[2019] UKFTT 0059 (TC)

TC06945

Appeal number: TC/2017/02926

CORPORATION TAX – capital allowances – expenditure on fixtures on which capital allowances had been claimed by previous owner – claim limited to amount which vendor had been required to bring into account – whether or not this was determined by allocations in contract between the parties – held not – whether or not this was determined by amount actually brought into account by vendor – held not – appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

GLAIS HOUSE CARE LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE PHILIP GILLETT

Sitting in public at Southampton Magistrates' Court on 21 January 2019

David Pett, counsel, instructed by Lane & Lane, Accountants, for the Appellant

Paul Eyles, officer of HMRC, for the Respondents

DECISION

1. This was an appeal against closure notices resulting from enquiries into the appellant's corporation tax returns for the accounting periods ending 31 March 2012 to 2014 inclusive.

2. The appeal relates to a partial disallowance of claims to capital allowances on fixtures totalling £318,792, made in a return for the year ended 31 March 2012. The partial disallowance has consequential effects upon the appellant's claims for capital allowances in the years ending 31 March 2013, 26 March 2014 and 31 March 2015.

The Facts

3. Prior to the hearing, the parties had agreed a statement of agreed facts as set out below, which I accordingly find as matters of fact.

4. On or around 24 March 2005, Kappians Care Homes ("KCH") purchased the freehold property of Glais House, Birchgrove Road, Glais, Swansea, SA7 9CN.

5. At all material times, the business of an ongoing residential care home has been carried on at the property.

6. The total amount of capital costs on fixtures claimed by KCH in their returns for capital allowances in relation to the property were as follows:

(1) Accounting period 28 February 2006: £103,287.

This comprised £68,500 in relation to the value of the fixtures (as defined in s173 Capital Allowances Act 2001 - installed or otherwise fixed in or to the purchased property ("fixtures")), the balance of £34,787 being in respect of fixtures in a part-built extension, commenced by KCH after purchase.

(2) Accounting period ended 28 February 2007: £100,213.

This was the balance of costs in relation to the extension, which, when added to the £34,787 above, totals £135,000.

(3) Accounting period ended 28 February 2009: £35,412.

This figure comprises both fixtures and other items (chattels and other equipment) which are not fixtures.

(4) Total claims by KCH were therefore £238,912.

7. It should be noted that the above claims include a claim for capital allowances in respect of the cold water supply to the property, in the amount of £15,000, which was not, at the time the expenditure was incurred, eligible for capital allowances. Nevertheless, HMRC, incorrectly, accepted the claim for capital allowances.

8. In the accounting period ended 28 February 2010, the residual value of KCH's main pool was £85,504.

9. In or around February 2010, KCH went into administration. No capital allowances were claimed by KCH in the accounting period ended 28 February 2011.

10. In May 2011, the appellant, Glais House Care Ltd ("Glais House"), purchased the business and assets of the residential nursing home, including the property, from the administrators of KCH for a total consideration of £1.7m, which, by clause 4.3 of the contract, was apportioned between the assets as follows:

(1) £1 for the Contracts (as defined);

(2) £35,000 for the Equipment (defined as "the items of machinery, computer hardware, telecommunications equipment, furniture, loose tools and any other equipment used by the Vendor for the purposes of the Business situated at the Property owned by the Vendor on Completion")

(3) £1 for the Fixed Assets (defined as "all fixtures and fittings, plant, machinery, equipment and other tangible assets physically attached to the Property and owned by the Vendor at Completion")

(4) £164,996 for the Goodwill;

(5) £1 for the Intellectual Property;

(6) £1 for the Licences [to carry on the business];

(7) £1,500,000 for the Property.

11. KCH was liquidated and wound up soon after the sale and, in its final accounting period, to 28 October 2011, a balancing allowance was claimed of £50,803. This implies that a disposal value of £34,701 was brought in by KCH.

12. The parties agree that this is likely to be a transposition error and the amount claimed should have been £50,503 meaning that a value of £35,001 was used by KCH (this figure corresponding to the £35,000 for Equipment and £1 for Fixed Assets as provided in the contract for sale).

13. On 26 March 2014, the Appellant submitted a claim for capital allowances in respect of qualifying expenditure on fixtures (only) purchased with the property as detailed in a written report commissioned by Glais House from Lane & Lane in 2013 ("the Valuation Report").

14. The Valuation Report identified the market value of qualifying assets which were fixtures within the property at the time of the sale by KCH to Glais House, the figures for their respective market values then being "indexed back" so as to determine the estimated costs, as at the time of their installation, of those fixtures.

15. The Valuation Report was submitted to the District Valuer who agreed the aggregate amount of the values for items specified in that report (albeit by a different methodology). The parties agree that those figures may, for the purposes of this appeal, be taken to be correct.

16. Accordingly, the valuation of those fixtures are agreed at £318,792, and it is accepted by HMRC that all those fixtures would have qualified for capital allowance

claims by Glais House, had there been no prior claims to capital allowances in respect of those fixtures by KCH.

17. At the hearing, HMRC attempted to challenge the figures set out in the report, with which it had previously agreed, but I decided that such a challenge would, at this stage, amount to litigation by ambush, which I said I could not consider. This challenge was therefore withdrawn.

The Law

18. The relevant legislation is contained in the Capital Allowances Act 2001 ("CAA").

19. Section 181 CAA provides, in effect, that if a person acquires an interest in relevant land to which any plant and machinery has become a fixture, and the capital expenditure falls to be treated in whole or in part as expenditure on the fixtures, the purchaser is to be treated as the owner of the fixture as a result of incurring that expenditure.

20. Section 562 CAA provides that all property sold as a result of one bargain is to be treated as sold together even though (a) separate prices are, or purport to be, agreed for separate items of that property, or (b) there are, or purport to be, separate sales of separate items of that property (per sub-section 562(2)).

21. Specifically, sub-section 562(3) provides:

> "If an item of property is sold together with other property, then, for the purposes of the CAA 2001 –
>
> > (a) the net proceeds of sale of that item are to be treated as being so much of the net proceeds of sale of all of the property as, **on a just and reasonable apportionment**, is attributable to that item, and
> >
> > (b) the expenditure incurred on the provision or purchase of that item is to be treated as being so much of the consideration given for all the property as, **on a just and reasonable apportionment**, is attributable to that item."

22. If, as in the present circumstances, allowances have previously been claimed by the vendor (ie, by KCH), s 62(1) CAA and s185 CAA impose limits on the maximum allowable amount on which the current owner, Glais House, may claim capital allowances for fixtures.

23. Section 185(2) provides:

> "if the new expenditure exceeds the maximum allowable amount, the excess….(a) is to be left out of account in determining the current owner's qualifying expenditure…."

24. Section 185(3) defines the "maximum allowable expenditure" as:

> "D + I where: D is the disposal value of the plant and machinery which the past owner **has been or is required** to bring into account, and I is any of the new expenditure that is treated under section 25 (building alterations in connection with installation) as expenditure on the provision of the plant or machinery".

25. Importantly Section 62(1) then restricts the amount of any disposal value to be brought into account as follows:

> "The amount of any disposal value required to be brought into account by a person (in this case, KCH) in respect of any plant or machinery is limited to the qualifying expenditure incurred by the person on its provision".

26. Section 188 CAA applies if a person, such as KCH, is treated as the owner of a fixture under, inter alia, section 176 (person with interest in relevant land having fixture for purposes of qualifying activity). Sub-section 188(2) provides that if the person ceases at any time to have the qualifying interest, he is to be treated as ceasing to be the owner of the fixture at that time. In this event, section 61(1) requires:

> "a person who has incurred qualifying expenditure…to bring the disposal value of the plant or machinery into account for the chargeable period in which (a) the person ceases to own the plant or machinery….."

27. Section 61(2) sets out a table of the disposal values to be brought into account in normal circumstances, but it is agreed between the parties that, in the case of fixtures, it is the table in s196 which is relevant, not that in s61.

28. Section 196(1) provides:

> "the disposal value to be brought into account in relation to a fixture depends on the nature of the disposal event, as shown in the Table which follows".

29. Item 1 in that Table states that, in the case of a "cessation of ownership of the fixture under section 188 because of a sale of the qualifying interest except where item 2 (not relevant here) applies", the disposal value is:

> "the part of the sale price that:
>
> > (a) falls to be treated for the purposes of this Part [of the CAA] as expenditure incurred by the purchaser [ie, Glais House] on the provision of the fixture, or
> >
> > (b) would fall to be so treated if the purchaser were entitled to an allowance."

Discussion

30. It is agreed between the parties that, when it acquired the business and assets of KCH, Glais House incurred expenditure of £318,792 on fixtures, including £13,226 on the cold water system and £17,006 on the mains electrical system, plus £35,000 on what was separately classified as equipment, when it acquired the assets of KCH.

31. KCH had originally incurred expenditure of £220,454, including £15,000 on the cold water system, and £18,458 on equipment, in acquiring those assets.

32. KCH had brought in, or intended to bring in, disposal proceeds of £35,001 when calculating its capital allowances for its final accounting period, when the assets had been sold to Glais House.

33. It is common ground between the parties that, because capital allowances had previously been claimed on the fixtures in question by KCH, the amount of expenditure on which Glais House can claim capital allowances is limited in two ways:

> (1) Under s185, the amount which can be claimed is limited to the amount "which the past owner **has been or is required** to bring into account" on its disposal, and
>
> (2) In addition, s62(1) provides that "the amount of any disposal value required to be brought into account by a person (in this case, KCH) in respect of any plant or machinery is limited to the qualifying expenditure incurred by the person on its provision".

34. The dispute between the parties arises because, when it disposed of its assets, KCH only brought into account in its capital allowance computations the amount of £35,001, which was the amount set out in the agreement for the sale of its assets and business to Glais House. HMRC argue therefore that this is the amount which should be treated as the amount which KCH "has been or is required" to bring into account. This would in effect cap the capital allowances which Glais House could claim on the pre-owned assets at £35,001.

35. In support of this argument, Mr Eyles, for HMRC, submitted that this figure of £35,001 was the only figure which KCH had in their possession at the time they prepared their tax computations and it was the amount which had been agreed between the vendor and the purchaser according to the contract between them. In addition, it was, in practice, the amount which had actually been brought into account by KCH. In his view therefore this was the amount which should be brought into account and which KCH was "required to bring into account".

36. However, Mr Pett, for Glais House, submitted that the provisions of the contract should be over-ridden by s562 which, as set out above, provides that all property sold as a result of one bargain is to be treated as sold together even though (a) separate prices are, or purport to be, agreed for separate items of that property, or (b) there are, or purport to be, separate sales of separate items of that property (per sub-section 562(2)).

37. Specifically, sub-section 562(3) provides:

> "If an item of property is sold together with other property, then, for the purposes of the CAA 2001 –

(a) the net proceeds of sale of that item are to be treated as being so much of the net proceeds of sale of all of the property as, **on a just and reasonable apportionment,** is attributable to that item, and

(b) the expenditure incurred on the provision or purchase of that item is to be treated as being so much of the consideration given for all the property as, **on a just and reasonable apportionment**, is attributable to that item."

38. Mr Eyles was unable to refer me to any other legislation or case law which might over-ride these provisions and I therefore agree fully with Mr Pett on his interpretation that the starting point for the calculation of the amount of expenditure on which Glais House can claim capital allowances is the proportion of the total purchase price which is attributable to the fixtures "on a just and reasonable apportionment".

39. This does of course leave HMRC in a difficult position in that they would undoubtedly wish to see symmetry between the figure for the disposal value which was actually brought into account in the capital allowance computations of KCH and the figure for the acquisition costs in the capital allowance computations of Glais House. Mr Pett's interpretation, with which I agree, does not necessarily produce this result, but, in my view, the legislation did not, at that time, set out to deliver this symmetry.

40. I understand that this issue was specifically recognised and addressed by the introduction of ss187A and 187B CAA, which were enacted by the Finance Act 2012 with effect for expenditure incurred on or after 1 April 2012. If HMRC's submissions on this issue are correct then the introduction of ss187A and 187B would not have been necessary, but this is not of course determinative of itself. Nevertheless, the transactions in this case pre-date those new provisions and they are not therefore relevant.

41. HMRC has already agreed that a just and reasonable apportionment of the acquisition expenditure incurred by Glais House produces a figure for the cost of the fixtures of £318,792. This includes a figure of £13,226 relating to the cold water system, which I consider separately below, leaving a net cost of £305,566.

42. Glais House is however unable to claim capital allowances on this amount because their claim is effectively restricted, by s62(1), to the amount of expenditure which KCH incurred on its acquisition of those assets. This has been agreed between the parties as being £220,454, including £15,000 relating to the cold water system, ie, £205,912 excluding the cold water system, and this is therefore the amount on which I consider Glais House may claim capital allowances.

Cold Water System

43. I must consider the expenditure on the cold water system separately.

44. It is agreed between the parties that KCH incurred £15,000 on the provision of a cold water system to the building in the years up to 2007, at a time when expenditure on cold water systems was not eligible for capital allowances. KCH claimed capital

allowances on this expenditure, incorrectly, and HMRC, again incorrectly, accepted this claim. I can do nothing to interfere with the calculation of the capital allowances claimed by KCH but, in my view, the amounts which are required to be brought into the capital allowance computations by KCH on its disposal of the fixtures must exclude the costs of the cold water system.

45. By the time Glais House acquired the property however, expenditure on cold water systems was eligible for capital allowances. In my view therefore, Glais House is free to claim capital allowances on the amount it spent on the acquisition of the cold water system without any limitation under s185 or s62(1). This amount is set out in the report by Lane & Lane and is agreed between the parties as being £13,226.

46. Mr Pett did suggest that perhaps Glais House should be able to claim capital allowances on the amount of expenditure incurred by KCH on the cold water system, of £15,000. This was on a basis which I did not fully understand, but I cannot see any reason to give relief for more than was actually incurred by Glais House. I therefore find that the amount of expenditure on which Glais House may claim capital allowances in respect of the cold water system is £13,226.

Mains Electrical System

47. Similar issues arise as regards expenditure on the mains electrical system. At the time KCH incurred expenditure on the mains electrical systems such expenditure was not eligible for capital allowances, but in this case HMRC refused KCH's claims for capital allowances.

48. By the time Glais House acquired the assets of KCH however such expenditure did qualify for capital allowances.

49. According to the Lane & Lane report, Glais House incurred expenditure of £17,006 on the mains electrical system and in my view they are entitled to claim capital allowances in full in respect of this amount. I understand that this is accepted by HMRC.

Equipment

50. The position regarding the capital allowance treatment of the non-fixed equipment which was not included in the figures for fixtures was not argued before me and I am not therefore clear what has been agreed between the parties on this issue. I believe however that I should address the issue for the sake of completeness.

51. The figures given to me state that KCH spent £18,458 on loose equipment. According to the contract between KCH and Glais House a consideration of £35,000 was attributed to this equipment but, as we have discussed above, the amount which should have been brought into account by KCH and on which Glais House could claim capital allowances should be the amount attributable to the equipment on a just and reasonable apportionment, limited to the amount which KCH spent on it of £18,458.

52. I have no figures for what might be a just and reasonable apportionment of the consideration paid by Glais House which should be attributed to the equipment but I think any claim to capital allowances must be limited to the lower of £18,458 and the amount of any just and reasonable apportionment of the purchase price to that equipment.

53. I understand that the report prepared by Lane & Lane did not include any analysis of the expenditure incurred by either KCH or Glais House on loose equipment. If I am wrong in this assumption then I must leave it to the parties to agree the relevant figures on the basis of my decision.

Costs

54. At the end of the hearing Mr Pett made an application on behalf of Glais House for costs on the grounds of the unreasonable behaviour of HMRC, specifically:

(1) Throughout the negotiation process, the basis of HMRC's arguments had been articulated differently at different times,

(2) HMRC had only disclosed the costs actually incurred by KCH at a very late stage of the proceedings, thus preventing Glais House from making a proper calculation of the capital allowances to which it was due, and

(3) At the hearing, HMRC had attempted to resile from its prior agreement with the figures set out in the report by Lane & Lane.

55. This case was classified as being a standard case, in which case I may only make an order for costs under Rule 10(1)(b) of the Tribunal Procedure (First-tier)(Tax Chamber) Rules 2009 if:

> "the Tribunal considers that a party or their representative has acted unreasonably in bringing, defending or conducting the proceedings;"

56. I do consider that HMRC's actions in attempting to challenge, at the hearing, the figures in the report prepared by Lane & Lane, which they had previously agreed, were unreasonable, but that only happened at the hearing itself and could not therefore have given rise to any additional costs on the part of Glais House.

57. The conduct of the negotiations was not something on which I received any evidence of great note, from either party. However, on the basis of the correspondence before me I cannot find anything unreasonable in the behaviour of HMRC in bringing, defending or conducting the proceedings, for the following key reasons:

(1) The asymmetry between the disposal proceeds brought into the final computations of KCH and the amount on which capital allowances were claimed by Glais House was clearly an issue for HMRC, which they would naturally wish to challenge,

(2) The amounts on which capital allowances were being claimed by Glais House differed substantially from the amounts set out in the contract between Glais House and KCH,

(3) Glais House were claiming capital allowances on expenditure of £318,792, which was considerably in excess of the expenditure actually incurred by KCH on the fixtures of £220,454, although this information was only made available to Glais House as part of the litigation process due to taxpayer confidentiality concerns before this stage, and

(4) The additional claims to capital allowances were only made some time after the purchase of the assets from KCH, following the preparation of the report by Lane & Lane.

58. In such circumstances I would expect HMRC to bring, defend and conduct proceedings with all reasonable means at their disposal and I am unable to find that their behaviour was in any way unreasonable in this respect.

59. I therefore decline to make any order as to costs.

Summary and Decision

60. I therefore find that Glais House is entitled to claim capital allowances in respect of its expenditure on the acquisition of the assets and business of KCH in the following amounts:

(1) £205,912 in respect of fixtures,

(2) £13,226 in respect of the cold water system,

(3) £17,006 in respect of the mains electrical system, and

(4) In respect of the loose equipment, the lesser of £18,458 and the amount which Glais House is deemed to have spent on it on a just and reasonable apportionment of the total acquisition costs.

61. For the above reasons therefore, this appeal is ALLOWED IN PART.

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

PHILIP GILLETT
TRIBUNAL JUDGE

RELEASE DATE: 28 JANUARY 2019