The Personal Tax Planning Review

SOMETHING OLD OR SOMETHING NEW?

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It is perfectly common for a company to carry on more than one trade but the consequences can cause problems, particularly when the company wishes to take advantage of the loss carry-back provisions of s.393A(1)(b) TA 1988. Losses can only be carried back to a period when the trade from which the losses derive was carried on. When the claim to repayment is submitted, you may find the Inspector looking closely at the trading activities and suggesting that your losses derive from a separate, and relatively new trade. You, on the other hand, may be keen to argue that the losses derive from the original trade, as extended by new activities.

Surprisingly, many useful principles and arguments to support the "extension" theory, can be found in elderly decided Tax cases which the Revenue won. These early cases have decisions which may have been coloured by the times, but are, nevertheless just as relevant today.

When using the arguments which are about to follow, the adviser must expect opposition from the Inspector, possibly along the lines of "commonsense arguments". Since when did the interpretation of tax law have anything to do with common sense?

Fishing for Profits

The early case of *Sutherland v CIR* 12 TC 63, concerned a company which owned a fishing vessel and used the vessel for its trade of drift fishing. The

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boat was compulsorily taken by the Admiralty and converted for use as a minesweeper. The company took no part in the minesweeping and received a charter fee from the Admiralty for the use of the boat.

The importance of deciding if the "new activity" represented a new or an extended activity, flowed from Rule 11 ITA 1918. Needless to say, a greater tax bill arose from an extended trade than from a new trade, so the Revenue naturally argued that the new minesweeping activities were an extension to the original trade of fishing!

Looking back at this case from 1993 it is difficult to accept that the charter rent could be within Case I Schedule D, let alone an extension to a trade of fishing. Times being hard, however, the Courts were anxious to assist the Exchequer and duly found for the Revenue.

To be fair to the Court, The Lord President did comment that "fishing was a different industry from minesweeping", which must count as one of the classic understatements to be found in Tax case law.

Despite this statement of the very obvious, the new activity was found to be an extension of the existing trade and the following important principles were laid down:

1) Employment of a company's assets for gain or profit, for whatever purposes, can represent one undivided trade.

2) The actual activities are unimportant, providing the assets are capable of adaption for the new use.

3) The principle applies to any "commercial assets" of the company.

How far do these principles extend? Could they be applied to a company's workforce, which in a period of slackness was used to produce profit (or loss) from some completely unconnected activity?

A Profits Explosion

The second case reviewed certainly seems to reinforce the broad line taken in the Sutherland case.

The case of *Howden Boiler & Armaments v Stewart* 9 TC 205 concerned a company which manufactured boilers in 1915. A substantial demand arose for explosive shells around this period of our history and the company obtained a contract from the French government to produce shells while continuing with boilermaking. It could be said that both shells and boilers are cylindrical, metallic, and liable to explode, but the similarities do seem limited.

The company used separate buildings and a separate workforce, and of course the shellmaking ceased in 1918 with the cessation of hostilities.

Despite any dissimilarities, both the Appeal Commissioners and the Court found that the new activity was an extension of the old.

For the purposes of this article it is interesting to look at the factors which the Commissioners and the Court found to be important:

1) The company Articles gave it the necessary powers to conduct the new activity.

2) The company had a common profit and loss account.

3) A common works manager was used for the two workforces.

4) The company had a single management, only the character and the extent of the business varied.

5) The company books evidenced a single trade.

Another Explosive Decision

The more recent case of *Cannon Industries Ltd v Edwards* 42 TC 625 has nothing to do with armaments, but does include a great deal of dicta which support the very early decisions already reviewed.

The company was part of a large group, and manufactured gas cookers etc. for sale to fellow subsidiaries and eventual sale onwards to wholesale customers. The company commenced a new activity, that of importing parts for electric foodmixers, assembling them, and selling them retail. As in earlier cases, the company claimed that the new activity was an extension of the original trade. The Court confirmed that an extension of the original trade had occurred, and the relevant factors were as follows:

1) The company minutes recorded the statement that the company had decided to "extend" its trade.

2) There was dual use of the company buildings.

3) There was a central purchase of materials.

4) The company had a single bank account.

5) The company had centralised accounting records.

6) The company used the same workforce.

7) The activities had the same overall management and control

The Conclusion

The internal management and control of a company is of more relevance than the nature of the activities, when considering whether a new activity represents an extension to an existing trade, or a brand new trade. The question may be of vital importance in a number of modern day situations.