr Seal as follows:

> "… my clear recollection of our negotiations is that you only preserved for GUS Plc benefit the two VAT matters referred to in paragraph 4(d) above [catalogue charging and merchant charges]. Although the compliance mechanism may allow you to utilise group relief, it was neither agreed nor intended that GUS plc should benefit from such claims. Clearly, if as a consequence of such group relief, GUS plc does benefit then appropriate compensation should be paid to MUK [March UK]."

18. Mr Seal's proposals regarding the right to repayment of VAT were accepted by GUS plc in a letter dated 6 January 2005 from Paul Atkinson to Bob Dillea, Group Tax Manager at Littlewoods Home Shopping Limited, subject to credit being given

for overprovisions under clause 10 of the Tax Covenant. The position was formally confirmed subsequently in a letter agreement dated 4 October 2006 between March UK, GUS plc and Home Retail Group plc (to which we shall refer in more detail later) where it is stated that:

> "It has been previously agreed between GUS and ourselves [March UK] that any refunds or other repayments in respect of VAT (and any related interest) repaid and/or repayable by HM Revenue and Customs in respect of agents' own commissions (the 'VAT Repayments') belong to, and will be paid over to, the companies we acquired from GUS under the sale agreement dated 27 May 2003 (the 'SPA'), irrespective of the periods to which the VAT Repayments relate. GUS agreed to procure that all those repayments are paid over to us, and has done so previously in respect of VAT Repayments to date."

19. It appears from this that the negotiations at the time of the Agreement, and the drafting of clause 11.7, had proceeded on the basis that any relevant VAT repayments would be made to March UK or to another member of the March UK group. That would explain why provision was made for certain payments (those relating to catalogue charging and merchant charging) to be made by March UK to GUS plc, and no provision for any such payments in the opposite direction. What is also clear from Mr Seal's comments, and Mr Atkinson's acceptance of the position, is that the parties recognised the distinction between the issue of entitlement and the issue of payment mechanics. Even though GUS plc might receive the payment as representative member, the benefit was accepted as belonging to the appropriate companies acquired by March UK.

20. It is, we consider, particularly worthy of note that this was the position arrived at by independent parties acting at arm's length following the sale by Gus plc to March UK. If there had been any doubt as to the entitlement or ownership of what were considerable sums in repayments of VAT, we consider that GUS plc would have resisted the claims made by March UK in this respect.

21. It is, we think, appropriate at this point to consider the legislative background to the mechanism for repayment of VAT in the case of a VAT group. Section 80(1) of the Value Added Tax Act 1994 ("VATA") provides that where a person has paid an amount to HMRC by way of VAT which was not VAT due to them, HMRC shall be liable to repay the amount to that person. HMRC is not liable to pay any overpaid amount except as provided by s 80 (s 80(7)). Section 78(1) makes similar provision regarding interest: such interest is payable to the person who has accounted to HMRC for the amount which HMRC are liable to repay.

22. The need for repayments of VAT to go to the person paying the overpaid amount, and interest to be paid to the person accounting for the overpayment must, in the context of a VAT group, be considered with reference to s 43 VATA. Under that section any business carried on by a member of the group is treated as carried on by the representative member, and any supply of goods or services by or to a member of the group is treated as a supply by or to the representative member. However, all

members of the group are jointly and severally liable for any VAT due from the representative member.

23. To understand the consequences of group registration, we were taken to the decision of the VAT Tribunal in *Thorn PLC v Customs and Excise Commissioners* (No 15283). The tribunal set out the obligations of the company designated as representative member; that company is required to make returns in relation to all supplies of group companies treated by s 43 as made by the representative member, and as such it is the person whom HMRC are empowered to assess where, for example, a return is incomplete or inaccurate.

24. The argument in *Thorn* was whether an assessment could be made on a successor representative member that was not the representative member at the time the relevant supplies were made (and indeed had not been in existence at that time), or whether the assessment had to be made on the company that was the representative member at the time of the supplies. The tribunal held that while a group subsists the expression "representative member" applies to whichever company is currently undertaking that role, disregarding any changes there may have been in the identity of the representative member. The successor representative member was accordingly properly assessed.

25. Mr Goldberg referred us to the alternative argument raised by the Crown in *Thorn*. This was that the representative member acts in a representative capacity, and so HMRC have power to assess a representative member on an amount of VAT due from another member of the group by virtue of s 73(1) and (5) VATA. The tribunal rejected this argument, holding that the representative member is not a representative in the sense of being an agent or trustee for the other members of the group. The representative member has the statutory role conferred by s 43; that role is distinct from the legal roles – personal representative, trustee in bankruptcy, liquidator amongst others – contemplated by s 73(5).

26. Mr Goldberg invited us to conclude from this that, although the representative member has statutory rights and duties, it does not have any common law rights and duties. In particular, he argued, it activities did not give it common law rights or obligations to the other members of the VAT group. Mr Gammie argued that all that *Thorn* could be taken to have decided in this respect was that the effect of the statutory provision is not to give rise to a legal capacity in the nature of those set out in s 73(5).

27. We agree with Mr Gammie. We accept, as he argued, that the statutory regime imposed by s 43 does not inhibit the relationship as between the representative member and other group members regarding contributions from one to another, or as regards amounts recovered by the representative member and then accounted for to the members of the group. What rights in this respect exist between the representative member and other group companies is a question to be determined in the circumstances and on the available evidence in each case.

28. By letter dated 25 November 2004 from HMRC to Mr R Mitchell, VAT manager of Littlewoods Limited, HMRC advised that in relation to Shop Direct Limited (which, because it is referred to as previously having been called ARG Equation Limited, must be a reference to SDG), since the claims related to a company that was a member of the existing GUS plc VAT group for the VAT periods in question, albeit with a different representative member, the overpaid VAT would be repaid to "this VAT group", meaning to GUS plc as the representative member of the group. HMRC made it clear that the fact that GUS plc no longer had any connection with SDG was irrelevant.

29. So it was that in February and May 2005, GUS plc received that part of VRP 1 that related to supplies by RGL and SDG up to 27 May 2003, and on 6 June 2005 received IP 1 in respect of interest. These amounts were paid to SDG by direction of March UK. In respect of supplies after 27 May 2003, repayments were made to March UK and to LL. LL paid those amounts to SDG.

30. We must determine, from the available evidence, what arrangements can be found to exist between group members at the relevant time, whether any such arrangements gave rise to any entitlement in SDG, and if so the nature of that entitlement. We were shown no documentary evidence of the internal group payments arrangements. But we were taken to a witness statement of Neil Griffin, who at the material time was Group VAT manager of GUS plc, which had been served in connection with claims of Littlewoods Retail Limited and others in the High Court in 2009. In that statement Mr Griffin referred to the group treasury function of the GUS group which essentially managed the cash-flow of the group. In this connection he recollects that at the end of each day cash balances of all businesses within the GUS group were pooled and interest was paid or received on the net balance.

31. Mr Griffin's statement went on to say that the representative member would make one single payment to HMRC for the GUS VAT group's VAT liability. On the same day it processed intercompany transactions to reflect the relevant debit or credit balance in the accounts of the individual operating companies within the VAT group. At the end of each accounting period, intercompany settlements were made, such that funds were transferred by the operating companies to the representative member in respect of the sums paid by the latter on their behalf. The settlements received from these other companies would be in the amounts shown on their internal VAT returns.

32. In our view, within a group, when payments are made there may be no clarity as to the legal status of those payments at a particular time, or whether they are made by reference to specific legal rights. But that does not mean that, as between members of a group, payments that are made in the absence of an identifiable right are necessarily in the nature of gifts. We do not regard the intercompany payments to which Mr Griffin referred in his statement as gifts from the operating companies to the representative member. We had no other evidence as to the manner in which the GUS group operated its treasury function. Where no identifiable right exists, but a payment is made, it will often be the case that such a payment recognises an obligation, on the one hand, and an entitlement on the other.

33. We agree with the submission of Mr Gammie that the obvious way in which groups of companies will approach the issue of accounting for VAT is for the companies that (ignoring the group fiction) make the supplies to fund the payment of VAT by the representative member, and to account for those payments in their own individual accounts. The corollary to that is that repayments of overpaid VAT will be expected to flow in the opposite direction. For all purposes other than VAT, the group companies are individual companies in their own right, and, if they operate in a commercial manner, would be expected to ensure that any depletion of their assets as a consequence of the overpayment of VAT would be redressed by receipt of the corresponding repayment.

34. In the case of the payments of amounts equal to part of VRP 1 and IP1 by GUS plc to SDG, at the direction of March UK, we find that these were not gifts by GUS plc, but a payment in recognition of the position, accepted as between independent parties acting at arm's length, that the right to the repayments belonged to SDG. That acceptance can be explained only by the fact that the repayments related to the supplies made in the trade of SDG and the trade of RGL which was transferred to SDG on 25 November 2000.

35. We find also that the payments made by LL to SDG were not in the nature of gifts. There is no evidence of the repayments of VAT to LL being regarded as an asset of LL. They were not treated as such in LL's accounts. Nor is there any evidence that LL chose to give away amounts equal to the relevant part of VRP 1 and IP 1 rather than investing those amounts by way of equity or loan or making distributions. If these amounts had been paid to SDG by way of gift, we would expect to have seen clear evidence in the accounts of LL of ownership of the relevant sums, and minutes showing the making of a gift or capital contribution. The natural implication is that LL as the representative member immediately passed the payment to SDG as the company accepted by the group to be entitled to it, as beneficial owner, and we so find.

VRP 2 and IP 2

36. The facts surrounding VRP 2 and IP 2 are somewhat more complex. VRP 2 and IP 2 were paid by HMRC on 19 September 2007 to Weil, Gotshall & Manches ("WGL") as agent of Argos Ltd. Like VRP 1, VRP 2 was an ACR repayment. It related to VAT overpaid by GUS Merchandise Corporation Limited and Kay & Company Limited in relation to supplies made by Kay & Company, Abound Limited, SDG, GUS plc and RGL. WGM paid an amount equal to VPR 2 and IP 2 to a parent company of SDG (LW Corporation Limited) at the direction of March UK, and these amounts were recognised in the accounts of SDG by means of an inter-company receivable due from LW Corporation.

37. We need to review the history of the transfers of trades into, and ultimately out of, SDG. The first such transfer was of the trade of SDG (then called John Noble Limited) to RGL (at that time called GUS Catalogue Order Limited). This took place on 1 June 1991, but we did not have a copy of any agreement or transfer. We infer,

and accordingly find, that the whole of SDG's, trade, together with all relevant rights, was transferred to RGL on that date.

38. RGL changed its name from GUS Catalogue Order Limited to GUS Home Shopping Limited on 1 April 1996. By an agreement of the same date it acquired the business of GUS plc. That agreement made certain special provision regarding amounts recoverable in respect of taxation. The Debts were included, by clause 2(B)(vii), in the sale of the Business, but the expression Debts was defined so as to exclude "any amounts recoverable by [GUS plc] in respect of taxation paid or payable by [GUS plc] in connection with matters or events occurring on or before the Transfer Date".

39. On 1 April 1997 the trades of Kay & Company and Abound (then called Family Hampers Limited) were transferred to RGL. We had the agreement in relation to Kay & Company, dated 10 October 1997, but not that in relation to Abound, although the transfer of the Abound business was evidenced by board minutes of Family Hampers Limited on 10 October 1997. In the absence of evidence to the contrary, we find that the terms of the two agreements are more likely than not to have been materially identical.

40. In the Kay & Company agreement similar provision is made regarding Debts as in the earlier GUS plc agreement. In this case, Debts is also defined, but with specific reference to VAT: "… excluding any amounts recoverable by [Kay & Company] in respect of taxation (including without limitation Value Added Tax) paid or payable by [Kay & Company] in connection with matters or events occurring on or before the Transfer Date". VAT is also referred to in Clause 2.2.11, which contains a similar exclusion for recoverable tax in the "sweep-up" provision to include all other assets owned by Kay & Company in relation to the business. There was no evidence before us as to why there was an express reference to VAT in the Kay & Company agreement, but we note that at the Transfer Date (1 April 1997) Kay & Company was the representative member of the GUS VAT group, and so had the right as against HMRC to repayments of VAT in respect of that group. However, the agreement itself is dated 10 October 1997, by which time Kay & Company had ceased to be the representative member, and RGL occupied that position.

41. It seems to us that the intention of this provision in the agreement was to preserve for Kay & Company rights to repayment of VAT which Kay & Company had itself paid as representative member prior to 1 April 1997. Although at the Transfer Date it would have been Kay & Company that would have had the right, as representative member, to repayment from HMRC, the agreement excludes the transfer of that right to RGL. However, the agreement operates only to exclude a transfer; it does not provide for any indemnity or other mechanism whereby RGL must pay any amount in that respect to Kay & Company.

42. Mr Goldberg argued that the consequence of these provisions excluding recoverable tax, and recoverable VAT, was that, even if the transferor companies could be regarded as having any right to VRP 2 and IP 2 at the outset, that right had definitively not been transferred to RGL (and so could not itself have been transferred

by RGL to SDG when RGL's trade was transferred on 25 November 2000). Mr Gammie submitted that the exclusions are irrelevant to this case as the amounts were paid by mistake and so cannot be amounts recoverable in respect of VAT or taxation. He also submitted that the payments would have been amounts recoverable from the representative member and not from HMRC.

43. In this respect we agree with Mr Goldberg. Applying ordinary principles of construction (per Lord Hoffman in *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 All ER 98) we have to ascertain the meaning the agreements would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract. We must exclude previous negotiations of the parties and declarations of subjective intent, but we have no evidence of those. Applying this test, we do not consider that the parties intended any distinction to be drawn between repayments of tax and repayments of amounts mistakenly paid as tax. We find therefore that such rights as GUS plc, Kay & Company and Abound had at the time of the transfer to repayment of what became VRP 2 and IP 2 were not transferred to RGL along with the respective trades of those companies.

44. The trade of RGL was transferred to SDG on 25 November 2000, as we have described earlier. According to our finding above, this transfer, although it otherwise included all the assets of the trade of RGL, did not include the rights to VRP 2 and IP 2 which had been reserved to GUS plc, Kay & Company and Abound. It did, however, include RGL's own rights in respect of supplies made in the period from 1 April 1996 to 30 September 1996.

45. By an agreement dated 28 October 2005 the trade of SDG was transferred to SDHSL (then called Littlewoods Home Shopping Limited). By clause 2.2 of that agreement it was provided that:

> "The Assets comprised in the sale and purchase hereby agreed are all of the undertaking and the assets of the Vendor used wholly or mainly in the Shop Direct Home Shopping Business at the Effective Date including the Vendor's right and title, such as it has, in the following:
>
> …
>
> 2.2.8 all the Vendor's rights against third parties which relate to the Shop Direct Home Shopping Business or the Assets …"

46. The expression "Assets" is itself a defined term. Clause 1.1 provides that Assets means:

> "all the Vendor's rights and title in the undertaking and the assets owned by the Vendor and used wholly or mainly in the Shop Direct Home Shopping Business as more particularly described in clause 2.2 as reflected in the management accounts of the Vendor for the period ended 28 October 2005 excluding for the avoidance of doubt the Excluded Assets."

47. Mr Goldberg submitted that this agreement transferred all of SDG's remaining rights to VRP 2 and IP 2 to SDHSL, so that SDG did not, after 28 October 2005, when it ceased to trade, have any such rights. Mr Gammie argued that the agreement expressly excluded such rights, because the Assets had to be reflected in the management accounts of SDG for the period ended 28 October 2005. Given that VRP 2 was brought into account only in 2008, the only conclusion is that management accounts would not have reflected the right to VRP 2.

48. We do not have the benefit of the management accounts. Our own construction of the agreement is that it was important for the relevant assets to be identified in the management accounts, and that only assets that were so identified would have been transferred to SDHSL. This is because the consideration for the transfer of the Assets was the assumption by the purchaser of the liabilities, and it was agreed that the SDG would owe SDHSL, as an interest-free loan, repayable on demand, an amount equal to the excess of the liabilities over the book value of the Assets. We agree with Mr Gammie that the management accounts must be considered not to have included the value of the VAT repayments, and consequently no book value would be attributable to such a right. In our view, SDG would not have wished to incur indebtedness to SDHSL whilst at the same time transferring to SDHSL assets which, because they were not included in the management accounts, would not have reduced the amount of that indebtedness. Accordingly, we conclude that such rights as SDG had to payment of VRP 2 and IP 2 were retained by it and not transferred to SDHSL.

49. During the hearing HMRC produced some further documentation which, Mr Gammie submitted, demonstrated that the right to the payment of VRP 2 and IP 2 could not have been transferred to SDHSL. The documents comprised a deed of discharge and release ("the Argos Deed") dated 12 September 2007 addressed to HMRC and executed by Experian Finance PLC (formerly GUS plc) and Argos Limited (companies not connected to the Appellants), and extracts from some minutes of board meetings of certain companies in the Appellant group, namely SDG, RGL, Kay & Company, Abound and Littlewoods Company Director Limited.

50. The Argos Deed refers to a request that had been made to make payments in accordance with Business Brief 113/06 to SDG, including amounts which HMRC had accepted, subject to final resolution of the *Fleming* and *Condé Nast* appeals, had been overpaid by companies which were at the relevant times members of the Argos VAT group. The deed records that HMRC had agreed to make the relevant payment to SDG on condition that it received an undertaking from SDG to repay the amount in certain circumstances, backed by a bank guarantee, and releases from Experian and Argos, and also from RGL, Kay & Company and Abound, which companies, the deed recites "HMRC have been informed became entitled to receive from HMRC any repayment pursuant to the [relevant repayment claims] when the GUS home shopping business was sold to March UK…". The board minutes of the various companies show that deeds of discharge and release consistent with the condition under the Argos Deed were approved and authorised to be executed, but we did not see any evidence of those deeds themselves.

51. The board minutes of SDG refer to the undertaking from that company in favour of HMRC, and the bank guarantee. They also make reference to a deed of appointment whereby WGM was to be appointed as agent of SDG to receive the relevant payment. All these documents were considered and approved for execution by SDG.

52. We have found, on our construction of the agreement for the transfer of SDG's trade to SDHSL, that SDG retained such rights to VAT repayments as it had at that time, which would exclude the rights which were retained by GUS plc, Kay & Company and Abound. We are not persuaded that the reference to companies, including Kay & Company and Abound, becoming entitled to receive certain payments from HMRC is indicative of the creation of an entitlement only at the stage of the sale of the home shopping business. The Argos Deed says nothing about the entitlement of those companies as against other companies, including Argos Limited and March UK. It deals only with the entitlement to receive payments from HMRC which, as we have seen, as a statutory matter could be paid only to the representative member. What this deed appears to demonstrate is that HMRC had been persuaded that it could pay WGM as agent for SDG, and that HMRC had agreed this course but only if it had protection against claims that might otherwise be made by companies claiming to be themselves entitled.

53. To the extent that the Argos Deed tells us anything, we consider that it supports our analysis of the agreements for the transfers of the trades of Kay & Company and Abound to SDG, and the transfer of the trade of SDG to SDHSL. The deed recognises rights in Kay & Company and Abound, but does not refer to any such rights in SDHSL.

54. Mr Goldberg also referred us to a passage in *Littlewoods Retail Ltd and others v Revenue and Customs Commissioners* [2010] STC 2072 which relates to the assignment to SDG by representative members of the GUS plc group of claims to compound interest. Those assignments were made on 6 May 2008, so after the payments of VRP 2 and IP2 (see [20]). Mr Goldberg argued that this demonstrated that the parties themselves considered that such an assignment was necessary, and that SDG at the time of VRP 2 and IP 2 did not have the right to those payments. We do not consider that the fact of these assignments assists the Appellants. All they show is that the group recognised, as was common ground in that case (see [22]), that where a representative member had paid the tax, that company was the correct claimant as a matter of law. It is evident, however, that the group itself was of the view, in common with the position it had adopted in relation to VRP 1 and IP 1, and VRP 2 and IP 2, that the real beneficiary, as between members of the group, was SDG, and that it was right therefore for the claims to be assigned to SDG. In our view, therefore, this supports a conclusion that SDG was, as far as the group was concerned, entitled to the relevant payments.

55. We earlier considered, in relation to VRP 1, the agreement dated 27 May 2003 whereby GUS plc sold a number of companies, including SDG, to March UK. We explained how this resulted in GUS plc receiving VRP 1 from HMRC, the acceptance by GUS plc and March UK that the VAT repayments belonged to the relevant

acquired companies and the arrangements made whereby VRP 1 was paid by GUS plc to SDG by direction of March UK.

56. Following that sale there was a proposal for the GUS group to be split, with GUS plc going into a separate and independent group from the ARG companies (including Argos Limited). This would have resulted in the VAT repayments being made by HMRC to the new representative member, within the ARG group, and no longer to GUS plc. The arrangements for payment by GUS plc would no longer operate.

57. That was the background to the letter agreement dated 4 October 2006 between March UK, GUS plc and Home Retail Group plc ("HRG"), the putative holding company of Argos plc, to which we referred earlier. As well as confirming the earlier agreement that the rights to VAT repayments and associated interest belonged to the March UK acquired companies, the letter agreement obliged HRG to procure that Argos Limited would irrevocably appoint WGM (the lawyers) as its agent to receive VAT repayments, and to pay the amount to March UK. March UK agreed to repay to HMRC any amount found to have been paid in error. Subsequently, on 9 October 2006, a deed poll was entered into by Argos Limited and HRG appointing WGM as agent to receive the relevant VAT repayments and related interest. This arrangement was notified by Argos Limited to HMRC by fax dated 10 October 2006.

58. VRP 2 and IP 2 were paid to WGM on 19 September 2007. That date is shortly after the date of the Argos Deed, and we conclude therefore that the payment was made after the Argos Deed had been executed and the other conditions had been satisfied.

59. It is an agreed fact that, on receipt of VRP 2 and IP 2 by WGM, amounts equal to those payments were paid to LW Corporation Limited at the direction of March UK, and the amount was recognised in the accounts of SDG by means of an inter-company receivable. The Argos Deed, on the other hand, and the relevant board minutes of SDG, evidence that, as well as WGM being the agent for Argos plc (by that time Argos Limited), that firm was also at the same time agent for SDG. In those circumstances there would have been no need for there to have been any direction by March UK.

60. Although the facts surrounding VRP 2 and IP 2 are more complex than those relating to VRP 1, in our view the analysis is materially the same. In our view, as between March UK and SDG there was an acknowledgement by March UK, in its agreements with GUS plc and HRG, that SDG was entitled to VRP 2 and IP 2. We find that the Argos Deed was executed, and the other conditions were satisfied, along with the appointment by SDG of WGM as its agent to receive the payment of VRP 2 and IP 2, as part of the administrative arrangements for the receipt of these payments from HMRC. If any direction was in fact required to be given by March UK, this was purely an administrative function, March UK being merely a conduit as part of the administrative arrangements. There is no evidence that March UK was at any time itself beneficially entitled to the payments, and we are satisfied that March UK did not make a gift to SDG. Nor of course was there any gift by Argos Limited.

61. March UK regarded SDG as entitled to the payment in respect of the overpayments, and consequent depletions in the assets of, the trades formerly carried on by SDG, including those transferred by GUS plc, Kay & Company, Abound and RGL. Any rights to VRP 2 and IP2 that were retained as at 1 April 1997 by GUS plc, Kay & Company and Abound on the transfers of the respective trades and assets to RGL could not at that time have been rights against RGL, which became the representative member of the group only on 7 August 1997, nor were they rights against SDG. Furthermore, whilst on 1 April 1997 it would have been Kay & Company that had the right, as representative member at that time, to repayment from HMRC of VRP 2, it had ceased to be representative member on 6 August 1997 and no longer had that right at the time of the repayment itself. At the time of the repayment, the only right that GUS plc, Kay & Company and Abound could have had in that respect was a right against the then representative member, Argos Limited. Any claim by any of those companies against SDG would therefore have to have been a claim in restitution. SDG accordingly received VRP 2 and IP 2 as beneficial owner at the time of receipt and was entitled to bring those payments into its own accounts as an exceptional item in relation to VAT and related interest.

62. Nor does the fact that payment was made to LW Corporation affect the question of SDG's entitlement, as owner, to VRP 2 and IP 2. The payment by WGM is readily explained by the fact that, at the material time WGM was, under the Argos Deed, acting as agent for SDG as well as for Argos Limited. The payment to LW Corporation merely reflected the loan that was made by SDG to LW Corporation, acknowledged as such by the creation of the inter-company receivable. Such a loan could not have been made by SDG were it not the beneficial owner of the relevant amount.

Shop Direct Home Shopping Limited ("SDHSL")

63. SDHSL received two VAT repayments (VRP 3 and 4) and two related interest payments (IP 3 and 4).

64. The claim to VRP 3 was made on 5 February 2002 and VRP 3 was paid by HMRC to LL on 24 January 2005. IP 3 was paid to LL in two tranches on 17 February 2005 and 28 February 2005. The VAT repayment was an ACR, which arose in respect of VAT overpaid by LL in respect of supplies made by LRL in the period from January 1999 to April 2003 and SDHSL in the period from 1 May 2003 to 25 September 2004.

65. The home shopping business of LRL was transferred to SDHSL (then called Littlewoods Home Shopping Limited) with effect from 4 May 2003 under an agreement dated 30 April 2003. The agreement transferred all the assets of the business, with the exception of certain Excluded Assets, none of which related to taxation. Debts were specifically transferred without any exclusion of repayments of tax, including repayments consequent upon the outstanding claim for VRP 3.

66. LL paid VRP 3 and IP 3 to SDHSL, which recorded the payments in its profit and loss account.

67. There is no evidence that the payments of VRP 3 and IP 3 to SDHSL were by way of gift by LL, and we find that they were not. They were paid to SDHSL as the company carrying on its own trade and the home shopping business formerly carried on by LRL from which the supplies had been made that gave rise to the right to repayment of VAT. We find that, within the group, SDHSL was beneficially entitled to those payments

68. VRP 4 and IP 4 were paid by HMRC to WGM as agent of LL on 30 August 2007. VRP 4 was an ACR, arising out of VAT overpayments over the period 1 January 1978 to 31 December 1986 made by six separately-registered companies, Brian Mills Limited, Burlington Warehouses Limited, Janet Frazer Limited, John Moores Home Shopping Service Limited, Littlewoods Warehouses Limited and Peter Craig Limited ("the Six Companies"), and in the period from 1987 to September 1996 by LL in relation to supplies by the Six Companies and LRL.

69. The trades of the Six Companies were transferred to LRL on 1 January 1993. It was accepted by the parties that this transferred the whole of those trades and all assets. The home shopping business of LRL, along with all the assets of that business, was later transferred to SDHSL, as previously described.

70. As agent for LL, WGM paid VRP 4 and IP 4 to SDHSL, which recorded the payments in its profit and loss account as an exceptional item.

71. There is no evidence that the payments of VRP 4 and IP 4 to SDHSL were by way of gift by LL, and we find that they were not. They were paid to SDHSL as the company carrying on its own business, and as the successor to the trades of the six Companies and the home shopping business of LRL, from which the supplies had been made that gave rise to the right to repayment of VAT. We find that SDHSL was beneficially entitled to those payments.

Reality Group Limited ("RGL")

72. RGL received VRP 5. The payment was made by HMRC to RGL, the representative member of the relevant VAT group at the time, in May 1998. It related to VAT overpaid by Kay & Company in respect of supplies made by Abound, Kay & Company and RGL itself in the period from 1 March 1996 to 28 February 1997. The overpayment arose because of an error by HMRC in charging VAT on a supplier's debtor balances as at 28 February 1997, when the standard method of calculating gross takings (SMGT) was withdrawn.

73. We have considered earlier the agreement whereby the trade of Kay & Company was transferred to RGL on 1 April 1997, and we have inferred that the terms of the agreement transferring the trade of Abound to RGL on the same date were materially the same. We have held, on our construction of the Kay & Company agreement, that the rights of those companies to repayments of tax, including any right to VRP 2, were not transferred to RGL. The same finding must therefore follow in relation to any rights to VRP 5.

74. Nevertheless, our analysis of the position of VRP 2 in relation to SDG is equally applicable to the position of VRP 5 and RGL. Any rights to VRP 5 that were retained as at 1 April 1997 by Kay & Company and Abound on the transfers of their respective trades and assets to RGL could not at that time have been rights against RGL. The Kay & Company agreement merely excluded those rights from the sale and did not impose any obligation on RGL, by way of indemnity or otherwise, to make payments in those respects to Kay & Company, and we infer that the same was true for the Abound agreement. It was entirely consistent therefore for the group to have considered that RGL was entitled to the payments, not only as a matter of mechanics as the representative member, but as the company carrying on its own business and as successor to the businesses of Kay & Company and Abound against which the VAT had been wrongly charged. No claims were made by Kay & Company or Abound, and if such claims had been made they would, in our view, have to have been restitutionary claims. RGL accordingly properly treated the payment as belonging to it and brought it into account as an exceptional item within cost of sales in its profit and loss account. We find that RGL was entitled to VRP 5 as beneficial owner of that amount, and not merely as representative member.

Littlewoods Retail Limited ("LRL")

75. LRL received three VAT repayments (VRP 6, 7 and 8) and three corresponding interest payments (IP 6, 7 and 8).

76. VRP 6 was paid by HMRC to LL on 22 November 1995 and 20 December 1995, and IP 6 was paid to LL on 27 December 1995 and 12 January 1996. The VAT payment was in relation to overpaid VAT attributable to the wrongful charging of VAT on debtor balances, outstanding in respect of credit sales on increases in the VAT rate. The overpayments had been made by the Six Companies and LL in respect of supplies made by the Six Companies in the period 18 June 1978 to 31 March 1991.

77. We have described the transfers to LRL of the trades of the Six Companies on 1 January 1993. Those transfers are accepted as having included all the assets of those businesses.

78. LL paid to LRL an amount equal to VPR 6 and IP 6, and those amounts were accounted for by way of a credit entry shown in cost of sales in LRL's profit and loss account.

79. In common with our earlier findings, we find that the payments by LL to LRL in respect of VRP 6 and IP 6 were not by way of gift, but were paid to LRL as successor to the trades of the Six Companies, from which the supplies had been made that gave rise to the VAT repayment. We find that LRL was beneficially entitled to those payments.

80. Each of VRP 7 and VRP 8, along with their associated interest payments (IP 7 and 8), were paid to LL in relation to VAT overpaid by LL in respect of supplies made by LRL. VRP 7 was an SMGT overpayment; VRP 8 is agreed to be "similar to" an ACR. LL paid the respective amounts to LRL. These amounts were not disclosed in

LRL's accounts, but were included in the tax computations as a credit to profit and loss account in the case of VRP 7 and IP 7 and as an income adjustment in the case of VRP 8 and IP 8.

81. For the reasons we have given in our analysis of other VAT repayments and interest payments, we find that these payments by LL to LRL were not by way of gift, but were paid to LRL in respect of its own trade from which the supplies which gave rise to the VAT repayments had been made. We find that LRL was beneficially entitled to those payments.

The law

82. The starting point for consideration of the corporation tax position of each of the Appellants is the statutory regime. We set out the relevant extracts below. We are concerned here with a number of accounting periods, spread over a considerable period, from 1 January 1995 to 30 April 2008. Certain legislative changes have been made over that time, and we will note those changes that are material. Otherwise we shall refer to only one version of each statutory provision. In each case we refer to provisions in force before the Corporation Tax Act 2009.

83. Section 6(1) of the Income and Corporation Taxes Act 1988 ("ICTA") provides that corporation tax shall be charged on profits of companies, and under s 8 a company is chargeable to corporation tax on all its profits wherever arising. Corporation tax is assessed and charged for any accounting period of a company on the full amount of the profits arising in the period (s 12).

84. Section 18 ICTA as it applied for tax year 1995-96 sets out the relevant provisions relating to Schedule D, Cases I, II and III:

> "(1) The Schedule referred to as Schedule D is as follows:-
>
> SCHEDULE D
>
> Tax under this Schedule shall be charged in respect of –
>
> (a) the annual profits or gains arising or accruing –
>
> …
>
> (ii) to any person residing in the United Kingdom from any trade, profession or vocation, whether carried on in the United Kingdom or elsewhere,
>
> …
>
> (b) all interest of money, annuities and other annual profits or gains not charged under Schedule A, C or E, and not specially exempted from tax.
>
> (2) Tax under Schedule D shall be charged under the Cases set out in subsection (3) below, and subject to and in accordance with the provisions of the Tax Acts applicable to those Cases respectively.
>
> (3) The Cases are –

> Case I: tax in respect of any trader carried on in the United Kingdom or elsewhere …
>
> …
>
> Case III: tax in respect of-
>
> Any interest of money, whether yearly or otherwise, …
>
> …
>
> Case VI: tax in respect of any annual profits or gains not falling under any other Case of Schedule D and not charged by virtue of Schedule A, C and E."

85. The Case III set out in the previous paragraph is relevant only to the issue of the taxation of IP 6. The Finance Act 1996 introduced a separate code for loan relationships. From tax year 1996-97, and accordingly for all other interest payments which are the subject of this appeal, this resulted in the substitution of a different Case III of Schedule D for corporation tax purposes. The applicable Case III in those circumstances is:

> "Case III: tax in respect of –
>
> (a) Profits and gains which, as profits and gains arising from loan relationships, are to be treated as chargeable under this Case by virtue of Chapter II of Part IV of the Finance Act 1996; …"

86. To a significant extent the payments received by the Appellants were related to overpayments of VAT in trades that had ceased to be carried on by the companies engaged in the trades at the time the VAT was overpaid. We have also considered earlier the analysis of what rights to repayments may be taken to have been transferred, or not transferred, on the various business transfers. To those extents argument centred around the special rules that apply to receipts after a discontinuance, and the provisions that apply where rights to payments were transferred. The relevant sections are s 103 and s 106 ICTA, which provide (so far as material):

> "**103 Receipts after discontinuance: earnings basis charge and related charge affecting conventional basis**
>
> (1) Where any trade, profession or vocation the profits of which are chargeable to tax under Case I or II of Schedule D has been permanently discontinued, tax shall be charged under Case VI of that Schedule in respect of any sums to which this section applies which are received after the discontinuance.
>
> (2) Subject to subsection (3) below, this section applies to the following sums arising from the carrying on of the trade, profession or vocation during any period before the discontinuance (not being sums otherwise chargeable to tax)—
>
> (a) where the profits for that period were computed by reference to earnings, all such sums in so far as their value was not brought into account in computing the profits for any period before the discontinuance, and

(b) where those profits were computed on a conventional basis (that is to say, were computed otherwise than by reference to earnings), any sums which, if those profits had been computed by reference to earnings, would not have been brought into the computation for any period before the discontinuance because the date on which they became due, or the date on which the amount due in respect thereof was ascertained, fell after the discontinuance."

"**106 Application of charges where rights to payments transferred**

(1) Subject to subsection (2) below, in the case of a transfer for value of the right to receive any sum to which section 103, 104(1) or 104(4) applies, any tax chargeable by virtue of either of those sections shall be charged in respect of the amount or value of the consideration (or, in the case of a transfer otherwise than at arm's length, in respect of the value of the right transferred as between parties at arm's length), and references in this Chapter, except section 101(2), to sums received shall be construed accordingly.

(2) Where a trade, profession or vocation is treated as permanently discontinued by reason of a change in the persons carrying it on, and the right to receive any sum to which section 103 or 104(1) applies is or was transferred at the time of the change to the persons carrying on the trade, profession or vocation after the change, tax shall not be charged by virtue of either of those sections, but any sum received by those persons by virtue of the transfer shall be treated for all purposes as a receipt to be brought into the computation of the profits of the trade, profession or vocation in the period in which it is received."

87. Section 110 contains supplemental interpretive provisions. Of relevance here is the provision of s 110(2)(a) that for section 103 purposes any reference to the permanent discontinuance of a trade includes a reference to any event which, under s 337(1) ICTA, is to be treated as equivalent to the permanent discontinuance of a trade. Section 337(1) provides as follows:

"Where a company begins or ceases to carry on a trade, or to be within the charge to corporation tax in respect of a trade, the company's income shall be computed as if that were the commencement or, as the case may be, discontinuance of the trade, whether or not the trade is in fact commenced or discontinued."

88. Section 42 of the Finance Act 1998 contains provisions, which are regarded as essentially codifying then existing law, concerning the relationship between tax on trading profits and accounts. This extract shows s 42(1) as originally enacted, and as amended by FA 2002 with effect from 24 July 2002:

"For the purposes of Case I or II of Schedule D the profits of a trade, profession or vocation must be computed [on an accounting basis which gives a fair view] [2002: in accordance with generally accepted accounting practice], subject to any adjustment required or authorised by law in computing profits for those purposes."

89. We noted earlier that FA 1996 introduced the loan relationships code for corporation tax. Section 81(1) sets out what is meant by a "loan relationship":

> "Subject to the following provisions of this section, a company has a loan relationship for the purposes of the Corporation Tax Acts wherever –
>
> (a) the company stands (whether by reference to a security or otherwise) in the position of a creditor or debtor as respects any money debt; and
>
> (b) that debt is one arising from a transaction for the lending of money."

90. A "money debt" is a debt which is, or has at any time been, one that falls, or that may at the option of the debtor fall to be settled either by the payment of money, or by the transfer of a right to settlement under a debt which is itself a money debt (FA 1996, s 81(2)).

91. None of the payments of amounts in respect of interest in these appeals arise from a transaction for the lending of money. However, HMRC argue that the payments fall within s 100 FA 1996, which, in relation to the bringing into account of interest, assimilate certain relationships that do not arise from the lending of money to loan relationships:

> **100 Interest, and exchange gains and losses, on debts etc not arising from the lending of money**
>
> (1) For the purposes of the Corporation Tax Acts, a company has a relationship to which this section applies in any case where—
>
> (a) the company stands, or has stood, in the position of a creditor or debtor as respects a money debt;
>
> (b) the money debt is not one which arose from a transaction for the lending of money (so that, in consequence of section 81(1)(b) above, there is no loan relationship); and
>
> (c) the money debt is one—
>
> (i) on which interest is payable to or by the company; or
>
> (ii) in relation to which exchange gains or losses arise to the company;
>
> and references to a relationship to which this section applies, and to a company's being party to such a relationship, shall be construed accordingly.
>
> (2) Where a company has a relationship to which this section applies—
>
> (a) this Chapter shall have effect in relation to the interest payable under, or the exchange gains or losses arising to the company from, the relationship as it has effect in relation to interest payable under, or (as the case may be) exchange gains

> or losses arising to the company from, a loan relationship to which the company is a party; but
>
> (b) the only credits or debits to be brought into account for the purposes of this Chapter in respect of the relationship are those relating to the interest or (as the case may be) to the exchange gains or losses;
>
> and, subject to paragraph (b) above, references in the Corporation Tax Acts to a loan relationship accordingly include a reference to a relationship to which this section applies.

Discussion

92. There are two primary issues with which we are concerned in this appeal. Firstly, there is the question whether the VAT repayments arise from a trade and are accordingly trading receipts, and if so whether the Appellants are liable to tax on those amounts either directly, as the person carrying on the trade, under Case I of Schedule D, or under the rules governing post-cessation receipts, in that case under Case I or Case VI. Secondly, there is an issue whether the interest payments are taxable under Case III by virtue of the loan relationships provisions (or, in the case of IP 6, under Case III as it applied before FA 1996), or otherwise under Case VI. If the interest payments are not taxable under any of these provisions, HMRC also argue that those payments can be taxed under Case I as trading receipts in the same way as the VAT repayments.

Accounting treatment

93. We consider first the application of s 42 FA 1998 in the context of the fact that, in each case, the Appellant accounted for the receipts as credits in its profit and loss account (evidenced, in the case of VRP 7 and IP 7, by LRL's tax computations; in relation to VRP 8 and IP 8 the relevant amounts were described in LRL's tax computations as an "income adjustment").

94. In our view, s 42 cannot determine the question whether a profit is a trading profit. That question must be determined in accordance with the statutory provisions and established authorities before s 42 can operate in respect of the computation of those profits. The mere fact that a receipt has been accounted for as a trading profit does not determine the question whether it is taxable as such; but once that threshold question has been determined so that there is a trading receipt, the trading profits must then be computed in accordance with generally accepted accounting practice, subject to any adjustments required or authorised by law.

95. In this respect we agree with the tribunal in *Pertemps Recruitment Partnership Ltd v Revenue and Customs Commissioners* [2010] SFTD 882 when it said at [32]:

> "We note that s 42 FA [1998] applies for the purposes of Sch D, Case I to compute the amount of profits. However the first step is to determine the nature of the receipt—does it fall within Case I in the first place? Only if it does, is s 42 brought into action to determine the amount that is brought into account as profits."

96. We also agree with the submission made by counsel for *Pertemps* in the Upper Tribunal [2011] SC 1346, at [88] that what the tribunal had said correctly recognised the difference between the threshold question whether a receipt is a trading receipt and the subsequent question of how the profits were to be computed if it was. We note in this connection that Arnold J commented *obiter* (at [90]) that, having regard to the argument of Miss Wilson, representing HMRC, to the effect that the mistaken payments having been included in the accounts which gave a true and fair view and were in accordance with generally accepted accounting principles, those payments were properly to be regarded as trading receipts, he did not think it was clear that the tribunal had made a decision adverse to HMRC. But we do not consider Miss Wilson's argument in *Pertemps* to be correct.

Are the VAT repayments trading receipts?

97. We turn therefore to consideration of the issue whether the VAT repayments were trading receipts of the Appellant companies.

98. In this regard Mr Goldberg put his case by reference to four points of, as he described them, general principle. We shall set them out here, and then consider the respective arguments of Mr Goldberg and Mr Gammie in relation to each:

> (1) Where there is a statutory right to a sum of money and money is received pursuant to that right, the source of the money is the statute and not something else.
>
> (2) Whilst it is accepted that some receipts of a trader which are not directly derived from his basic trading activities may be regarded as trading receipts, in order for that to be so they must be paid to the trader for some specific trading purpose.
>
> (3) Where a recovery is attributable to a trading activity in an earlier period, and the profits of that earlier period have been correctly computed, it is inherently unlikely that the recovery can be taxed in a later period as a receipt of a trade.
>
> (4) Just because a sum is included in a company's accounts, it does not follow that it is liable to tax.

Proposition (1)

99. Mr Goldberg referred us to *Davis v Powell* [1977] STC 32, a case on capital gains tax. There a tenant farmer surrendered his lease of agricultural land in consequence of a notice to quit from his landlord. The landlord paid him statutory compensation for disturbance under s 34 of the Agricultural Holdings Act 1948. The tenant was assessed to capital gains tax on the compensation on the ground that it was a capital sum derived from an asset, namely the lease, and in particular was received in return for the surrender of rights.

100. In the High Court, on appeal from the general commissioners, Templeman J held that the compensation was not derived from an asset. He said (at p 35):

> "What is said in this case is that the taxpayer had a lease and that lease was an asset; it was property of some form. He disposed of that asset by accepting the notice to quit which was given and by getting out, and he derived a capital sum from the asset when he did so. The capital sum was the amount of the compensation under s 34, which, as I have said, was £591. It does not seem to me that the compensation paid under s 34 is derived from the asset, namely the lease. It is not derived from an asset at all: it is simply a sum which Parliament says shall be paid for expense and loss which are unavoidably incurred after the lease has gone."

101. *Drummond v Austin Brown* [1984] STC 321 was another case concerning capital gains tax. There the taxpayer gave up possession of certain business premises of which he was the tenant, and received compensation under s 37 of the Landlord and Tenant Act 1954. The taxpayer was assessed to capital gains tax on the footing that the payment constituted a capital sum derived from an asset (the lease) or, alternatively, that it was compensation for the loss of an asset. It was held by the Court of Appeal, following *Davis v Powell*, that the taxpayer's right to compensation on the termination of the lease was not derived from the lease. Giving the judgment of the court, Fox LJ said (at p 324):

> "In our opinion the £31,384 was not derived from the lease. The word 'derive' suggests a source. The right to the payment was, in our view, from one source only, namely the statute of 1954. The lease itself gives no right to such a payment. It was the statute, and the statute alone, which created the right to the payment. The statute simply created an entitlement where none would otherwise have existed. And in creating that entitlement it did not require that any provisions were to be written into the lease. Thus, there is no deeming provision which would in any way require one to treat the lease as being the source of the entitlement."

102. Mr Goldberg also took us to the headnote of *FJ Chalke Ltd and another v Revenue and Customs Commissioners* [2009] STC 2027, where, in a claim for compound interest on repayment of overpaid VAT, it was held that s 80(7) was clear and unambiguous in providing that the only basis on which HMRC were liable to repay overpaid VAT was by means of a claim under s 80(1). It left no room for the co-existence of other remedies for the recovery of overpaid VAT from HMRC. The interest claimed, whether simple or compound, could only be interest in respect of the VAT which was overpaid and which had been repaid, namely interest on the principal sums.

103. Except in the case of RGL, the amounts that are the subject of these appeals do not derive directly from HMRC, but were paid by, or at the direction of, the representative member which was itself entitled to be paid both the principal sums in respect of overpaid VAT, and interest on those sums. Payments made by, or on behalf of, the representative member do not have as their source the statute under which the payments have been made to the representative member.

104. RGL, on the other hand, received VRP 5 from HMRC as representative member of the relevant group. If Mr Goldberg's first proposition is correct, it would mean that

the source of the payment would not be the trades of Kay & Company, Abound and RGL itself, but only the statutory provision under which VRP 5 was paid, namely s 80(1) VATA.

105. We do not accept this proposition. The question is not under what legal machinery the payment is made, but what the payment was in substance for. The source of the right to the payment is part of the matrix of facts which will provide the answer to that question, but it is not itself decisive. That much, we consider, is clear from *London & Thames Haven Oil Wharves Ltd v Attwooll* 43 TC 491, to which Mr Gammie referred us.

106. That case concerned the question whether a payment of compensation for loss of use of a fixed asset used in the taxpayer's trade was chargeable to tax under Case I of Schedule D as a revenue receipt. The principles to be applied were explained by Diplock L J in the Court of Appeal (at p 515):

> "I start by formulating what I believe to be the relevant rule. Where, pursuant to a legal right, a trader receives from another person compensation for the trader's failure to receive a sum of money which, if it had been received, would have been credited to the amount of profits (if any) arising in any year from the trade carried on by him at the time when the compensation is so received, the compensation is to be treated for income tax purposes in the same way as that sum of money would have been treated if it had been received instead of the compensation. The rule is applicable whatever the source of the legal right of the trader to recover the compensation. It may arise from a primary obligation under a contract, such as a contract of insurance, from a secondary obligation arising out of non-performance of a contract, such as a right to damages, either liquidated, as under the demurrage clause in a charter-party, or unliquidated, from an obligation to pay damages for tort, as in the present case, from a statutory obligation, or in any other way in which legal obligations arise. But the source of a legal right is relevant to the first problem involved in the application of the rule to the particular case, namely, to identify what the compensation was paid for. If the solution to the first problem is that the compensation was paid for the failure of the trader to receive a sum of money, the second problem involved is to decide whether, if that sum of money had been received by the trader, it would have been credited to the amount of profits (if any) arising in any year from the trade carried on by him at the date of receipt, that is, would have been what I shall call for brevity an income receipt of that trade. The source of the legal right to the compensation is irrelevant to the second problem. The method by which the compensation has been assessed in the particular case does not identify what it was paid for; it is no more than a factor which may assist in the solution of the problem of identification. I will not again traverse the cases. They seem to me to be directed to the solution of one or other of these two problems, which are not always distinguished in the judgments. In the course of these judgments, different metaphors and similes (appropriate no doubt to the particular facts of the case) have been

> used. But I do not think that any of these conflict with the rule as I have expressed it."

107. In this case s 80 VATA operates to provide a means whereby overpayments of VAT may be recovered. That is a relevant factor in identifying why the payment has been made. The payment is made by virtue of the statute, but that does not determine the underlying source. That can only be determined by the answer to the further question, which is what in substance the payment is for. We do not consider that the cases on capital gains tax can assist the analysis, so clearly set out by Diplock L J.

Proposition (2)

108. Whilst accepting that some receipts of a trader which are not directly derived from his basic trading activities may be regarded as trading receipts, Mr Goldberg argued that those receipts must be paid to a trader for a specific trading purpose. He submitted that where a sum is recovered under a statutory or other right which is not of a kind which evinces any intention as to how the recovery is to be used, it cannot be a trading receipt. There is then no nexus between the statutory right and the trade which is sufficient to make the receipt a trading receipt.

109. In this respect Mr Goldberg referred us to *Murray v Goodhews* [1978] STC 207. There the taxpayer company was the tenant of a number of tied public houses. The owner decided to terminate certain of the tenancy agreements over a period of two years. Although there was no provision for more than three months' notice of termination, the owner chose to make voluntary payments to the tenant during the two-year period. It was held in the Court of Appeal that every case of a voluntary payment had to be considered on its own facts to ascertain the nature of the receipt in the recipient's hands. It is the character of the receipt that is significant; the motive of the payer is significant only so far as it bears, if at all, on that character. On the findings of fact made by the special commissioners, in particular the findings that there had been no disclosure by the owner to the tenant of the way in which the payments had been calculated, that there had been no subsequent negotiation about the payments, that the amount of the payments had no connection with the profits earned by the tenant, and that the calculation had not been linked with any future trading relationship between the parties, the Court of Appeal held that the commissioners had been fully justified in finding that the sums paid to the tenant were not trading receipts.

110. In his judgment Buckley LJ reviewed the authorities on the treatment of voluntary payments as trading receipts, including *Walker v Carnaby, Harrower, Barham & Pykett* 46 TC 561, where payments were treated as having been gifts not made as consideration for services rendered, and on that footing were held not to be chargeable to tax. He referred in particular to *Simpson v John Reynolds & Co (Insurance) Ltd* [1975] STC 271, another case of a voluntary payment, made by a client to an insurance broker on the ending of that relationship. In that case Russell LJ said (at p 274):

> "For the Crown it was contended that the fact that a payment is made without legal obligation does not per se elude the fiscal grasp. This is

> true. Gifts made or promised during the relevant connection may well be caught. It was also pointed out that the fact that payments are made after the connection has ceased does not per se elude the fiscal grasp. This also is true: for it may be part of the connection that such payments after its determination are to be expected. But this does not in my view lead to the suggested conclusion that when both of those circumstances are present—that is to say, where the gift is wholly voluntary and made unexpectedly after the business connection has come to an end—the payment is within the statutory language."

111. On the facts of that case the conclusion was that the payments could not be held to come within the charge to tax under Schedule D. Stamp LJ said (at pp 274-5):

> "It is not in question that the series of payments, of which this payment of £1,000 was one, was made and promised voluntarily. The payments were promised to be made by the former customer after the relationship of customer and broker had terminated. They were not made to satisfy any legal liability, real or imagined, to which the customer was or believed itself to be subject. The payments were not made by way of additional reward for any particular service rendered by the brokers or for their services generally. They were not made pursuant to the terms of a trading contract or as compensation for the breach of any such contract. The brokers were not entitled to, and indeed did not expect to receive them. Then, out of the blue came the promise, unenforceable as it was, to make them. By the time they were promised to be made, the trading relationship was, as I have said, terminated. The payments were voluntary payments, and I find wholly satisfactory the description of them as made by way of recognition of past services or by way of consolation for the rupture of a business relationship: a rupture which no doubt the client company were sad to see. It is no doubt a convenient way of describing them to say that they came to the taxpayer "by virtue of its trade" because the taxpayer would never have got them had it not for many years carried on the trade and performed valuable services to the donor. But the words "by virtue of the trade" are not in the section and it is in my judgment inappropriate to describe the payments as arising from the trade."

112. After referring to cases falling on the other side of the line, namely *IRC v Falkirk Ice Rink Ltd* [1975] STC 434 and *McGowan v Brown and Cousins* [1977] STC 342, Buckley LJ summarised the position as follows:

> "In my opinion a perusal of these authorities leads to the conclusion that every case of a voluntary payment, and we are only concerned with cases of that kind in the present appeal, must be considered on its own facts to ascertain the nature of the receipt in the recipient's hands. All relevant circumstances must be taken into account. These may include the purpose for which the payer makes the payment, or the terms, if any, on which it is made, as for example in the *Falkirk* case, where the payment was made for the purpose of its being applied in the recipient's business in the future; or it may be made by way of voluntarily supplementing the price paid for goods or services provided by the taxpayer in the course of his trade or business in the past, as in *Australia* (*Commonwealth*) *Comr of Taxation v Squatting*

> *Investment Co Ltd* and *Severne v Dadswell* and *McGowan v Brown and Cousins*; or the payment may be merely in the nature of a testimonial or a solatium which, although it recognises the value of past services, is not paid specifically in respect of any of those services, or of expected future services, by the taxpayer to the payer, as in the case of *Chibbett v Joseph Robinson & Sons*, *Walker v Carnaby, Harrower, Barham & Pykett* and *Simpson v John Reynolds & Co* (*Insurances*) *Ltd*. I stress that it is the character of the receipt in the recipient's hands that is significant; the motive of the payer is only significant so far as it bears, if at all, on that character."

113. Mr Gammie referred us to *Smart v Lincolnshire Sugar Co Ltd* 20 TC 643, where the British Sugar (Subsidy) Act 1925 provided that a subsidy be paid for 10 years on sugar manufactured in Great Britain from beet grown there. An Act of 1931 provided for further assistance, by way of weekly advances, to be given to companies engaged in such manufacture. The advances were repayable only in certain circumstances. Payments under the 1925 Act were brought into account in the profit and loss accounts, and taxed as trading receipts. But the taxpayer argued that the advances under the 1931 Act were not trading receipts, or were not trading receipts until the period during which possible repayment might be claimed had expired. It was held that, in view of the business nature of the sums in question, they were trading receipts to be taken into account in the year in which they were received.

114. Lord Macmillan gave the only substantive speech in the House of Lords. He first made the point, from which we can see echoes in the later judgment of Diplock LJ in *London & Thames Haven*, that the question whether the payments received by the company under the 1931 Act were or were not trading receipts depends upon the character and incidents of those payments, and it was therefore necessary to examine the relative provisions of the Act. He then referred to the statutory provisions, remarking in particular on the use by the draftsman of the term 'advances' which, in certain circumstances, would fall to be repayable. He then continued (at p 670):

> "But in my view the question ought not to be decided on merely verbal arguments. What to my mind is decisive is that these payments were made to the Company in order that the money might be used in their business. Here I definitely part company from Finlay, J., who thought that they "were not subsidies or grants to assist the Company in their business" [1]. We are told in the Stated Case that it was because of an apprehension that the companies might not be able to pay to the growers of beet the prices they had contracted to pay that this further assistance was given by the Government. It is true that the Appellants apparently did not actually require to have recourse to the "advances" they received, for in their accounts for the relevant years, which have been produced, the advances are not carried into profit and loss account but are entered as liabilities in the balance sheet, and the profit and loss accounts show a balance of trading profit without taking the "advances" into account. But if the Company had not happened to be able to pay for their raw material otherwise they could properly have used the "advances" for this purpose. It was with the very object of enabling them to meet their trading obligations that the "advances" were made;. they were intended artificially to supplement their trading

> receipts so as to enable them to maintain their trading solvency. If the "advances" had in any year been carried to the credit of the Company's trading account, as might properly have been done, and the trading account had in consequence shown a profit instead of a loss, can it be doubted that the credit balance would rightly have entered into the computation of the Company's profits or gains for tax purposes?"

115. Lord Macmillan rested his judgment on his view of the business nature of the sums in question which the company received, namely that they were supplementary trade receipts bestowed on the company by the Government and accordingly proper to be taken into the computation of the company's profits or gains for the year in which they were received.

116. Mr Gammie also referred us to *Falkirk Ice Rink*, the well-known case where a members' curling club which used an ice rink for curling made a voluntary payment to the owner and operator to cover the additional cost of curling in a particular season. The club feared that, in the absence of the donation, the owner might have to discontinue the provision of facilities for curling. In the Court of Session the Lord President (Lord Emslie) summarised the position that, firstly, for a payment to be a trading receipt the recipient must, in the first instance, be a trader (this is of course now subject to the rules on post-cessation receipts). Not every receipt by a trader in the course of his business is a trading receipt in the income tax sense, and whether a particular payment to a trader is to be regarded as a trading receipt is one which must be answered in each case in the light of all the relevant circumstances.

117. In looking at those relevant circumstances, Lord Emslie considered that the fact that the payment was voluntary was neutral. He went on to conclude (at pp 49-50):

> "In spite of the fact that there was no agreement between the Respondent and the club requiring the club to make any such payment to the Respondent and that the payment was not in respect of services rendered by the Respondent to the club in the past and that the Respondent gave no undertaking in return for the donation, I am of opinion that the payment was made in order that the Respondent might use it in their business and that in substance and in form it was a payment made to a trading company artificially to supplement its trading revenue from curling and in order, in the interests of the club and its members, to preserve the Respondent's ability to continue to provide curling facilities in the future. In its quality and nature this payment was of a business nature. It was accordingly a trading receipt in the hands of the Respondent and the question of law should be answered in the negative."

118. Mr Goldberg submitted that the important point in *Falkirk Ice Rink* was that the voluntary payment was made by a customer. We accept this, but the derivation of the payment is not decisive of its nature. What is important is the quality and nature of the receipt.

119.We conclude from this that we are unable to accept Mr Goldberg's second proposition. There is no rule that, in order to be trading receipts, sums not directly derived from his basic trading activities must be paid for a specific trading purpose.

The only principle is that one must have regard to the character of the receipt, and the purpose of the payment, or the motive of the payer, is relevant only in so far as it bears upon that question. All the relevant circumstances must be taken into account. We accept Mr Goldberg's submission that in *Smart* the fact that the payments were required by the statute to be used in the business was decisive, but that is not the principle to be derived from that case or from any of the other authorities.

Proposition (3)

120. Mr Goldberg's third proposition was that where a recovery is attributable to a trading activity in an earlier period and the profits for that earlier period have been correctly computed, it is inherently unlikely that the recovery can be taxed in a later period as a receipt of a trade. He referred to the fact that the overpayments of VAT in this case were made in periods which ended some time before the periods of receipt which have now been assessed. The goods in respect of which VAT was overpaid were sold in years before those now being assessed, and any right to repayment was created, albeit in inchoate form, in the years in which the original trading took place.

121. Mr Goldberg referred to the fact that the sums recovered could not have been brought into account for the years when the original trading took place. For those years, for all the Appellant companies, the possibility of recovery was left out of account. Mr Goldberg postulated that a similar accounting result could have been achieved if a lower sales price (taking account of a claim for different VAT treatment) had been accounted for in the accounts, but with a provision for the possibility that their might not be recovery of VAT. This, he argued, would have been similar to the position which obtained in *Morley v Tattersall* 22 TC 51, where unclaimed balances on the accounts of vendors with a firm of auctioneers, which were transferred to the credit of the partners by way of annual transfers although the firm remained liable to pay any claims in that respect, were held not to be trading receipts.

122. *Morley v Tattersall* was considered in *Pertemps Recruitment Partnership Ltd v Revenue and Customs Commissioners* [2011] STC 1346, to which we referred earlier in the context of s 42 1998. In that case the taxpayer carried on the business of a recruitment agency. Customers were invoiced on a regular basis. Some payments could not be reconciled to a particular invoice, and unreconciled balances that were more than six months old were transferred to a balance sheet account. At the end of the financial year that balance sheet account was released to the taxpayer's profit and loss account. The Upper Tribunal distinguished *Morley v Tattersall* on the basis that in that case the unclaimed balances were not the property of the auctioneers, but of their clients; in the case of *Pertemps*, the payments had been made by mistake and were the property of Pertemps, albeit that the customers had a claim for restitution.

123. In *Pertemps* in the Upper Tribunal it was held that there was no requirement in s 18(1)(a) that the trader be legally entitled to the receipts making up the profits. Case law showed that legal entitlement was not a prerequisite. Moreover the fact that a payment was made in circumstances such that the payer had a restitutionary claim to repayment of that sum did not mean that the recipient was not legally entitled to receive and keep the money unless and until a claim for repayment was made.

Furthermore, the mistaken payments derived from the business relationship between the taxpayer and its customers were made by the customers in the belief that they owed money to the taxpayer for services supplied by the taxpayer and were an unavoidable incident of the taxpayer's trade. Having regard not only to the nature of the payments (money which upon receipt became the taxpayer's), but also their purpose, the First-tier Tribunal had been entitled to conclude that they were trading receipts.

124. Mr Gammie also referred us in this respect to *Tapemaze v Melluish* [2000] STC 189, in the High Court, where the taxpayer's appeal against a finding of the special commissioners that advance payments of rent for the hiring of motor vehicles that were retained by the taxpayer company on the sale of its business and included in its profit and loss account for the accounting period of the sale, when it ceased to trade, were receipts of the trade for that accounting period, was dismissed.

125. In the course of his judgment in *Tapemaze*, Hart J considered *Morley v Tattersall*, but found it of no assistance. He said (at p202):

> "None of the decisions relied upon by the Crown demonstrates that, in the context of accruals accounting, a cash receipt is in some way stamped once and for all at the moment of receipt with the character of either having to be or not having to be brought into account in the computation of profit from the trade. Mr Singh's proposition that the advance payments of rental were trade receipts which would in due course fructify into taxable profits from the trade, and that the accruals accounting concept simply served to indicate when that fructification should be fairly viewed as having taken place, carried with it the implication that sooner or later those receipts would necessarily appear in the accounts as, or as components of, a profit from the trade.
>
> That implication appears to me to be going too far. In the present case, for example, had the terms of the sale agreement provided for the sums in question to be passed to the purchaser (whether or not for an additional consideration) there might have been no profit of a revenue nature to be recognised. The present question would then not have arisen. It would still have been accurate to say that the advance rentals when received were receipts of the trade, but that by itself would have told one nothing necessarily useful about the taxability of the appellant's profits under Case I of Sch D for the period in question."

126. Mr Justice Hart rejected the Crown's argument that because the payments were originally received in the course of trade, the subsequent appearance in the company's profit and loss account of a sum in respect of profits related to those receipts necessarily means that that sum has the character of profits from the trade for corporation tax purposes. The beginning and end of the enquiry was to consider the source of the profit properly recognised as income in the accounts.

127. We agree with Mr Gammie that there is nothing in the decided cases that supports Mr Goldberg's third proposition. As Mr Justice Hart said in *Tapemaze*, the starting point and the end point is the source of the profit, and there is no inherent likelihood or unlikelihood of the result that can be based on the fact that a recovery is

attributable to a trading activity in an earlier period. The question is whether the actual receipt or accrual arose from the trade.

Proposition (4)

128. We referred earlier to our views on the meaning of s 42 FA 1998. On this basis, we accept that the mere fact that sums have been included in the Appellants' profit and loss accounts, it does not follow that they are liable to tax. As we have found, the threshold question whether a receipt is a trading receipt must first be determined. The accounting treatment is an element of that enquiry, but it is not determinative.

Conclusions on the trading receipts issue

129. In our view, applying the principles we have derived from the authorities, the VAT repayments received by each of the Appellants were trading receipts. We have found in each case that the Appellants were beneficially entitled to the payments, and that those payments were not made by way of gift.

130. We have concluded that the fact that the payments in respect of overpaid VAT were made by HMRC to the representative member (or to an agent on behalf of the representative member) under the statutory provisions of s 80 VATA does not mean that the receipt, even in the case of VRP 5, cannot be a trading receipt. The fact that those payments are required to be made by a statutory provision relating to overpaid VAT is a relevant factor in determining what the payments were for, both when made by HMRC, and also when made by the relevant representative member.

131. We are required, in determining the character of the receipts, to take account of all relevant circumstances. Having regard to the statutory derivation of the payments, the underlying reasons why overpayments of VAT had arisen, and the transfers of trades within the groups, we conclude that the payments were to compensate for depletions in the trading results of the various companies whose supplies had given rise to the VAT overpayments, and the payments were directed to the companies that were carrying on those trades or had succeeded to them, save only for the case the payment of VRP 2 to SDG which, as we have found, retained the right to that payment on the transfer of its trade to SDHSL. The payments restored amounts which would have been brought in as trading profit if there had been no overpayments of VAT. The character of the receipts in the hands of each of the Appellants was accordingly, in our view, that of trading receipts.

132. There is, as *Pertemps* confirms, no requirement that a trader should be legally entitled to the receipts which make up the traders' profits. Thus, even if, contrary to our finding that SDG and RGL were beneficially entitled to VRP 2 and VRP 5 respectively, there might be some doubt as to the legal rights retained by GUS plc, Kay & Company and Abound in respect of VRP 2 and VRP 5, no competing claim to those payments was made, and there is, in our view, no reason on the facts in relation to VRP 2 why the payment should not be treated as a trading receipt in the hands of SDG, nor in relation to VRP 5 why the payment should not be treated as a trading receipt of RGL. Those receipts nevertheless would bear the character of trading

receipts. Any competing claim might, as noted by Hart J in *Tapemaze*, have affected the issue of whether there was a profit of a revenue nature to be recognised, but not the question whether there was a trading receipt.

133. We agree of course with Mr Goldberg that *Pertemps* cannot in any respect override *Morley v Tattersall*, which was distinguished in that case. But we do not agree with his submission that this case is closer to *Morley v Tattersall*. In that case the auctioneers were never beneficially entitled to the monies they received in a fiduciary capacity for their clients. That was in contrast to the position in *Pertemps*, where the mistaken payments were the property of Pertemps, albeit that the customers had a right of restitution. We have found in each case that the Appellants were beneficially entitled to the VAT repayments. That was the case even in relation to SDG's receipt of VRP 2 and RGL's receipt of VRP 5, where we have found that any rights that were retained by GUS plc, Kay & Company and Abound were not rights against SDG, in the case of VRP 2, or RGL in the case of VRP 5 and that any claim by those companies against SDG or RDG would have to have been made in restitution.

134. In our view, in each case the true source of each of the VAT repayments was the trade in the course of which the original overpayments of VAT arose. The VAT repayments were, accordingly, trading receipts arising out of those trades.

Liability to tax on the trading receipts

135. Where the trading receipts arise from a trade carried on by the recipient itself at the time of the original supplies which gave rise to the overpayments of VAT, we find that the recipient is taxable under Case I of Schedule D to the extent that the receipt gives rise to profit in the recipient's accounts. This applies to part of VRP 1 paid to SDG (£12,600,000 in respect of supplies made by SDG in the period from 25 November 2000 to 25 September 2004), VRP 3 paid to SDHSL (£1,600,000 in respect of supplies made by SDHSL in the period from 1 May 2003 to 25 September 2004), VRP 5 paid to RGL (£49,800,000 in respect of supplies made by RGL in the period from 1 March 1996 to 28 February 1997), and VRP 7 and VRP 8 paid to LRL (as to the whole).

136. In respect of the remaining payments we need to consider sections 103 and 106 ICTA, on which we received the competing submissions of the parties. Those sections deal with receipts arising from the carrying on of a trade which has been permanently discontinued. These are commonly described as "post-cessation receipts". The provisions were brought in as a result of it being held in cases such as *Purchase v Stainer's Executors* 32 TC 367 and *Carson v Cheyney's Executor* 38 TC 240 that where a trade which was the source of an income had ceased, and an amount of income arose after the trade had ceased, those receipts could not be taxed.

137. The basic charging provision for post-cessation receipts is s 103 ICTA, which we have set out above. It charges tax under Case VI of Schedule D on sums arising from the carrying on of a trade which has been permanently discontinued. This includes,

by virtue of s 110(2) and s 337(1), a case where a company has ceased to carry on a trade, even where the trade is not in fact discontinued.

138. Mr Goldberg argued that s 103 could apply only to charge the person who had carried on the trade. We do not agree. As Mr Gammie submitted, s 103 does not refer to any particular person on whom the charge is to be levied; it is a charge on the relevant sums to which the section applies, and taxes the receipt of those sums. It is clear, and the historical background of the *Stainer's Executors* and *Cheyney's Executor* cases confirms, that personal representatives of a trader may be taxed on post-cessation receipts arising from the discontinued trade of a deceased trader, who will not themselves have carried on the trade. Furthermore, s 103(3) expressly excludes sums received by a person "beneficially entitled" to them. This in our view indicates that the person to be charged on the sums received is the person entitled to the receipt of the relevant sums, whether or not that person has formerly carried on the trade.

139. Section 106 makes special provision where rights to receipts within s 103 are transferred. Section 106(1) deals with the position where the right to receive the relevant sum has been transferred for value. In such a case tax is charged, not on the amount of the sum received, but on the amount or value of the consideration, or market value, if the transfer is not at arm's length. It was common ground that s 106(1) had no application to these appeals.

140. Section 106(2), on the other hand, is relevant. That applies where the trade is treated as permanently discontinued by reason of a change in the persons carrying it on, and the right to receive the sum to which s 103 would otherwise apply is transferred to the persons carrying on the trade after the change. In those circumstances s 103 does not apply. No person can be charged on the relevant receipts under s 103. Instead, any sum that is received by the persons carrying on the trade is brought into the computation of the trading profits in the year in which it is received.

141. Where there is a transfer within s 106(2), the effect is two-fold. First, s 103 does not apply. This means that no Case VI charge can arise on the receipt, or on the value of the transfer of the right under s 106(1); s 106(1) is expressed to be subject to s 106(2). Absent s 106, the successor trader would have been liable under Case VI on the receipts of the relevant sums as described in s 103. The effect of s 106(2) is to convert that Case VI charge into a charge under Case I on the receipt as part of the computation of the successor's profits.

142. Section 106(2) has two effects, and in our view each of them is independent of the other. If there is a transfer to the successor trader, the effect is that s 103 does not apply, and that is the effect whether or not the amount is received by the successor trader so that it is brought into account in the trading profits of the successor. The charge on the successor is dependent on the successor receiving the relevant sum. If that sum is received by another person, and cannot be treated as received by the successor, that other person cannot, in our view, be charged under s 103. Although Mr Gammie argued that there was nothing to prevent such a person being charged

under s 103, we do not agree. It is s 106(2) itself, which provides that tax may not be charged under s 103 if the right to receive the relevant sum has been transferred to a successor trader.

143. We have reached this conclusion, we have to say, with some hesitation. The effect is that, where a trade has discontinued without a transfer of the right to post-cessation receipts, any recipient of those sums arising from the former trade is taxable under Case VI by virtue of s 103. As we have found, this is not confined to receipts by the original trader. On the other hand, where there has been such a transfer, our construction of s 106 is that s 103 must be excluded, and a tax charge can only arise under Case I if the recipient of the relevant sum is the successor trader. A receipt by any other person escapes taxation. Whilst that appears to create a gap in the post-cessation rules, albeit one that is likely to arise only in unusual circumstances, we nevertheless conclude that this is the proper construction of s 106(2).

144. We are conscious also that, in construing s 106(2) in the way we have, we are departing from the description of that provision given by the special commissioners in *Rafferty v Revenue and Customs Commissioners* [2005] STC (SCD) 484 (at [95] and [96]). We were not referred to *Rafferty*, but in that case the special commissioners drew attention to the purpose of s 106(2) being to preclude the same receipts being brought into computations of profits twice, both on the transferor, under s 103 or s 106(1), and on the transferee as a trading receipt, and to determine that the charge to tax on such receipts falls on the transferee. But the special commissioners then went on to say that s 106(2) provides that tax is not chargeable if the transferee of the trade brings the sums into computation of its profits, and that the transferor is not taxable if he transfers the right to receive the sums to his successor in the trade who pays tax on the same sums.

145. We are unable to construe s 106(2) so as to provide for the same degree of conditionality. In our view, s 103 is excluded by s 106(2) only if the trade is treated as permanently discontinued by reason of a change in the persons carrying it on and if the right to receive the relevant sum is then transferred to the persons carrying on the trade. There is, in our view, no further condition that the successor brings that sum into its computation or pays tax on that sum, although s 106(2) provides that the successor will do so on a receipts basis.

146. We turn now to apply these principles to each of the VAT repayments which are not within those that are taxable on general principles under Case I of Schedule D.

(1) VRP 1. Certain of the supplies to which VRP 1 relates were made by RGL. We have found that the whole of RGL's trade, together with all rights and entitlements, was transferred to SDG. Section 106(2) applies. In consequence SDG is liable under Sch D, Case I on that part of VRP 1 which derives from RGL's trading.

(2) VRP 2. VRP 2 was paid to LW Corporation, the amount being recognised as a receivable in SDG's accounts. There was, for s 103 purposes, a receipt of this sum, to which SDG was beneficially entitled, after SDG had ceased to trade following the transfer of its trade to SDHSL.

We have found that SDG retained the right to payment of VRP 2, and did not transfer it to SDHSL. Consequently, s 106(2) does not apply in relation to the transfer of the trade to SDHSL. Section 103 accordingly applies. That part of the VRP 2 that relates to the trades of SDG itself and RGL is correctly assessed on SDG under Case VI by virtue of s 103.

We have found that the rights of GUS plc, Kay & Company and Abound to VRP 2 were not transferred to RGL, and cannot therefore have passed to SDG. In relation to those transfers, therefore, s 106(2) does not apply. Section 103 does apply. That part of VRP 2 that relates to the trades of GUS plc, Kay & Company and Abound is correctly assessed on SDG under Case VI by virtue of s 103.

(3) VRP 3. The transfer of the home shopping business of LRL to SDHSL carried with it all rights to that part of VRP 3 which related to the supplies of LRL. That part of VRP 3 is accordingly to be brought into account under Case I by virtue of s 106(2).

(4) VRP 4. VRP 4 related to the trades of the Six Companies and LRL. LRL succeeded to the trades of the Six Companies, with the right to VRP 4, and LRL transferred the home shopping business, along with its rights to VRP 4, to SDHSL. VRP 4 is therefore taxable under Case I by virtue of s 106(2).

(5) VRP 5. Part of VRP 5 related to the trades of Kay & Company and Abound which were transferred to RGL. We have found that the rights of Kay & Company and Abound to VRP 5 were not thereby transferred to RGL. Section 106(2) does not apply, but RGL is correctly assessed to the relevant part of VRP 5 under Case VI by virtue of s 103.

(6) VRP 6. The supplies giving rise to the repayment were made by the Six Companies to whose trades and assets, including the right to VRP 6, LRL succeeded. LRL is accordingly correctly assessed on VRP 6 under Case I by virtue of s 106(2).

147. In summary, we have found that all the VAT repayments are trading receipts, either of existing trades or trades that have discontinued, and all are taxable under Schedule D, Case I or Case VI as we have described.

Are the interest payments taxable?

148.We turn now to consider the tax position of the interest payments. There was no payment of statutory interest by HMRC to RGL. All relevant payments, of amounts equal to the statutory interest, were received by SDG, SDHSL and LRL directly or, in the case of SDG, indirectly, from the representative members who had received the statutory interest payments from HMRC under s 78 VATA.

149. HMRC's case is that all these amounts were payments of interest, and that the interest is taxable as such in the hands of each of the Appellants, firstly, in the case of LRL on IP 6 under Case III as it stood before the introduction of the loan relationships rules, and otherwise under Case III as it applies for corporation tax on the basis that

the interest payments are profits or gains arising from loan relationships under FA 1996. HMRC also argue that if Case III is not applicable, then the interest can be charged under Case VI, or if not then the interest payments are part of the trading receipts and taxable as such in the same way as for the VAT repayments.

150. Mr Goldberg argued that the amounts recorded in the Appellants' accounts in respect of the interest payments were not interest at all. They did not derive from debt claims or money debts. HMRC did not owe any money to any of the Appellants and, he submitted, none of the Appellants were owed money or debts by the representative member making the payment. These payments were made under arrangements made as and when the various interest payments were received, and not, with the exception of the arrangements for the payment of IP 2 to SDG, under any obligation.

151. Mr Gammie started by referring us to s 18(1)(b) ICTA, which charges tax on "all interest of money". The first question, therefore, is whether the sum in question is interest of money. In this connection Mr Gammie referred us to *Riches v Westminster Bank Limited* [1947] AC 390. In that case the appellant, Mr Riches, had entered into an agreement in 1936 with a Mr Ridsdel under which, in consideration of his introducing to Mr Ridsdel a transaction involving the purchase of a block of shares, Mr Ridsdel was to pay him one-half of any profits which might be made on the sale of the shares. Mr Ridsdel fraudulently failed to pay over the whole of the sum to which Mr Riches was entitled, and Mr Riches took action for recovery against the bank, as judicial trustee of Mr Ridsdel's will. The result was that Mr Riches recovered the difference between what had been paid and what should have been paid. In the exercise of his discretion under the relevant statute the judge awarded interest, at the rate of 4% from the period when the sum should have been paid to the date of judgment. The bank deducted income tax at the then standard rate on its payment of the interest amount.

152. For the appellant it was argued that the award made by the judge in the exercise of his discretion was in the nature of an award of damages, and not under contract, and could not have the character of interest. The sum awarded was not interest in the true sense but was part of a lump sum given as compensation for the detention of money due to the appellant. Furthermore, the "interest" so awarded was never accruing. It had no existence until it was awarded as part of the amount for which judgment had been given, and did not have the quality of being recurrent or being capable of recurrence, which is an essential feature of interest of money.

153. The House of Lords held that the interest awarded was interest of money within Schedule D of the Income Tax Act 1918. There was no incompatibility between damages and interest. An argument that there was such an incompatibility, as Lord Simonds said (at p 406) "confuses the character of the sum paid with the authority under which it is paid". The argument that the interest ordered to be paid was not "interest of money" for tax purposes because it had no existence until it was awarded and did not have the quality of being recurrent or capable of recurrence was also rejected. A sum which was calculated on the footing that it accrues *de diem in diem* has the essential quality of recurrence in sufficient measure to bring it within the scope of income tax. It is irrelevant that the calculation begins on one day and ends

on another. What is more important is that the payment is income (see per Lord Simonds at pp 410 - 411).

154. This case is authority that the source of a payment is immaterial in determining whether a payment is in the nature of interest. What is relevant is whether the amount has the quality of income and is properly to be regarded as interest in the sense of having been calculated by reference to a principal sum on a basis which takes account of a period over which the principal sum is due or by reference to which the calculation is made.

155. We have held that the VAT repayments made to each of SDG, SDHSL and LRL were made in respect of entitlements that existed between the relevant group companies. We have found that these payments were not made by way of gift, but that, in each case, the recipient was beneficially entitled to the payments. In the same way, the recipients were entitled to be paid, and were paid, amounts equal to the statutory interest received by the representative members from HMRC. As between the representative member and the recipient company that payment has the quality of income, and it has been calculated on the principal amount of the relevant VAT repayment at the statutory rate of interest over the period for which the VAT was repayable. That has the essential quality of recurrence, and we find accordingly that the payments of the IP amounts were interest.

156. That, we think, disposes of the payment of IP 6 to LRL. That payment is taxable under Case III of Schedule D.

157. The position of the other payments of interest depends on an analysis of the loan relationships provisions in FA 1996. It is common ground that the interest was not payable on a debt arising from a transaction for the lending of money. There was accordingly no "loan relationship" within the meaning of s 81 FA 1996. The question, therefore, is whether the interest paid to the relevant Appellants can be assimilated to interest arising on a loan relationship by virtue of s 100 of that Act.

158. For s 100 to apply, it is necessary that the Appellant in each case stands in the position as creditor as respects a money debt and that the money debt is one on which interest is payable to the Appellant. The expression "money debt" is itself defined by s 81(2). For these purposes it is essentially a debt which falls to be settled by the payment of money.

159. We consider that, in the case of each of SDG (in relation to IP 1 and IP 2), SDHSL (in relation to IP 3 and IP 4) and LRL (in relation to IP 7 and IP 8), the payments were of interest. We have found that the VAT repayments were made, not by way of gift from the representative member, but because within the group the Appellant companies were entitled to those payments. That entitlement gave rise to an obligation at the relevant time for the representative members to make the VAT repayments to the Appellants. The making of those payments in respect of the entitlements we have found existed at the time is, in the light of our finding that they were not made by gift, evidence of the discharge of the obligations of the

representative members in this respect. That, in our view, amounts to a money debt for the purpose of s 100.

160. The interest payments were calculated on the amounts due in respect of the VAT repayments, that is to say on the amounts of the money debts, and by reference to the period for which the VAT was repayable. It is of no consequence that these amounts did not accrue over the entire period that the VAT remained overpaid; they were nevertheless calculated at the relevant time by reference to that period. The interest accordingly arose from the money debt that was discharged on the making of the VAT repayment.

161. Accordingly, we find that all the interest payments were properly assessable on the Appellants under Case III of Schedule D.

Decision

162. In summary, we have concluded that:

(1) the VAT repayments were trading receipts;

(2) those receipts are chargeable to corporation tax on each of the Appellants, either under Case I or Case VI of Schedule D, as we have described; and

(3) the interest payments are chargeable to corporation tax under Case III of Schedule D.

163. The appeal of each Appellant is dismissed.

Application for permission to appeal

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.

ROGER BERNER

TRIBUNAL JUDGE

RELEASE DATE: 14 February 2012