TC04298

Appeal number: TC/2014/00401

FIRST-TIER TRIBUNAL
TAX CHAMBER

Corporation tax – loss relief on succession to trade – streaming of losses against profits of predecessor trade – interpretation of s 343(3) ICTA – Falmer Jeans v Rodin considered – HELD – No explicit streaming rules in s 343(3) – streaming could not be implied – succession gave rise to single surviving trade – all losses of predecessor available to successor – appeal allowed.

LEEKES LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE RACHEL SHORT
MR NICHOLAS DEE

Sitting in public at Royal Courts of Justice, the Strand London on 8 January 2015

Nikhil Mehta of Gray's Inn Tax Chambers instructed by Deloittes LLP for the Appellant

Elizabeth Wilson of Pump Court Tax Chambers instructed by the General Counsel and Solicitor to HM Revenue and Customs for the Respondents.

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DECISION

1. This appeal concerns the Appellant's right to claim relief for losses amounting to £1,655.756 in its corporation tax return for the year ending 31 March 2010 as a result of its succession to the business of Coles Limited (“Coles”) on 19 November 2009.

Background Facts.

2. The facts are not materially in dispute between the parties as set out in HMRC’s statement of case:

3. The Appellant, Leekes Ltd carries on a trade of running out of town department stores. At the relevant time it owned four stores, three in Wales and one in Wiltshire.

4. On 18 November 2009 the Appellant purchased the entire share capital of Coles of Bilston Limited for £1. Coles’ trade at that date comprised three furniture stores plus warehousing facilities in the west midlands. In the eight months of trading prior to the sale Coles had a turn-over of £12.7 million and its trading loss for the period was £950,321. It had trading losses carried forward of £2,262,120.

5. On 19 November 2009 the business of Coles was hived-up to the Appellant at fair value of £892,928. Coles became dormant following the transfer of its business and retained no liabilities. One of the Coles stores was renovated and re-opened in November 2010 selling the Appellant’s products. All three Coles stores were re branded as Leekes Ltd stores and continued to trade selling the same types of products. The three Coles stores sustained an aggregate trading loss of £176,258 for the accounting period ending 31 March 2010 according to Leekes Ltd’s accounts.

6. The Appellant’s corporation tax computation for the year ended 31 March 2010 showed overall adjusted trading profits of £1,655,756 offset against trading losses of the same amount said to have been brought forward under s 393 Income and Corporation Taxes Act 1988 (“TA 1988”). The Appellant stated in the notes to its tax computation that it had succeeded to the Coles trade and had losses available for offset under s 343 TA 1988 of £3,167,441 of which £1,655,756 were offset in the current period.

7. HMRC opened an enquiry into the Appellant’s corporation tax return for the period ended 31 March 2010. HMRC issued a closure notice on 17 September 2013 disallowing the losses claimed. The Appellant wrote to HMRC requesting a review on 15 October 2013. That review decision was issued on 20 December 2013 and confirmed the disallowance of the losses. The Appellant appealed to this Tribunal on 15 January 2014.

Evidence.

8. The Tribunal saw copies of;

(1) The Share Purchase Agreement relating to Cole of Bilston Limited dated 18 November 2009 between N A Cole and Others and Leekes Limited.

(2) The Asset Purchase Agreement relating to the business of Cole of Bilston Limited dated 19 November 2009 between Cole of Bilston Limited and Leekes Limited.

The Share purchase was made for nominal consideration of £1. No specific price was paid for the trading losses recognised in Coles' accounts.

Witness evidence.

9. We were provided with the witness statement of Mr Mike Fowler, Group Finance Director of Leekes Ltd, dated 15 July 2014 which was taken as read. Mr Fowler was not cross examined.

10. Mr Fowler explained Leekes Ltd's growth strategy in 2009 and its targeted geographical area for that growth, which was the midlands. He said that Leekes Ltd became aware that the Coles business was up for sale and knew that Coles and Leekes Ltd had a wide range of common brands and suppliers in the furniture sector and shared similar demographics in terms of customer base. He said that the firms had a similar history and that parallels between each company's customer base gave strong indications of the likely success of the Coles stores with enhanced product offerings.

11. Mr Fowler stated that Leekes Ltd decided there was no need to keep the Coles business as a separate trading entity, their stores could be operated within the same structure as the existing Leekes Ltd stores. After the acquisition the stores continued to sell substantially the same products and customers were served by the same staff. Unfortunately the results achieved by the Coles stores after the acquisition did not hit the projected sales figures.

The Law.

12. S337 TA 1988 sets out the tax effect of companies beginning or ceasing to carry on a trade:

> S337(1) *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*".

13. S 343 is the principal provision with which we are concerned and sets out the tax effects of a succession – **"Company reconstructions without a change of ownership:**

> 343(1) *Where, on a company ("the predecessor") ceasing to carry on a trade, another company ("the successor") begins to carry it on, and –*
>
> *(a) on or at any time within two years after that event the trade, or an interest amounting to not less than a three-fourths share in it belongs to the same persons as the trade, or such an interest belonged to at some time within a year before that event; and*
>
> *(b) the trade is not, within the period taken for the comparison under paragraph (a) above, carried on otherwise than by a company which is within the charge to tax in respect of it;*
>
> *then the Corporation Tax Acts shall have effect subject to subsections (2) to (6) below.*

In paragraphs (a) and (b) above references to the trade shall apply also to any other trade of which the activities comprise the activities of the first mentioned trade...........

S 343(3) Subject to subsection (4) below and to any claim made by the predecessor under s 393A(1), the successor shall be entitled to relief under s 393(1) as for a loss sustained by the successor in carrying on the trade, for any amount for which the predecessor would have been entitled to relief had it continued to carry on the trade.

14. Sections 343(8) and (9) deal with situations in which there has been a succession to something different than the trade of the successor company. HMRC accepted that these provisions were not in point in this case:

S 343(8) *where on a company ceasing to carry on a trade, another company begins to carry on the activities of the trade as part of its trade, then that part of the trade carried on by the successor shall be treated for the purposes of this section as a separate trade, if the effect of so treating it is that subsection (1) or (7) above has effect on that event in relation to that separate trade; and where on a company ceasing to carry on part of a trade, another company begins to carry on the activities of that part as its trade or part of its trade, the predecessor shall for the purposes of this section be treated as having carried on part of its trade as a separate trade if the effect of so treating it is that subsection (1) or (7) above has effect on that event in relation to that separate trade.*

S 343(9) *Where under subsection 8 above any activities of a company's trade fall, on the company ceasing or beginning to carry them on, to be treated as a separate trade, such apportionment of receipts, expenses, assets or liabilities shall be made as may be just"*

15. S393 deals generally with how companies can use losses against their taxable profits:

393(1) *Where in any accounting period a company carrying on a trade incurs a loss in the trade, the loss shall be set off for the purposes of corporation tax against any trading income from the trade in the succeeding accounting period; and (so long as the company continues to trade) its trading income from the trade in any succeeding accounting period shall then be treated as reduced by the amount of the loss, or by so much of that amount as cannot be relieved under this section or (if a claim is made under section 393A(1) under section 3939A(1) or section 393B(3)) against income or profits of an earlier accounting period*"

16. There is no dispute between the parties that there has been a "succession" for the purposes of s 343 ICTA 1988. We saw the closure letter from HMRC to the Appellant stating this dated 17 September 2013 which said:

"*I have agreed with your agents, Deloitte, that Leekes Ltd succeeded to the trade of Cole .... Consequently s 343(1) ICTA 1988 preserves the trade losses of Cole, allowing those losses to be set-off against the future profits of that trade. As explained in my letter of 16 May 2012 to Deloitte, s 343(3) ICTA 1988 only*

permits the successor (Leekes Ltd) to use the preserved losses against the profits of the separately identifiable trade that previously belonged to Cole"

17. This letter sets out the point in dispute which is whether losses made by Coles prior to succession are available to Appellant under s 343 (3) ICTA 1988 or whether they can only be used against profits of the Coles trade post succession, what the parties referred to as "streaming".

18. HMRC accepted in their statement of case and before the Tribunal that post succession Leekes Ltd carried on the trade of Coles "as an identifiable part of its expanded business" as that principle was set out in the *Bell v National Provincial Bank* case. (*Bell v National Provincial Bank of England Ltd* (5 TC 1))

19. There is no dispute that the other technical criteria for a succession to be treated as having occurred as set out in s 343 were met by Leekes Ltd and Coles.

20. In the main this appeal revolves around a question of statutory interpretation of legislation which has been on the UK statute book unchanged since 1965. Perhaps surprisingly there are no authorities which are directly relevant to the point of interpretation in question. Although a number of authorities were cited to us the parties accepted than none of these were directly relevant.

Taxpayer Arguments

21. The Appellant argues that both on a narrow approach, looking only at the terms of the legislation itself, and on a wider approach, taking account of various case authorities and the principles behind the legislation, there is no justification for restricting the losses which are available to the successor company Leekes Ltd as suggested by HMRC. The losses available are all of the losses stated in Coles' accounts as at the date of succession which could be used against the new combined trade of the two companies.

The Trade hypothesis

22. The Appellant accepts that there are two hypothesises underlying the application of s 343(3) – first that the successor should be treated as having incurred the losses in question "*as for a loss sustained by it in carrying on the trade*". That hypothesis in s 343(3) confers on the successor company an entitlement to losses equivalent to that available as if it had carried on the predecessor's trade itself.

23. The Appellant explained that many of the interpretive points made by HMRC to suggest that the trade referred to in the first limb of s 343 was a separate trade, being the trade originally carried on by Coles, were relevant only in situations in which what had been transferred was something less than the trade of the predecessor company, so that the predecessor trade could no longer be identified; in that situation s 343(8) referred to the *activities of a trade*, which was intended to cover situations, as in *Falmer Jeans*, when the profit making apparatus of a trade had not been transferred. (*Falmer Jeans Ltd v Rodin* (63 TC 55)) It was in these specific circumstances only that "streaming" was intended to apply, not as here, where a whole trade had been succeeded to. Where s 343(1) and s 343(3) apply and there is an identity of trade before and after the succession, there is no restriction of losses which can be offset against the same, but enlarged, post succession trade.

The Quantum Hypothesis

24. The Appellant does not accept that it is possible to interpret s 343(3) as giving rise to a restriction in the quantum of losses available by reference to the profits of the predecessor either before or after the succession. Even if it is correct that "the trade" in the second limb of s 343(3) is a reference to the predecessor's original trade, the reference in s 343(3) to "*any amount for which the predecessor would have been entitled to relief*" only takes account of the quantum of the losses available and is not intended to extend to considering what, if any, profits the predecessor might have had against which those losses could be utilised. This hypothesis is intended to ensure that the amount of loss available for relief is the amount which the predecessor would have been entitled to had it continued to carry on the trade. The "relief" available, via s 393 TA 1988 is relief against the profits of the new trade; it is not measured or capped by the profits of the predecessor's trade.

Lack of clear statement that streaming required.

25. If parliament had intended losses to be streamed under s 343(3), specific wording would have been required in the legislation as was in fact provided in s 343(8). Moreover there is no reason in principle why the full amount of the losses should not be available against the new combined trade. The "real" losses from the Coles trade should be available to be offset against the "real" profits from the combined trade post succession. S 343 is intended to be a relieving provision; had Coles continued to trade it would have been able to use these losses against its future profits and there is no reason that Leekes Ltd as the successor company should be put in a worse position.

Case authorities

26. The Appellant referred to the *Laycock v Freeman Hardy & Willis Ltd* (22 TC 288) and *Briton Ferry Steel Co Ltd v Barry* (23 TC 414) cases stressing that they were both considering pre-1965 legislation in which it was in HMRC's interests to argue that there had been a succession to bring profits of the predecessor companies into tax. In their view, the judgement of Sir Wilfrid Greene MR in the *Briton Ferry* case recognised the artificiality of splitting a newly acquired business from an existing business when deciding whether there had been a succession:

> "*it is obvious that where somebody.......who is already carrying on a business, acquires a business from somebody else and continues to carry it on, difficult questions must arise, because in the ordinary course of business, if the business acquired is carried on, it becomes, to a greater or lesser extent, merged in fact in the old business of the company. It may alter its character; and the reality of the matter is that, as from the date of such an acquisition, there is one business and one business only, namely the business of the person who is carrying it on................That is the fact of the matter, that one company is carrying one business, but the sub rule directs us to regard the position in a different light..............*(Wilfrid Greene MR at page 429)

Splitting the successor business into two separate parts is an artificial exercise rather than a reflection of a fundamental approach of the tax legislation. That artificial splitting should only be applied in limited circumstances where it is required by statute. In other cases it is necessary to consider "the reality of the whole matter" as was made clear in the *Aviation & Shipping* decision. (*Aviation & Shipping Co, Ltd v Murray* (39 TC 595))

27. The only relevant decision on the post 1965, new version of the succession rules is the *Falmer Jeans* decision; the Appellant stressed that that case did not concern the

general succession rules at s 343 (1) and (3) but the specific rules at s 343(8) where something other than a "trade" had been succeeded to. However the Appellant considered that Millet J's decision in that case made it clear that s 343(1) and s 343(8) and (9) are mutually exclusive and it is not correct to assume that the post 1965 legislation was intended to replicate the law as it stood when the *Freeman Hardy Willis* and *Briton Ferry* cases were decided so any extrapolation from those cases needs to be considered very carefully:

> "*I have analysed s 252 [now s 343] and in particular subsection 7 [now 8] at some length because, in my view, such an analysis shows that a major purpose of the sub sections is to carry forward relief in situations not covered by subsection (1); specifically in situations where (i) the trading activities formerly carried on by the predecessor are carried on by the successor but would be differently described when the successor's trade is described as a whole and (ii) where the profits from those activities are realised in the form of global receipts which do not distinguish between the different activities by which they are earned*" Millett J at page 71 para L in *Falmer Jeans.*

28. The Appellant's view is that its transaction falls within example 1 of the sets of facts considered by Millett J at page 69 para G of his judgment "*where a predecessor has ceased to carry on a trade and the successor has begun to carry it on*" since this is a "whole trade" succession it falls within s 343(1) and there is no question of any streaming being applied.

HMRC Arguments

The Trade Hypothesis

29. HMRC's argument is that s 343(3) on its face refers to a succession to "a trade" that trade being the trade of Coles and that therefore in determining what losses are available to be taken over by the successor company, only the losses which would have been available to Coles as a "relief" under s 393 in its trade had the succession not occurred are taken account of. HMRC's interpretation of s 343(3) is that "the trade" referred to twice in the final phrase of that section can only be "the trade" of Coles.

30. HMRC rely in particular on the description of a succession given in the *National Provincial Bank* case "*He had the old one (business) before. He has the old one still and the new one in addition and to that new one he had succeeded*". On this analysis s 343(3) applies only in situations such as the one there described where there is a readily identifiable trade which has been succeeded to. In other circumstances, if there is no readily identifiable trade, where there has been a merger post succession, s 343 (8) not s 343(3) will be in point.

31. HMRC say that the intention of s 343 as a relieving provision is not to put a successor company such as Leekes Ltd in a better position than it would have been in had the succession not occurred by giving it access to losses of another trade, but to ensure that losses which have been incurred in the predecessor, Coles' trade, should not be lost as a result of the change of ownership. HMRC are clear that losses have to be matched to "the trade" to which Leekes Ltd has succeeded and that is the trade of Coles only. HMRC argue that their approach gives effect to the legislative policy behind s 343 as made clear by the streaming provisions in s 343(8) and (9) and as supported by statements made in the *Falmer Jeans* case by Millett J

" [s 343(1)] does not require the successor to begin to carry on the trade which it has acquired as a separate trade. The subsection is clearly satisfied where the successor does so; but it may also be satisfied where the successor begins to carry it on as part of its trade.......... but if Sir Wilfrid Greene's reasoning is adopted, the subsection would not be satisfied in the situation which occurred in Laycock v Freeman Hardy Willis and is probably not satisfied in the present case" Millett J at page 70 paragraph E.

It is necessary to identify the trade to which the successor has succeeded, that is the trade of the predecessor, not the new combined trade of the successor company. Losses have to be matched to the trade to which the company has succeeded.

32. HMRC referred to the statements of Sir Wilfrid Greene MR in the *Freeman Hardy & Willis* case where he referred (at page 299) to "*The profits or gains are the profits or gains earned by means of a trade to which the taxpayer in question has succeeded. Accordingly, the question arises; is it possible to put the finger upon some taxable profits arising from a trade, and say of those profits that they arise from a trade which was taken over* ?"

33. Ms Wilson described this as following the profits, or putting your finger on the trade to which you have succeeded. In this she was following her approach of identifying a separate post-succession trade to which the losses should attach.

The Quantum Hypothesis

34. In determining what losses are available by way of relief to Coles, HMRC suggest that it is not sufficient to take the quantum of losses shown in Coles' accounts at the time of the succession. It is also necessary to consider what actual relief would have been available to Coles at that time, s 343(3) refers to "*as for a loss sustained by the successor for any amount which the predecessor would have claimed as relief*"; if, as here, the original company was making losses and would have had no profits against which losses could have been claimed by way of relief, the answer to what losses are available to the successor company is nil.

35. HMRC's starting point is to look at s 393 as applied to Coles prior to the succession and ask what relief would have been available to Coles. Since Coles had no profits for the period, no relief is available under s 393 and therefore there are no losses to which s 343(3) can apply. In determining what losses are available to the successor company, it is necessary to treat the original company's trade as a continuing separate trade after the succession and losses can only be claimed to the extent that that continuing trade gives rise to profits.

36. HMRC specifically protest against the Appellant's approach which suggested that s 343(3) meant that the successor was treated as having made the losses in question; that was not the effect of the statutory wording in s 343(3). The primary purpose of s 343 is to remove the restriction on claiming the losses of a trade which has ceased; its purpose is not to give access to those losses to an entity which has not been involved in generating them.

Identifying the post succession trade and its profits

37. This line of argument led HMRC to a number of hypothesises to sustain their approach to interpretation, including how the profits of the original company's trade

should be ascertained post-succession. HMRC insisted that this was both a correct and feasible approach, if not always straightforward and cited authorities in particular *Freeman Hardy Willis* as evidence for the need for this to be done.

38. In HMRC's view the practical issues with ascertaining what the notional profits of the predecessor company were post succession did not mean that some kind of streaming should not be applied; a transfer pricing type approach could be used to help. The fact that profits were in fact pooled post succession did not mean that the trade could not be treated separately for tax purposes (see for example the *Briton Ferry* case).

Lack of clear wording to indicate that streaming required

39. HMRC argue that no specific wording is required in s 343 to state that profits needed to be streamed against the predecessor's trade because that can be implied into s 343 and is implicit in the machinery of s 393, which only gives loss relief against a particular trade.

***Discussion*.**

40. We have concluded that the Appellant's interpretation of s 343(3) is to be preferred to that of HMRC. This is for three main reasons: (i) it recognises that there is no explicit reference to a requirement to stream losses in s 343(1) and (3) (ii) it avoids the extensive deeming and practical difficulties of application which are the unavoidable result of HMRC's approach (iii) it provides an approach to the legislation which is more closely aligned to commercial reality.

Starting principles

41. The legislation under consideration here is relatively old and, as accepted by both parties, not drafted as clearly as might have been hoped. HMRC referred to the drafting as "succinct".

42. We have taken as a starting principle that the usual approach of the UK tax legislation is to assume that one taxpayer carries on one trade and that any move away from that assumption might be expected to be clearly stated assuming a competent draftsman; Millett J in the *Falmer Jeans* case referred to the "*skill and economy of language which has been employed by the draftsman*" of the relevant provisions. We have also taken account of the statements of Sir Wilfrid Greene MR in the *Briton Ferry* case that, post succession, the fact of the matter is that there is only one business and that any tax legislation which relies on a separation of businesses (and or trades) after a succession is making an artificial distinction which does not reflect commercial reality.

Case authorities

43. Despite lengthy citations from case authorities provided by both parties, we do not consider that there is anything in any of the authorities which provides definitive guidance on the point at issue here; the authorities, including *Falmer Jeans*, casting at best a sideways light onto how s 343(3) should be interpreted. We do think that there are some helpful comments in Millett J's analysis in the *Falmer Jeans* case, including in particular his comments that s 343(1) is intended to apply where the successor carries on some or all of the trading activities of the predecessor and, importantly, that it is not required that the successor begins to carry on the trade which it has acquired as a separate trade (*Falmer Jeans* at page 70 para E Millett J) and that subsection (1)

and subsection (8) of s 343 are mutually exclusive, rather than subsection (8) being a clarification or explanation of subsection (1).

44. The question as to whether there had been a succession for s 343 purposes is not in dispute. The basic premise of the relieving provision in s 343(1) (combined with s 337) is that if one company ceases to carry on a trade and another begins to carry it on, the trade of original company has disappeared. The underlying assumption of s 343(1) is that in the usual case a succession will lead to a single new trade. Any suggestion that the two trades are combined as a result of a succession but that nevertheless they should still be treated as identifiable parts for the purposes of identifying tax losses is counter to this starting principle.

45. Our main concern with HMRC's approach is that having accepted that there has been a succession, their arguments depend on the survival of the predecessor's trade, even when it has been amalgamated with the trade of the successor. HMRC's support for this approach came primarily from the *National Provincial Bank* case, which is based on the pre-1965 laws concerning the tax treatment of successions when it was required to identify a separate trade post succession. The focus of the court in the *National Provincial Bank* case was not whether a separate trade continued post succession, but whether the original trade had been "wiped out of existence" as a result of the acquisition of the target business.

46. We think that there are statements even in the *National Provincial Bank* case which are counter to HMRC's arguments; including that: "*What difference does it make that that person who succeeds to the concern should himself already have an existing business ? Does he the less succeed to the new one because of the old one? It seems to be certainly not. He had the old one before. He has the old one still and the new one in addition, and to that new one he has succeeded"* Indeed it is on that analysis of a succession that HMRC accepted (as set out in their letter of 17 September 2013) that there had been a succession in this case.

47. HMRC's suggestion that it was possible to do some kind of tracing exercise and "put your finger on" the profits from the original trade is also counter to this approach. Our view is that a distinction needs to be made between a standard succession to which s 343(3) applies and the arguments on which HMRC rely which are derived from the *Falmer Jeans* and *Freeman Hardy Willis* cases which were not standard succession cases but cases in which something less than or different from an identifiable trade had been transferred to the successor. We agree with the Appellant on this point that for this reason it is incorrect to extrapolate from the principles applied in those cases to the facts under consideration here. We do not accept that other than in succession cases to which s 343(8) applies there is any clear authority for a requirement to trace through profits post succession.

Statutory interpretation

48. The issues between the parties came down a question of statutory interpretation and we have approached this on basis that if there is more than one interpretation of the legislation, we should prefer the result which is most in line with commercial reality and gives rise to less need for recourse to legal fictions, or the "mountains of fictions" referred to in the *Aviation & Shipping Company* case.

49. We accept that s 343(3) on its face involves at least two hypothesises, what we have called the trade hypothesis and the quantum hypothesis "*the successor shall be entitled to relief under s 393(1),* ***as for a loss*** *sustained by the successor in carrying on the trade, for any amount for* ***which the predecessor would have been entitled*** *to*

relief had it continued to carry on the trade" but the question is how far those are intended to be taken.

The Trade Hypothesis

50. It is clear that s 343(3) is drafted with a situation in mind in which the successor company takes on the original company's trade and there is no existing trade of the successor with which the predecessor trade is amalgamated. In those circumstances there is only one trade, and it is one and the same trade in the hands of the original company and the successor company. We do not think that there is anything in the statutory wording which gives any clear guidance either way as to how the legislation is intended to work if the successor has an existing trade to which the original trade is added.

51. Cases, and in particular the *National & Provident Bank* case are very clear that it is possible for there to be a succession in these circumstances. The result of a succession is that the predecessor's trade ceases at the moment of succession and becomes the trade of the successor. We consider this to be the result of the interaction of s 337 and s 343. Therefore, any subsequent entitlement to losses under s 393 can only be an entitlement of that single entity.

52. If a succession does not result in a single trade, then s 343(8) is the relevant section but HMRC have said that this is not in point here. We do not think it is possible to both argue for streaming and argue that s 343(8) is not in point; either there is a single trade being carried on, and s 343(1) is in point, with no streaming because the assumption is that post succession there is only one trade, or there are two separate things going on; an activity and a trade but then the relevant legislation is s 343(8). Any suggestion that streaming is implicit in s 343(3) but explicit in s 343(8) needs to offer an explanation for the different drafting approach between those two sections; HMRC's answer to this is to limit the application of s 343(1) to circumstances where the succession has resulted in two separately identifiable trades. We do not consider that this interpretation is in line with the most natural reading of s 343(1) or with the authorities in this area including the statements of Millett J in *Falmer Jeans.*

53. If the result of a succession is that there is one on-going trade, that trade can only be the trade of the successor. For that reason we agree with the Appellant's approach to the "trade hypothesis" in s 343(3). Our view is that the first limb of s 343(3) should be read as meaning that the losses should be available "*as if the successor had sustained the losses in the post succession trade"*.

The Quantum Hypothesis

54. We agree that having identified "the trade" as the successor's trade in the first limb of s 343(3), there is an argument for consistency that "the trade" referred to in the second limb of s 343(3) must also be the successor's trade. However, even if HMRC is correct and the trade which is referred to here is Coles' trade, our view is that the "quantum hypothesis" cannot be taken as far as looking at the actual profits of Coles' trade post succession or indeed for any later periods. That seems to us to ignore the commercial reality of what has occurred, an approach which should be avoided (see *Aviation & Shipping Company*).

55. We have considered how s 343(3) could be applied if HMRC's interpretation is correct and a separate trade needs to be traced and its profits streamed after a succession has occurred. If the original trade makes no profits in the year of

succession (as target businesses often will not), then there will never be any losses available for the succession rules to apply to in the succession year and s 343(1) and s 343(3) are otiose in this situation. Equally, how would the rules then be applied for later years, firstly to determine whether the original business had made profits, which would be counterfactual once the succession had occurred, and at what stage would the losses from the original business be recognised and why ? HMRC did not provide any realistic answer to these points.

56. In this instance because of the geographic location of the acquired business, it was possible to physically identify a separate trade after the succession and more realistic to identify a separate stream of profits. But the fact that these particular circumstances make it more straightforward to identify a separate stream of profits can have no implications for what is in principle the correct interpretation of this legislation. In many instances a succession will mean a loss of identity for the acquired trade, as was recognised in the *National Provincial Bank* case and the legislation needs to be able to provide a sensible answer in those circumstances.

57. For these reasons we agree with the Appellant that s 343(3) cannot be read so as to give rise to a restriction in the quantum of losses available by reference to the profits available in the notional trade of the predecessor post succession.

Other points of interpretation

58. Both parties set out arguments which involved extrapolations from other parts of s 343 (especially s 343(8)) other parts of the tax legislation and the principles which might or might not apply to loss relief. We have treated these as second order arguments and do not consider that they should be determinative of the issue here. We do not accept that because streaming is applied in circumstances when the old trade and the new trade are not the same (as in *Falmer Jeans*) it must necessarily follow that there is no streaming when the old and the new trades form part of the same trading activities.

59. However, we do accept that if streaming was intended to apply for the purposes of s 343(1) this should be made explicit in the legislation as it is in s 343(8). We do not agree with HMRC's argument that streaming can be implied into s 343 if, as is the case here, it has been accepted that there has been a succession. To this extent the statements of Millett J in *Falmer Jeans* support the Appellant and our conclusion that the streaming rules in s 343(8) are not an extension of s 343(1) and (3) but are discrete stand alone provisions which are intended to apply in very specific situations in which s 343(1) would not apply.

Conclusion

60. For these reasons we have concluded that the preferable interpretation of s 343, on the premise that a succession has occurred, is that all the losses of the predecessor's trade which has been subsumed with the successor's trade should be available for offset against the combined profits of the successor company. Leekes Ltd's appeal is therefore allowed.

61. 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 "Guid-

ance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

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RACHEL SHORT
TRIBUNAL JUDGE

10 **RELEASE DATE: 27 February 2015**