Press Summary

20 November 2024

R (on the application of Cobalt Data Centre 2 LLP and another) (Appellants) v Commissioners for His Majesty's Revenue and Customs (Respondent)

[2024] UKSC 40

On appeal from [2022] EWCA Civ 1422

Justices: Lord Briggs, Lord Sales, Lord Burrows, Lady Rose, Lord Richards

Background to the Appeal

This appeal concerns the conditions for the availability of the initial 100% capital allowances ("**EZA**") regime arising from expenditure incurred in the construction of buildings in an enterprise zone under the Capital Allowances Act 2001 ("**the 2001 Act**"). In particular, it concerns section 298(1) of the 2001 Act which provides that the time limit for expenditure on the construction of a building is "(a) 10 years after the site was first included in the zone, or (b) if the expenditure is incurred under a contract entered into within those 10 years, 20 years after the site was first included in the zone". The judgment refers to years 1 to 10 as "**the first period**" and to years 11 to 20 as "**the second period**".

The Appellants ("**the taxpayers**") argue that the expenditure they incurred for the construction of data centres was "under a contract entered into within those 10 years" within the meaning of section 298(1)(b) and they are therefore entitled to tax relief under the EZA regime. The Respondent ("**HMRC**") resists this by arguing that the expenditure fell outside the time limits.

By way of background, the Tyne Riverside Enterprise Zone, which included the Cobalt Business Park ("**the Site**"), was established for the period 19 February 1996 to 18 February 2006. In early 2006, the Site's owner, Atmel, realising that the enterprise zone would soon be coming to an end, took steps to preserve the ability to claim EZAs in respect of future construction work at the Site. Amtel therefore incorporated two wholly owned and controlled special purpose companies: Highbridge North Tyneside Developer One Ltd ("**the Developer**") and Highbridge North Tyneside Contractor One Ltd ("**the Contractor**").

On 17 February 2006, two days before the deadline specified in section 298(1) of 10 years after 19 February 1996, the Developer and the Contractor entered into a type of building contract which has come to be known as a golden contract. The contract has been labelled "**the Golden Contract**" in these proceedings. The distinguishing feature of a golden contract is that, rather

than prescribe a single construction project which the contractor undertakes to carry out, it sets out a range of alternative construction projects, each described in detail, between which the developer is entitled to (and must) choose, by service of a notice upon the contractor.

The Golden Contract gave the Developer the right of selection of one out of six specified projects, called Works Option 1 to Works Option 6. The Golden Contract incorporated the conditions of the JCT Standard Form of Building Contract with Contractor's Design 1998 Edition ("**the JCT Standard Form**") with certain specified amendments agreed by the parties. By clause 12 of the JCT Standard Form as incorporated in and amended by the Golden Contract ("**clause 12**"), the Developer was given a right to change the design, quality or quantity of "**the Works**" included in the detailed specifications within each Works Option.

At various times between February 2009 and April 2011 (falling within the second period), the Developer purported to exercise both the right to select and the right to change under clause 12. The Developer and the Contractor also purported during this period to vary the Golden Contract so as, amongst other things, to enable the Developer to select more than one of the specified Works Options. As a result, the Contractor built three buildings, called DC1, DC2 and DC3. The buildings differ in significant respects from the subject matter of any of the Works Options set out in the Golden Contract in its original form.

In April 2011, the taxpayers purchased the benefit of the Golden Contract from the Developer in relation to DC2 and DC3. In their tax returns for the year 2010-2011, the taxpayers claimed for capital allowances under the EZA regime pursuant to section 298(1)(b) of the 2001 Act, arguing they had incurred expenditure under the Golden Contract in respect of DC2 and DC3 ("**the Relevant Expenditure**"). Using DC2 as an illustration, the Second Appellant claimed capital allowances in the sum of £153 million.

By notices issued on 28 July 2016, HMRC denied the taxpayers' EZA claims. The Upper Tribunal allowed the taxpayers' appeal, holding that the Developer's expenditure on each of DC2 and DC3 was incurred under the Golden Contract within the meaning of section 298(1)(b). The Court of Appeal allowed HMRC's appeal. The taxpayers now appeal to the Supreme Court.

Judgment

The Supreme Court unanimously dismisses the appeal. The Court holds that section 298(1)(b) only allows capital allowances under the EZA regime to be claimed for expenditure where, on the tenth anniversary of the site being included in the enterprise zone, there is a contractual relationship under which the expenditure had either been agreed upon in terms, or it arose from building work on that site which the developer by then had a contractual right to require. The Relevant Expenditure does not meet this test. Lord Briggs and Lord Sales give the judgment, with which the other members of the Court agree.

Reasons for the Judgment

The issues which arise for decision by the Court are as follows **[11]**:

> (i) Was the Relevant Expenditure triggered by the exercise of the Developer's unilateral rights to select and to change conferred by the Golden Contract in its original form? ("The Clause 12 Issue")
>
> (ii) If not, does section 298 on its true construction enable expenditure, incurred by reason of a variation during the second period of a contract originally made in the first period, to be treated as expenditure incurred under the original contract? ("The section 298 Issue")
>
> (iii) If it does, was the Relevant Expenditure triggered by a variation or by a replacement of the Golden Contract? ("The Variation Issue")

The Court begins by considering the section 298 Issue **[58]**. The taxpayers first put forward a procedural objection that the Court should not consider this issue at all. The taxpayers argue that as HMRC did not raise this argument in the Upper Tribunal it is too late now, and would be an abuse of process, for HMRC to rely on it **[59]**. The Court rejects this objection as, amongst other reasons, HMRC advanced this argument in the Court of Appeal and the taxpayers did not object to it at that stage, and it is not open to them to object to it for the first time before the Supreme Court **[60]-[68]**. Additionally, as the Court considers the Court of Appeal was wrong on this issue, it is in the public interest that the law should be clarified by the Supreme Court **[69]**.

On the substance of the section 298 issue, the Court explains that the interpretation of statutes, and taxing statutes in particular, requires close attention to the purpose of the provision in issue, and a realistic view of the transaction to which it is alleged to apply **[70]**. The Court considers section 298's statutory context and a statement made by the Government when enterprise zones were created **[77]-[79]**. From this context, the Court concludes that the purpose of the time limit in section 298 is that the construction of buildings attracting 100% capital allowances should have occurred, or been the subject of contractual commitment, within the 10-year period of the site being included in the enterprise zone **[83]**.

The Court holds that both the taxpayers' and HMRC's proposed interpretations of section 298(1) fail to give effect to its purpose **[84]-[93]**. The Court holds that an alternative interpretation of section 298(1)(b) is correct. On this interpretation, to determine whether expenditure falls within the time limit in section 298(1)(b), one must ask the following question: was there by the tenth anniversary of the Site being included in the enterprise zone, a contractual relationship under which the relevant expenditure had either been agreed upon in terms, or which arose from building work on that site which the Developer had a contractual right to require for example by the exercise of the right to select and and/or the right to change? If, and only if, the answer to that question is "yes" was the expenditure incurred "under a contract entered into within those 10 years" as required by section 298(1)(b) **[95]**.

In this appeal, the Relevant Expenditure was incurred in the building of DC2 and DC3. However that expenditure may be viewed, as a package or two packages, there was not on the tenth anniversary date (19 February 2006) a contractual commitment in terms to incur that expenditure. This means that the only way for the Relevant Expenditure to be covered by section 298(1)(b) is if it was validly achieved by the exercise by the Developer of its rights to select and to change, i.e. if the taxpayers succeed on the clause 12 issue **[104]**.

The Court holds that the taxpayers fail on the clause 12 issue **[108]-[124]**. The Golden Contract gives the Developer a right to select one of six different buildings, identified in each Works Option **[118]**. On its proper interpretation, clause 12 permits changes to the design, quality and quantity, attributable to that building. Clause 12 does not extend, as the taxpayers submitted, to changing from one (already selected) building to another specified in a different Works Option, still less to choosing some completely different type of building, on a different site, outside the confines of any of the six Works Options **[118].** The result of this reasoning is that the appeal should be dismissed.

On the Variation Issue, the Court explains that as the operation of section 298 does not depend on whether the changes were a variation or a replacement of the Golden Contract, this issue does not strictly arise for the Court's determination **[15], [161]**. However, as the issue of how to determine whether a change is a variation or replacement has been fully argued in the appeal, the Court considers it to be of sufficient public importance to address it at the level of principle **[15]**. The Court states that whether a change amends the principal agreement or discharges and replaces it depends on the intention of the parties **[129]-[149]**. However, it is possible for there to be exceptional cases where the Court will not give effect to the parties' intention if it brings the law into disrepute and damages its legitimacy in the eyes of the public **[147]**. The Court

acknowledges this is a somewhat vague standard which does not precisely identify the limits of parties' ability to specify that a change to a contract is a variation rather than replacement, but the court deals with practical legal questions and does not seek to provide exhaustive abstract statements of the law **[149]**.

For these reasons, the Court dismisses the appeal and concludes that on the proper interpretation of the 2001 Act the Relevant Expenditure was not incurred under a contract made before the end of the first 10 year period, as required by section 298(1) **[162]**.

References in square brackets are to paragraphs in the judgment.

NOTE:
This summary is provided to assist in understanding the Court's decision. It does not form part of the reasons for the decision. The full judgment of the Court is the only authoritative document. Judgments are public documents and are available at: Decided cases - The Supreme Court