TC02593

Appeal number: TC/2010/01916

Income tax - loss relief claimed from sole trader film distribution activity. Issues arising: (1) Was the Appellant carrying on a trade; (2) Was business carried on on a commercial basis; (3) Was business carried on with a view to the realisation/reasonable expectation of profit; (4) Were the profits calculated in accordance with GAAP; (5) What would profits calculated in accordance with GAAP have been; (6) Was the expenditure incurred wholly and exclusively for the business.

FIRST-TIER TRIBUNAL
TAX CHAMBER

PATRICK DEGORCE **Appellant**

- and -

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

TRIBUNAL: JUDGE J. BLEWITT
C. E. FARQUHARSON

Sitting in public at Bedford Square, London on 1, 2, 3, 4, 8 and 9 May 2012 and 15 June 2012.

Mr Jonathan Peacock QC leading Mr Jolyon Maugham, Counsel, instructed by Field Fisher Waterhouse LLP for the Appellant.

Mr Michael Gibbon QC leading Mr Michael Jones, Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents.

DECISION

Introduction

1. This reference concerns the Appellant's self-assessment for the year ended 5 April 2007 which showed a net loss for tax purposes in the sum of £20,151,186. The Appellant claimed loss relief in respect of his sole trader film distribution activity and set £18,849,319.70 of that loss against other income in that year (the remainder of the loss being carried forward) for the difference between the purchase price of film rights and the value of those rights.

2. Where the legislation applicable has since been repealed we will deal with the law as it was during the period relevant to this case. Schedule D of the Income and Corporation Taxes Act 1988 ("ICTA") provides for tax to be charged on the annual profits or gains arising or accruing to a resident of the UK from any trade, profession or vocation. The tax charge is classified into six Cases of Schedule D. Case I applies to tax in respect of the annual profits or gains arising from any trade which is carried on in the UK by any person.

3. This reference arises from HMRC decision to amend the Appellant's self-assessment tax return on the basis that the sole trade activity did not give rise to Case I trading losses.

Background

4. This case involves the purchase and subsequent assignment of rights in two films; *Tropic Thunder* and *The Love Guru* on 5 April 2007.

5. Mr Degorce is one of twelve Related Appellants who participated in such transactions which led to HMRC opening enquiries on 22 June 2007 into their tax returns for the year ended 5 April 2007.

6. On 18 May 2009, following an application made by the taxpayers under section 28A (4) of the Taxes Management Act 1970 ("TMA") the Tribunal directed HMRC to issue closure notices in respect of the enquiries by 16 August 2009.

7. On 14 August 2009 closure notices were issued by HMRC to three of the Related Appellants. Notices of Appeal were lodged with HMRC on behalf of those Related Appellants in September 2009.

8. Mr Degorce and the remaining eight Related Appellants were informed by HMRC on 14 August 2009 that closure notices would not be issued to them as enquiries continued pertaining to unrelated aspects of their tax returns.

9. On 9 February 2010 a joint referral of questions to the Tribunal, pursuant to s 28ZA TMA 1970 was agreed between all parties. The Notices of Referral were filed with the Tribunal on 24 February 2010.

10. On 19 May 2010 HMRC served a Statement of Case which set out the questions referred.

11. On 25 January 2011 the Tribunal issued a direction under Rule 18 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 specifying Mr Degorce's case as a lead case and staying the cases of the eleven other Related taxpayers.

12. The questions referred were:

(a) Whether any Case 1 trade losses arise from the sole trader film distribution activity; and

(b) If so, the amount allowable for tax purposes.

13. At the hearing, both parties agreed that the issues to be determined (as set out at paragraph 12 above) should be answered by reference to the following questions:

(i) Whether, during the year ended 5 April 2007, Mr Degorce carried on a trade;

Irrespective of our findings on this question, we were invited to consider the following points:

(ii) Whether the trade was carried on on a commercial basis;

(iii) Whether the trade was carried on with a view to the realisation of profits and, if so whether it was carried on so as to afford a reasonable expectation of profit;

(iv) Whether the profits of the trade, if any, for the year of assessment 2006-2007 were calculated in accordance with generally accepted accounting practice ("GAAP");

(v) If the profits of the trade were not calculated in accordance with GAAP, what would those profits have been had they been calculated in accordance with GAAP;

(vi) Whether the expenditure of the Taxpayer on the rights in the films was wholly and exclusively laid out or expended for the purposes of the trade.

A Summary of the Transactions and Relevant Parties

Principal Parties

14. Mr Degorce entered into a complex set of transactions in relation to the acquisition and assignment of film rights and also in relation to the financing of that acquisition. It may be helpful at this stage to identify the principal parties involved.

Patrick Degorce	A hedge-fund manager and the Lead

	Appellant ("Appellant") in this case
Christopher Petzel	A media entrepreneur with Fierce Entertainment
Goldcrest Film Distribution Limited ("GDistribution")	The assignee from Mr Degorce of certain distribution rights in the films
Goldcrest Film Rights Limited ("GFilm")	The assignor of certain distribution rights in the films to Mr Degorce
Goldcrest Funding Limited ("GFunding")	The provider of loan funding to Mr Degorce
Goldcrest Pictures Limited ("GPictures")	The supplier of film and advisory services to Mr Degorce
Mazars LLP ("Mazars")	A UK limited liability partnership which provided Goldcrest with valuations of the film rights and which was instructed to prepare accounts for the taxpayers participating in the transactions relevant to this appeal.
Adam Kulick	Corporate Finance Executive employed by Goldcrest Film Finance

HMRC's Case

15. It was HMRC's case that the sole trade activity did not give rise to Case 1 losses in the year ended 5 April 2007. HMRC contended that Mr Degorce was involved in a tax avoidance scheme ("the Goldcrest Film Scheme" / "Goldcrest Pictures Scheme" or "the Scheme"), the primary aim of which was to generate artificial income tax losses for the participants and fees for Goldcrest. HMRC did not argue that the transactions entered into by Mr Degorce were a sham, but submitted that in determining whether or not Mr Degorce was carrying on a trade the Tribunal must examine the transactions in their entirety and assess the reality of the arrangements.

16. HMRC contended that the Scheme was designed to generate losses for the individual participants by ensuring that the film rights were acquired by the individual participants at a price which would far exceed the value of the future net income stream received in return for the onward sale of the film rights. It was for this reason that the price of the film rights was vastly increased between purchase by an entity of Goldcrest called Upsticks based in the BVI from Paramount and sale of those rights to GFilm (prior to their sale to individual participants of the Scheme such as Mr

Degorce). The losses generated in respect of the participants did not represent true economic loss and the Scheme was intended to allow the participants to attain leverage for their losses through the use of limited-recourse financing. HMRC contended that GFunding's recourse under the loan agreement was limited to the distribution revenues received by the individual taxpayer.

17. HMRC contended that the Scheme had three main drivers:

(a) The primary goal as far as the individual participants were concerned was to generate income tax losses to shelter their taxable income for 2006-2007;

(b) In respect of Paramount, the Scheme represented a means by which it could sell a limited share in the distribution proceeds of its films for what it considered to be a reasonable price for such a share;

(c) As regards Goldcrest, the Scheme generated fee income from the individual participants.

18. HMRC pointed to the terms of the transactions which demonstrate the circular movements of money over the course of one day and the lack of any real control exercised by Mr Degorce over the Rights.

19. It was submitted that the composite transaction of Mr Degorce was not of a trading nature. HMRC contended that even if Mr Degorce is found to have carried on a trade in 2006-2007, that trade was not carried on on a commercial basis with a view to the realisation of profits or so as to afford a reasonable expectation of profit.

20. HMRC further contended that the profits of the trade for the year of assessment 2006-2007 were not calculated in accordance with GAAP and that the expenditure by Mr Degorce on the film rights was not wholly and exclusively laid out/expended for the purposes of the trade.

The Appellant's Case

21. The Appellant submitted that he was carrying on a single trade of acquiring and exploiting film distribution rights and that between 2005 and 2009 he acquired and exploited six different tranches of film rights.

22. Mr Degorce (and those appointed by him) exercised, on a commercial basis, discretion as to which films or territories to acquire and formed a commercial view about the right price for those Rights following negotiations.

23. Mr Degorce contended that he sought to make a profit from his exploitation of the Rights and that the accounts were properly prepared in accordance with UK GAAP.

24. It was submitted that HMRC's assertion that the Scheme had an overall fiscal purpose is irrelevant and does not lead to the conclusion that Mr Degorce was not carrying on a trade or that such trade was carried on on a non-commercial basis.

25. The cost to Mr Degorce of acquiring the Rights was an expense that was wholly and exclusively incurred by him for the purpose of his trade of acquiring and on-selling film distribution rights. Even if (which is not accepted) money was expended for primarily fiscal reasons, that fiscal motivation does not prevent the expenditure being wholly and exclusively incurred for the purpose of its trade.

The Evidence

26. We had a substantial amount of documentary evidence before us as the hearing of the appeal. In addition we heard oral evidence from the following witnesses:

- Mr Patrick Degorce (in addition to his two written witness statements dated 14 October 2011 and 26 April 2012);
- Mr Christopher Petzel, on behalf of the Appellant (in addition to his witness statement dated 14 October 2011);
- Mr John Graydon, an expert instructed on behalf of the Appellant (who also produced 3 written reports dated 14 October 2011, 2 May 2012 and 2 May 2012);
- Mr Michael Thornton, an expert instructed on behalf of HMRC (who also produced a written report dated 29 February 2012);
- Mr Richard Cannon, an expert employed by HMRC (who also produced 2 written reports dated 29 February 2012 and 30 April 2012).

27. We were also provided with a joint statement prepared by Mr Graydon and Mr Cannon which set out a list of issues upon which agreement had been reached and those upon which the experts remained in dispute, more about which we will say in due course.

28. We should note at this point that where the terms "resale/sale" are used in this decision, we are referring to the second limb of the transaction whereby Mr Degorce assigned the rights he had purchased. Also, our use of the word "scheme" is not intended to prejudge any issues in this case, but rather is used for ease of reference.

Authorities

29. We were provided with a significant number of authorities to which we will refer in due course.

Relevant Statutory Provisions

30. There was no dispute between the parties as to the legislation applicable in this case which can be summarised as follows: Mr Degorce's claim was made under the Income and Corporation Taxes Act 1988. Section 380 (1) ICTA 1988 provides that relief is allowed:

"Where in any year of assessment any person sustains a loss in any trade, profession, vocation or employment carried on by him either solely or in partnership."

31. The only definition of "trade" is found in s 832 (1) ICTA:

"In the Tax Acts, except in so far as the context otherwise requires..."trade" includes every trade, manufacture, adventure or concern in the nature of trade."

32. S 384 (1) ICTA qualifies the provision for claiming relief as follows:

"... a loss shall not be available for relief under section 380 unless for the year of assessment in which the loss is claimed to have been sustained, the trade was being carried on on a commercial basis and with a view to the realisation of profits in the trade..."

33. Section 384 (9) ICTA clarifies that where a trade is carried on so as to afford a reasonable expectation of profits, it will be treated for the purposes of s 384 (1) as being carried on at that time with a view to the realisation of profits.

34. A claim can be carried back under s 381(1) ICTA where an individual carrying on a trade sustains a loss in the trade, subject to s 381 (4) which states that relief shall not be given under sub-s 1 unless the taxpayer's trade was carried on on a commercial basis and in such a way that profits in the trade could reasonably be expected to be realised in that period or within a reasonable time thereafter.

35. Therefore, in order to make a claim for loss relief the Appellant must satisfy the requirements of ICTA that:

(a) A loss was sustained in a trade carried on by him;

(b) That the trade was carried on on a commercial basis; and

(c) With a view to a reasonable expectation of profit.

36. In determining this reference the Tribunal was invited to consider whether the expenditure of the Appellant on the rights in the films was wholly and exclusively laid out or expended for the purposes of the trade as required by s 34 (1) Income Tax (Trading and Other Income) Act 2005 ("ITTOIA").

GAAP and Case I trading profits

37. Section 42 (1) Finance Act 1998 provides that Case I profits of a trade must be computed in accordance with generally accepted accounting practice ("GAAP"), more about which we will say in due course.

A Summary of the Transactions

The Scheme Mechanics

38. The following is intended to provide the background to the scheme and an outline of the transactions entered into by Mr Degorce and is taken from the facts, agreed by both parties in this appeal. Where the facts set out were disputed, we have either dealt with the issue at a later stage as the contentious fact relates to the issues to be determined, or we have set out our findings below, having taken the view that the findings are not material to the issues to be determined. We should note that any views expressed in relation to taxpayers other than Mr Degorce on the basis of documentary evidence, are made in order that the reader may fully understand the wider context of the Scheme and that in determining the issues in this case, we have focussed our attention on the transactions specific to Mr Degorce, having heard no direct evidence in respect of the eleven Related Appellants.

39. The various Goldcrest companies identified in this case form part of the Goldcrest Group of companies which, since its establishment in 1977, has financed, produced and/or distributed over 100 titles including *Gandhi, The Killing Fields, Chariots of Fire* and *Room with a View* that have won numerous prizes including Academy Awards and British Academy of Film and Television Art Awards.

40. On or around 2 April 2007 the Appellant received a letter in relation to a "Goldcrest Business Proposal" from Ms Karina Challons, who worked in the Specialist Tax Group of HSBC Private Bank. The letter set out information about the Goldcrest Film Scheme and recorded certain details about the Appellant's financial position, including that his 2006-2007 UK taxable income "is in excess of £19m". Ms Challons also stated:

> "Whilst the trade is carried on with a view to being a profitable venture, it is likely that a loss will arise in the first Accounting Period due to Generally Accepted Accounting Principles ("UK GAAP")".

41. The letter went on to set out significant amounts of information relating to the intended tax treatment of the proposal.

42. The letter made clear that HSBC Private Bank was acting as an intermediary between the Appellant and Goldcrest and that it was to receive an introducer's fee for doing so, which would be paid by Goldcrest.

43. On 2 April 2007 the Appellant signed an Acceptance Form for GPictures. This recorded a "Payment Amount" of £21,923,456 (being the "Purchase Price" as stated on the "Rights Purchase List", plus 8% of the Purchase Price). The Purchase Price was in respect of rights in the film *Star Trek XI*. The additional 8% which was the interest due to accrue on the outstanding principal amount of the loan amounted to £1,623,959. The initial payment on acceptance was to be £4,823,160 (which was equal to 22% of the Payment Amount; the remaining 78% was to be financed by the Appellant by means of a loan). By the Acceptance Form the Appellant authorised

GPictures as attorney to sign what were defined as "Relevant Agreements" (in effect, all documents necessary for the Appellant to execute in order to participate in the scheme), and he agreed to confirm and ratify the execution of all Relevant Agreements.

44. On 2 April 2007 the Appellant applied to GFunding for a loan. The application recorded a "Payment Amount" of £21,923,456 (being "the Purchase Price, plus 8% of the Purchase Price, as stated on the Rights Acceptance Form which forms part of Schedule 1"), and an initial payment made on acceptance of £4,823,160 (being "equal to 22% of the Payment Amount if you intend to take out a Loan").

45. On 2 April 2007 PG Trustees Limited, a Guernsey company, acquired control of a BVI company called Upsticks Limited ("Upsticks") at the request of lawyers to the Goldcrest group. Although not accepted by the Appellant, we found as a fact that Upsticks was to be provided with a £25,000 fee for its role in the Scheme, as evidenced by the document "Transaction Summary Goldcrest: Paramount" (in bundle E5 headed "Documents received from Goldcrest") which stated:

> "Upsticks will therefore have paid…to 5555,…to Grace Productions LLC. It will then pay to Goldcrest Pictures by way of a transaction fee £1,456,194 which will leave the company with a £25,000 day one fee."

The £25,000 was also evidenced by an email dated 19 April 2007 from Mr Kulick requesting "£25,000 to be transferred from GFF LLP to the account below as compensation for Upsticks Limited" and a further email dated 20 April 2007 which had the subject "Upsticks Payment" and confirmed that the payment had been instructed via BACS.

The Film Rights Movements through the Scheme Structure

46. An email exchange between Goldcrest and Paramount timed at 01.26 and 02.57 on 4 April 2007 led to the identity of the films which would be purchased by the Appellant and other "traders" (email from Mr Kulick at 02.57) being finalised:

(email 01.26 from D. Friedman at Paramount to Mr Kulick)

> "We have just concluded our meeting and we still would like to withdraw (blank). Please proceed with the contingency plans for Tropic Thunder and then Love Guru if necessary."

It was after the Appellant had paid his contribution to GPictures that Paramount finalised the identity of the films to be used in the scheme, as evidenced by an email dated 4 April 2007 at 14:41 from Mr Kulick to the Appellant:

> "…Unfortunately Revolutionary Road is no longer available. Angus, Tropic Thunder and Love Guru all have availability. When would you like to discuss?"

To which the Appellant replied (at 15:30 on the same day):

"…may be lets do after 5 to be sure mr petzel is out of his bed…"

And a further email at 15:36 from Mr Kulick to the Appellant which stated:

"…By the way, your cash contribution has just arrived"

47. On 4 April 2007 the Goldcrest group provided the Appellant with a "Financial Analysis and Valuation" in respect of both *The Love Guru* and *Tropic Thunder*. Each document gave financial details in relation to what were described by the Goldcrest group as "comparable" films, and provided under the heading "Valuation" details of a Purchase Price and a Payment Amount (respectively, £11,810,646 and £12,755,498 for *The Love Guru*, and £8,779,120 and £9,481,450 for *Tropic Thunder*). The document also stated that the "financial illustrations set out above are for illustrative purposes only and are not a forecast of future returns."

48. Grace Productions LLC ("Grace") (a Paramount entity) entered into four deeds with Upsticks (the "Head Acquisition Deeds") in relation to Film Rights for certain territories of *The Love Guru, Revolutionary Road, Angus Thongs and Full Frontal Snogging* and *Tropic Thunder*. Although the Appellant did not agree the price as contended by HMRC and found in the Head Acquisition Deed for each film, in the absence of any evidence to the contrary we accepted those figures.

49. Clause 3.1 of each of the four Head Acquisition Deeds provided that all sums were to be paid to a sterling account in the name of Grace at JP Morgan Chase on London Wall. Payment of £6,300,011 was made by GFilm (from its sterling account) to Grace.

50. In each case Upsticks was obliged under Clause 3.3 of each of the four Head Acquisition Deeds "as a separate obligation" to pay Grace 94.54% of all sums received by it from GFunding pursuant to a loan agreement made between 5555 Communications Inc (a Paramount entity), as lender and GFunding as borrower ("the 5555 Loan Agreement").

51. Upsticks entered into four deeds with GFilm in relation to the same film rights ("the Acquisition Deeds" with which we were provided). GFilm was to pay Upsticks (in each case "in the manner provided for in the Payment Instructions")*:*

> (a) £12,967,428 for *The Love Guru* (being £1,705,826 and US$22,219,249 at an exchange rate of 1.9730:1 (USD:GBP));
>
> (b) £12,382,777 for *Revolutionary Road* (being £1,628,910 and US$21,217,380);
>
> (c) £7,349,660 for *Angus* (being £966,821 and US$12,593,341);
>
> (d) £15,192,014 for *Tropic Thunder* (being £1,998,445 and US$26,030,893).

52. The aggregate of the purchase prices for those film rights under the Acquisition Deeds was £47,891,933, being £6,300,002 and US$82,060,863 (the latter being the 5555 Loan).

53. This amount was "full and final consideration for the Rights and Materials assigned and transferred". In each case, 13.15% of the overall price was to be paid in sterling and the reminder by an apportionment of the US$82,060,863.

54. By the 5555 Loan Agreement, 5555 lent GFunding US$82,060,863 ("the 5555 loan") "to enable the borrower to enter into the Sole Trader Loan Agreements (i.e. the limited recourse loans to the participants in the Scheme) and make available loans to the Sole Traders to enable the Sole Traders to acquire certain distribution rights in certain of the Films." We were satisfied from the documentary evidence that the Loan Agreement document demonstrated that GFunding irrevocably instructed 5555 to pay the loan to an account in GFunding's name at Coutts. The making of the loan was expressed to be subject to conditions precedent, including the delivery to the lender of fully executed:

- Distribution Agreements for all of the individual participants in the Scheme;
- Acquisition Agreements;
- Studio Distributor Agreements;
- Head Acquisition Agreements;
- Sub-Acquisition Agreements for all of the individual participants in the Scheme.

55. By a "Loan Purchase Agreement" 5555 sold the 5555 Loan and the benefit of the 5555 Loan Agreement to Upsticks for a purchase price of US$82,060,863. Clause 2.1 of the Loan Purchase Agreement provided that the purchase price was to be made into an account of Paramount Pictures Corporation re 5555 Communications Inc at JP Morgan Chase on London Wall and, although not accepted by the Appellant, we found as a fact from the documentary evidence available that no cash passed between Upsticks and 5555; the sum of US$82,060,863 was paid to 5555 by GFilm.

56. Notwithstanding the purchase by Upsticks of the benefit of the 5555 Loan, Upsticks remained subject to the obligation in the Head Acquisition Deeds to pay to Grace 94.54% of all sums it might receive from GFunding in respect of the 5555 Loan, leaving Upsticks with 5.46% of such sums.

57. On 5 April 2007, the Appellant entered into, inter alia, the following agreements:

(a) A Film Advisory Agreement dated 5 April 2007 pursuant to which GPictures was to provide the Appellant with advisory services for a fee of £1,623,959.60 plus a performance fee equal to 2% of receipts received from the exploitation of the distribution rights;

(b) A Loan Agreement with GFunding pursuant to which GFunding agreed to advance the sum of £17,100,295 to the Appellant exclusively for the purpose of his acquiring certain distribution rights (the "GFunding Loan"). Accompanying this was an irrevocable direction that the amount

be paid by GFunding straight to the GPictures dollar account. Interest was to accrue on the outstanding principal amount of the loan at a rate of 8% per annum.

(c) One of the conditions precedent for the advance of the loan was the full execution of the Distribution Agreement between the Appellant and GDistribution;

(d) A Deed of Security Assignment in respect of the Loan Agreement with GFunding;

(e) A Sub-Acquisition Deed with GFilm, pursuant to which GFilm assigned to the Appellant all its rights, title and interest in:

- *Love Guru* in the territories of the USA, Canada, Scandinavia, France, Ireland, Far East, Eastern Europe and Other; and
- *Tropic Thunder* in the territories of the USA and Canada

For a term of 60 years commencing on 5 April 2007, for a total price of £20,299,495.

(f) A Distribution Agreement to assign to GDistribution the distribution rights in the films that the Appellant had purchased from GFilm for a term commencing on delivery of a Laboratory Access Letter in respect of the Films and concluding on 5 April 2067. The consideration for the assignment was:

(i) 100% of all Distribution Receipts (as defined therein) until the Distribution Receipts equalled 32.3% of the Purchase Price; and

(ii) Thereafter 100% of the remaining Distribution Receipts (to be on the basis of Net Proceeds.)

The term "Distribution Receipts" was defined in the Distribution Agreement as "all sums actually and indefeasibly received by [GDistribution] from the exploitation of the Distribution Rights pursuant to the Sub-Distribution Agreements".

(g) A Deed of Security Assignment in respect of the Distribution Agreement with GDistribution.

(h) Payment Directions agreeing that any monies which the Appellant was entitled to under the Distribution Agreement were to be paid by GDistribution as follows:

(i) 55% to GFunding until the GFunding Loan was repaid;

(ii) 2% to GPictures in respect of the performance fee under the Film Advisory Agreement; and

(iii) The remaining 43% to the Appellant.

(i) A Notice of Assignment pursuant to which the Appellant notified GDistribution that, inter alia, he had assigned by way of security to

GFunding the right to receive the monies he was entitled to receive under the Distribution Agreement and the benefit of his rights under the Distribution Agreement.

(j) Two Short form Assignments in respect of each of the Sub-Acquisition Deed and the Distribution Agreement.

58. In addition to the services that were provided to him under the Film Advisory Agreement, the Appellant took advice from Mr Petzel of Fierce Entertainment – a media entrepreneur based in Los Angeles, more about whom we will say later.

59. GDistribution entered into "Sub-Distribution Agreements" in respect of *The Love Guru, Revolutionary Road, Angus Thongs and Full Frontal Snogging* and *Tropic Thunder* under which GDistribution agreed to assign the rights in the films to Paramount Pictures Corporation "in consideration for an entitlement to Defined Proceeds in Respect of the Rights" for a term commencing on delivery of a Laboratory Access Letter in respect of the relevant films and concluding on 5 April 2067. Pursuant to the "Defined Proceeds Entitlement" Paramount Pictures Corporation was to apply the "Defined Proceeds" during the Term in the following order and manner:

(a) Until Defined Proceeds equalled 97% of the Purchase Price, Paramount Pictures Corporation was to retain 66.67% of 100% of the Defined Proceeds;

(b) Until Defined Proceeds equalled 97% of the Purchase Price, Paramount Pictures Corporation was to pay amounts equal to 33.33% of the Defined Proceeds to or at the direction of GDistribution;

(c) Once Defined Proceeds equalled 97% of the Purchase Price, 100% of the remaining Defined Proceeds are thereafter to be retained by Paramount Pictures Corporation;

(d) Paramount Pictures Corporation was thereafter to pay to or at the direction of GDistribution, an amount equal to 33.33% of "Net Proceeds", until repayment of the 5555 Loan in full; and

(e) Upon repayment of the 5555 Loan in full, Paramount Pictures Corporation was thereafter to pay to or at the direction of GDistribution, an amount equal to 15% of the Net Proceeds until the end of the term.

60. The link between the amount paid to GDistribution under the Sub-Distribution Agreement and the amounts payable to the Appellant under the Distribution Agreement meant that if/when the 5555 Loan has been repaid the Appellant would be entitled to a maximum 15% share of the proceeds of the rights in the Films he assigned to GDistribution. This was not accepted by the Appellant, however we were satisfied that the Sub-Distribution agreement reflected this and an email from Mr Kulick to Paramount dated 25 March 2007 confirmed the same, stating:

"…For purposes of clarity, please find below our understanding of some of the commercial deal points.

> …Our Sole Traders recoup on an Adjusted Gross Basis from the territory until they have received 15% net of any loan repayments and Studio Distributor recoups to 85% of direct costs (no studio overhead); thereafter we split net receipts on a 15%/85% basis…)"

61. By letter dated 16 April 2007, GFunding wrote to the Appellant stating that "Goldcrest Funding Limited ("the Lender") is pleased to confirm acceptance of your application for a loan facility (the "Facility") under the terms of the Loan Agreement between the Lender and yourself". The limit was expressed to be $33,738,881, and the loan was expressed to be "for the exclusive purpose" of purchasing certain distribution rights in *The Love Guru* and *Tropic Thunder*. The letter stated "We can confirm that the funds were released in accordance with your instructions on or before 5 April 2007 for the stated purpose."

62. On 1 May 2007 the Appellant signed an Acceptance Form for GPictures. This recorded a "Payment Amount" of £21,923,454 (being the "Purchase Price" as stated on the "Rights Purchase List", plus 8% of the Purchase Price). The Purchase Price was made up of £11,520,375 for rights in various territories in The Love Guru and £8,779,120 for rights in the various territories in Tropic Thunder. The additional 8% amounted to £1,623,959. The initial payment on acceptance was to be £4,823,160 (equal to 22% of the Payment Amount as the Appellant intended to take out the loan). By the Acceptance Form the Appellant authorised GPictures as attorney to sign what were defined as "Relevant Agreements" (in effect, all documents necessary for the Appellant to execute to participate in the transaction), and he agreed to confirm and ratify the execution of all Relevant Agreements. This Acceptance Form was a replacement for the one signed by the Appellant on 2 April 2007. The "Payment Amount" recorded (£21,923,454) differed by £2 from the "Payment Amount" recorded in the original Acceptance Form (£21,923,456). In each case the payment on acceptance was exactly the same: £4,823,160. The price paid by the taxpayers to Goldcrest far exceeded that paid by Upsticks to obtain the same rights from Paramount, as evidenced by the Head Acquisition Agreements and Sub-Acquisition Agreements provided to us.

63. *Tropic Thunder* £8,779,120 was released in the USA on 13 August 2008. Gross US box office receipts were approximately $110,416,702. To date, the Appellant has not received any economic return from the rights he purchased in *Tropic Thunder*.

64. *The Love Guru* for £11,520,375 was released on 20 June 2008. Box Office receipts totalled approximately $40,863,344 worldwide. To date the Appellant has not received any economic return from the rights he purchased in *The Love Guru*.

Valuation of the Distribution Rights held in the Films

65. An email dated 13 April 2007 shows contact between Goldcrest and accountants MRI Moores Rowland (who at or around that time became part of Mazars LLP, and therefore will be referred to hereinafter as "Mazars") with a view to (a) preparing accounts for the taxpayers' participation in the transactions for the period 5 April 2007, and (b) providing valuations of the Film Rights in respect of the Films.

66. On or around 14 June 2007, further to the instructions and information provided by Goldcrest as the Appellant's agent, Mazars provided financial statements for the Appellant for the period 2 April to 5 April 2007. The accountants' report was made to the Board of GPictures, not to the Appellant. It stated that "Goldcrest Pictures Limited have acknowledged their duty to ensure that Patrick Degorce has kept proper accounting records and to prepare financial statements that give a true and fair view". Mazars LLP reported to the board of GPictures and stated that they valued the rights in the Films held by the Appellant at the end of 5 April 2007 as follows:

(a) The rights in *Tropic Thunder* in the territories of North America and Canada at £380,487; and

(b) The rights in *Love Guru* in the territories of North America, Canada, Iceland, Scandinavia, France, Far East, Eastern Europe and Other (Israel, Middle East, Turkey, West Indies, India/Pakistan and airlines) at £501,310.

67. Based on valuations of the rights held by the Appellant, the accounts showed a "provision made against cost of films rights acquired" of £19,417,698 under cost of sales, expenditure on professional fees of £1,609,426, and bank fees of £1,000, and an overall net loss of £21,028,124.

The Appellant's Tax Return for the Year Ending 5 April 2007

68. The Appellant's tax return for the year ended 5 April 2007 was filed on 25 January 2008. Within his tax return, the Appellant included a set of self-employment pages.

69. The box entitled "Sales/business income (turnover)" was left blank. The expenses item headed "Costs of sales" included the figure £19,417,698.00. In addition, allowable legal and professional costs and finance charges were claimed. His loss for tax purposes was stated to be £20,151,186.00.

70. The stated loss of £20,151,186.00 was offset against other income of £18,849,319.70 which arose in the tax year, leaving a loss of £1,301,866.30 to be carried forward.

The Issues

71. We were invited to consider a number of issues in this case and we will deal with each in turn, noting that on some matters the evidence overlapped. Whilst it is our intention to set out the evidence which led to our findings of fact, we must note that it would be a not insignificant and potentially unhelpful task to simply repeat all that we heard and read. In those circumstances we took the approach of summarising the relevant evidence and submissions.

Was the Appellant carrying on a trade?

72. This was the main issue in the case regarding which we heard a significant amount of evidence and submissions.

73. In the absence of any statutory definition of "trade" beyond that found in s 382 ICTA 1988 we were referred to a number of authorities, which it may be helpful to deal with at this stage. We considered all of the authorities cited and relied on by the parties which are too numerous to set out in any detail. Consequently, we have set out below those which we found provided the most assistance.

74. In *Ransom v Higgs* [1974] STC 539 ("*Ransom*") (per Lord Reid) it was stated:

> "The Income Tax Acts have never defined trade or trading farther than to provide that trade includes every trade, manufacture, adventure or concern in the nature of trade. As an ordinary word in the English language 'trade' has or has had a variety of meanings or shades of meaning. Leaving aside obsolete or rare usage it is sometimes used to denote any mercantile operation but it is commonly used to denote operations of a commercial character by which the trader provides to customers for reward some kind of goods or services.
>
> …It is, however, in my view a question of law as to what is the meaning of "trade"...
> In considering whether a person 'carried on' a trade it seems to me to be essential to discover and to examine what exactly it was that the person did....To be engaged in trade or in an adventure in the nature of trade surely a person must do something and if trading he must trade with someone."

75. The case of *Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes)* [1989] STC 705 ("*Ensign*") provided the following guidance:

> "The production of a film, or the completion of an uncompleted film (or, I might add, the purchase of a completed film), in each case with a view to its distribution and exploitation for profit, are all typical (though highly speculative) commercial transactions in the nature of trade. It is with those words 'for profit' that the questions in the present case are primarily concerned.
>
> ....I take the law to be as follows:
>
> (1) In order to constitute a transaction in the nature of trade, the transaction in question must possess not only the outward badges of trade but also a genuine commercial purpose.
> (2) If the transaction is of a commercial nature and has a genuine commercial purpose, the presence of a collateral or ulterior purpose to obtain a tax advantage does not 'denature' what is essentially a commercial transaction. If, however, the sole purpose of the transaction is to obtain a fiscal advantage, it is logically impossible to postulate the existence of any commercial purpose.
> (3) Where commercial and fiscal purposes are both present, questions of fact and degree may arise, and these are for the commissioners. Nevertheless, the question is not which purpose was predominant, but whether the transaction can fairly be described as being in the nature of trade.

(4) The purpose or object of the transaction must not be confused with the motive of the taxpayer in entering into it. The question is not why he was trading, but whether he was trading. If the sole purpose of a transaction is to obtain a fiscal advantage, it is logically impossible to postulate the existence of any commercial purpose. But it is perfectly possible to predicate a situation in which a taxpayer whose sole motive is the desire to obtain a fiscal advantage invests or becomes a sleeping partner with others in an ordinary trading activity carried on by them for a commercial purpose and with a view of profit.

(5) The test is an objective one...

(6) In considering the purpose of a transaction, its component parts must not be regarded separately but the transaction must be viewed as a whole. That part of the transaction which is alleged to constitute trading must not be viewed in isolation, but in the context of all the surrounding circumstances. But this must mean all relevant surrounding circumstances; that is to say, those which are capable of throwing light on the true nature of the transaction and of those aspects of it which are alleged to demonstrate a commercial purpose.

(7) If the purpose or object of a transaction is to make a profit, it does not cease to be a commercial transaction merely because those who engage in it have obtained the necessary finance from persons who are more interested in achieving a fiscal advantage from their investment. Even where the trader is the creature of the financier, the two activities are distinct and the object of one is not necessarily the object of the other.

(8) In FA & AB Ltd v Lupton, Lord Morris said ([1972] AC 634 at 647,47 TC 580 at 620):

'It is manifest that some transactions may be so affected or inspired by fiscal considerations that the shape and character of the transaction is no longer that of a trading transaction. The result will be not that a trading transaction with unusual features is revealed but that there is an arrangement or scheme which cannot fairly be regarded as being a transaction [in the nature of trade].'

In my judgment this is the true significance of a fiscal motive. Fiscal considerations naturally affect the taxpayer's evaluation of the financial risks and rewards of any proposed venture, and are often the decisive factor in persuading him to enter into it. First-year allowances, enterprise zones, government grants and the like operate as financial inducements to businessmen to engage in commercial activities which would be financially unattractive or unacceptably speculative without them. Such motivations, even if paramount, do not alter the character of the activities in question. But while a fiscal motive, even an overriding fiscal motive, is irrelevant in itself, it becomes highly relevant if it affects, not just the shape or structure of the transaction, but its commerciality so that, in Lord Morris's words, 'the shape and character of the transaction is no longer that of a trading transaction'. But nothing less will do.

(9) Accordingly, in my judgment, and adapting the words of Lord Simon in Thomson v Gurneville ([1972] AC 661 at 679, 47 TC 633 at 679), the question is whether, in the light of all relevant circumstances, the transaction is capable of being fairly regarded as a transaction in the nature of trade, albeit one

intended to secure a fiscal advantage or even conditioned in its form by such intention; or is incapable of being fairly so regarded but is in truth a mere device to secure a fiscal advantage, albeit one given the trappings normally associated with trading transactions."

76. The case also clarified that:

"It is not the law that a transaction the paramount (but not the sole) object of which is to obtain a fiscal advantage cannot be a trading transaction."

77. In the Court of Appeal it was said:

"What is the ultimate question?
To summarise my views on the law in this case the position, in my judgment, is as follows:
(A) Whether a transaction is to be classified as commercial normally falls to be determined objectively by reference to the nature of the transaction itself ie is it a transaction of a kind similar to transactions of the same nature in the commercial world and carried out in a similar way.
(B) In addition to the outward badges of trade, in order to be a trading transaction its purpose must be commercial.
(C) The question 'was it trading?' is a question of fact for the commissioners.
(D) In deciding that question, the commissioners must look at the transaction as a whole including the steps taken for its implementation.
(E) The commissioners must decide whether the transaction was in reality merely a device to secure a fiscal advantage or a genuine trading activity.
(F) The ultimate question always remains 'what was the purpose of the transaction?' That question will normally be answered by an objective analysis of the transactions viewed as a whole.
(G) If the appearance of the matter (as shown by an objective analysis of the transactions) is equivocal, the subjective intention of the taxpayer is relevant in determining the purpose of the transaction and will generally be decisive.
(H) A transaction can be equivocal and therefore evidence of subjective intention relevant even if there was a possibility of the transaction producing a commercial profit (as opposed to a tax benefit) to the taxpayer.
(I) Although the purpose of the other party or parties to the transactions (being part of the circumstances) is relevant, the question in each case is whether the taxpayer was trading. Just because the other party to the transaction in question may have no fiscal object and viewed from his angle the transaction is one by way of trade, it does not follow that the taxpayer as a party to the same transaction is also engaged in trade.
(J) If the sole purpose of the transaction is to gain a fiscal advantage, in law that cannot amount to trade.
(K) If the transaction has some commercial features but also an element of fiscal advantage, it is for the commissioners to weigh the conflicting elements to decide whether the transaction was entered into by the taxpayer for essentially commercial purposes but in a fiscally advantageous form or essentially for the purpose of obtaining a fiscal advantage under the guise of a commercial

transaction. In the former case, the transaction would constitute trading; in the latter it will not."

78. The case of *Marson v Morton* [1986] STC 463 (at 470) ("*Marson*") set out that:

"...a single, one-off transaction can be an adventure in the nature of trade."

79. The case also went on to set out a number of features which can assist a Court in determining such issues; often referred to as "badges of trade":

"The matters which are apparently treated as a badge of trading are as follows:
(1) That the transaction in question was a one-off transaction. Although a one off transaction is in law capable of being an adventure in the nature of trade, obviously the lack of repetition is a pointer which indicates there might not here be trade but something else.
(2) Is the transaction in question in some way related to the trade which the taxpayer otherwise carries on? For example, a one-off purchase of silver cutlery by a general dealer is much more likely to be a trade transaction than such a purchase by a retired colonel.
(3) The nature of the subject matter may be a valuable pointer. Was the transaction in a commodity of a kind which is normally the subject matter of trade and which can only be turned to advantage by realisation, such as referred to in the passage that the chairman quoted from Reinhold? For example, a large bulk of whisky or toilet paper is essentially a subject matter of trade, not of enjoyment.
(4) In some cases attention has been paid to the way in which the transaction was carried through: was it carried through in a way typical of the trade in a commodity of that nature?
(5) What was the source of finance of the transaction? If the money was borrowed that is some pointer towards an intention to buy the item with a view to its resale in the short term; a fair pointer towards trade.
(6) Was the item which was purchased resold as it stood or was work done on it or relating to it for the purposes of resale? For example, the purchase of second-hand machinery which was repaired or improved before resale. If there was such work done, that is again a pointer towards the transaction being in the nature of trade.
(7) Was the item purchased resold in one lot as it was bought, or was it broken down into saleable lots? If it was broken down it is again some indication that it was a trading transaction, the purchase being with a view to resale at profit by doing something in relation to the object bought.
(8) What were the purchasers' intentions as to resale at the time of purchase? If there was an intention to hold the object indefinitely, albeit with an intention to make a capital profit at the end of the day, that is a pointer towards a pure investment as opposed to a trading deal. On the other hand, if before the contract of purchase is made a contract for resale is already in place, that is a very strong pointer towards a trading deal rather than an investment. Similarly, an intention to resell in the short term rather than the long term is some

indication against concluding that the transaction was by way of investment rather than by way of a deal. However, as far as I can see, this is in no sense decisive by itself.

(9) Did the item purchased either provide enjoyment for the purchaser (for example, a picture) or pride of possession or produce income pending resale? If it did, then that may indicate an intention to buy either for personal satisfaction or to invest for income yield, rather than do a deal purely for the purpose of making a profit on the turn. I will consider in a moment the question whether, if there is no income produced or pride of purchase pending resale, that is a strong pointer in favour of it being a trade rather than an investment.

I emphasise again that the matters I have mentioned are not a comprehensive list and no single item is in any way decisive. I believe that in order to reach a proper factual assessment in each case it is necessary to stand back, having looked at those matters, and look at the whole picture and ask the question—and for this purpose it is no bad thing to go back to the words of the statute—was this an adventure in the nature of trade? In some cases perhaps more homely language might be appropriate by asking the question, was the taxpayer investing the money or was he doing a deal?"

80. In taking into account the principles derived from authorities set out above and others to which we were referred, our approach to the issue as to whether or not the Appellant was trading was as follows:

(1) To consider the badges of trade, bearing in mind that such features, where present, are not necessarily determinative of the issue;

(2) We bore in mind that even where an ulterior (even paramount) motive to obtain a tax advantage is present, this does not automatically "denature" a commercial transaction;

(3) To determine the question of trade as a matter of law and thereafter consider whether, on the facts, a trade existed;

(4) The test is an objective one;

(5) That the transaction must be analysed as a whole and viewed in the context of its surrounding circumstances where that context assists in determining the true nature of the transaction;

(6) To ask ourselves "What did Mr Degorce actually do?"

Badges of Trade: Summary of Submissions

(a) That the transaction in question was a one-off transaction

81. It was submitted by HMRC that there was no element of repetition within the April 2007 Goldcrest Scheme when viewed from the taxpayers' perspective; participation was confined to a single composite transaction each.

82. HMRC contended that the transaction amounted to the purchase by the Appellant of the potential income stream on the basis that the transactions in which

the Appellant was involved were planned and executed as a whole and that the Appellant was left (as with other Scheme participants) holding rights to a potential net income stream from certain films for a term of up to 60 years, the nature of which was fixed under the terms of the Distribution Agreement and the income from which was contingent upon:

- Whether Paramount decided to exploit the films in question (absolute discretion on its part found in documents such as the Sub-Acquisition Deed between GDistribution and Paramount);
- The success of the films;
- The quantum of the manifold deductions that fell to be made against any of the film proceeds before any share of the income went to the Appellant.

83. HMRC invited us to only consider the year 2006-2007 and submitted that the Appellant's participation in previous years in Ingenious Film Partners LLP and Ingenious Film Partners 2 LLP are under enquiry on the basis that those LLPs are considered by HMRC to be part of film-based tax schemes and about which no facts are before us. Furthermore, it was submitted by HMRC that the Appellant's involvement with Goldcrest Schemes in subsequent years are also under enquiry on the basis that they repeat the acquisition of potential income streams in 2006-2007.

84. On behalf of the Appellant it was submitted that Mr Degorce's involvement in similar transactions prior to 2006-2007 and (as a sole trader) subsequent to 2006-2007, combined with his unchallenged evidence that he had been exploring opportunities in the film sector points to a badge of trade.

85. It was contended that to disregard the Appellant's actions both prior to and post the instant transactions would be to ignore the context in which the Appellant's activities in 2006-2007 take place.

(b) Is the transaction in question in some way related to the trade which the taxpayer otherwise carries on?

86. HMRC highlighted that the transaction carried out by the Appellant, which resulted in the lump sum purchase of the potential income stream for a 60 year term bears little (if any) relation to his occupation as a hedge fund manager. HMRC submitted that it was a new activity taken up at the close of the 2006-2007 tax year and as such was not an existing trade.

87. To the contrary, the Appellant argued that this badge points towards a trade when viewed in the context of the Appellant's prior involvement in Ingenious Film Partners LLP and Ingenious Film Partners 2 LLP, which they say were "trading transactions involving the production of a slate of films, and for development, distribution, sales and rights and library acquisitions". In addition, the Appellant had been exploring opportunities in the film sector up to and including 2006-2007.

(c) The nature of the subject matter

88. Both parties agreed that the question posed in *Marson*: "was the transaction in a commodity of a kind which is normally the subject matter of a trade and which can only be turned to account by realisation...?" points toward a badge of trade. It must be noted that although HMRC accepted in principle that a potential income stream could be the subject matter of trade, it is not accepted that the Appellant traded in such.

(d) Was the transaction carried through in a way typical of the trade in a commodity of that nature?

89. HMRC contended that the Appellant's composite transaction cannot be viewed as having been carried through in a way typical of trade. It points to the acquisition of the potential income stream without any subsequent resale, relying on *Ransom v Higgs* for the proposition that "trade...presupposes a customer...you must trade with someone..."

90. The Appellant disagreed and argued that the cases of *Ensign Tankers, HMRC v Halycon Films LLP* [2010] STC 1125 ("*Halycon*"), *Micro Fusion 2004-1 LLP* [2010] STC 1541 ("*Micro Fusion*") and *Icebreaker 1 LLP v HMRC* [2011] STC 1078 support the contention that in each case it was common ground that the relevant partnership was trading where transactions involved the lease/licence of film rights/production for a stream of income of which the partnership had no control. The Appellant also contended that HMRC have failed to recognise that there was a purchase and a sale of the rights.

(e) What was the source of finance of the transaction?

91. As to the source of finance, HMRC submitted that this was provided by GFunding by way of medium term (5 years) not "short-term" borrowing which points away from trading.

92. The Appellant disagreed; 78% was borrowed to fund the purchase of the Rights which, it says, points towards trading. The Appellant contended that HMRC have ignored the Vice-Chancellor's words in *Marson v Morton* that the purchase of an item with a view to its resale in the short-term is a trading transaction.

(f) Was the item which was purchased resold as it stood or was work done on it or relating to it for the purposes of resale?

93. It was accepted by the Appellant that no work was done on the item purchased which points away from trade.

(g) Was the item purchased resold in one lot as it was bought, or was it broken down into saleable lots?

94. As to whether the item which was purchased was resold in one lot as it was bought or broken down, the Appellant accepted that the rights were sold as bought, noting that GFilms appears to have split the collection of rights it acquired from

Upsticks. HMRC asserted that the composite transaction did not involve any breaking down of any asset into lots.

(h) What were the purchasers' intentions as to resale at the time of purchase?

95. Regarding the purchaser's intentions as to resale at the time of purchase, HMRC argued that, properly viewed, the transaction was a composite in which there was no relevant acquisition or sale of an asset which satisfies this test, but rather the payment of a lump sum in return for the potential income stream. HMRC submitted that there is no evidence to demonstrate that the Appellant intended to sell the potential income stream at the time of purchase.

96. The Appellant agreed that the Rights were sold on the same day as purchased and the fact that Mr Degorce was contractually bound to do so, but the Appellant submitted that it cannot be ignored that an asset was purchased and sold with focus only on the resultant revenue stream. As such, the Appellant argued that this badge is a very strong pointer towards a trading deal.

(i) Did the item purchased either provide enjoyment for the purchaser (for example, a picture) or pride of possession or produce income pending resale?

97. As to whether the asset provided income pending resale, HMRC argued that viewed as a composite transaction, the only asset acquired was the potential income stream which produced no income for the Appellant. It is contended that the asset in question suggests a non-trading activity.

98. The Appellant contended that this badge points towards trade; only through the sale of the Rights could income be produced and there is no suggestion that the Rights provided enjoyment or pride of possession to the Appellant pending resale.

Findings of Fact on badges of trade

99. We found as a fact that there was no element of repetition in Appellant's transaction. We had no detailed evidence before us relating to Mr Degorce's activities either pre or post 2006-2007. As regards those pre 2006-2007, there was no evidence to support the assertion on behalf of the Appellant that there existed a "deemed film trade" nor has any binding finding been made by a Court or Tribunal in that regard. Similarly, whilst we accepted that the Appellant had been involved in activities similar to that before us after the relevant period (2006-2007), we noted that those activities were subject of an enquiry by HMRC and again, no determination has been made on the issue of trade. In our view, it would be unsafe to accept the Appellant's assertions in the absence of any detailed examination of the evidence and consequently found that we must deal with the transaction as a one-off transaction.

100. We accepted that Mr Degorce may well have explored opportunities in the film sector, but in our view the contemplation of any such activities is distinguishable from the reality of actually entering into such transactions.

101. We note that although in our view, the transaction must be regarded as a one-off this finding does not prevent it from being regarded as an adventure in the nature of trade.

102. As to the question of whether the transaction related to Mr Degorce's day to day business, for the reasons set out above we did not consider his activities involving the film industry pre and post 2006-2007 in some way related to the trade which Mr Degorce otherwise carries on, namely that of a hedge fund manager.

103. The parties agreed (HMRC in principle) that a potential income stream could be the subject matter of trade and that this factor points towards a trade. In those circumstances we do not feel it necessary to comment further.

104. In our view, the cases relied on by the Appellant to support the argument that there was a purchase and sale of the rights did not assist. The case of *Ensign* involved the subsequent intention for distribution, as opposed to the present case in which, in our view, the distribution was an integral part of a composite transaction. The issue as to whether there was a trade or not was not argued; the Court focussed on the issue of expenditure.

105. In our view the cases of *Halcyon, Icebreaker* and *Micro Fusion* also do not assist as no specific consideration was given to the issue of "trade" and the Tribunal appears to use the words "trade" and "business" without distinction.

106. We accepted the submission of HMRC, relying on *Ransom*, that the Appellant did not intend to sell the potential income stream and therefore, in the absence of a customer, the transaction cannot be viewed as having been carried through in a way typical of trade.

107. There was no dispute that the majority of funding came from a loan from GFunding. The 5 year term of the loan cannot, in our view, be said to be short-term and whilst we accept that resale in the short-term is indicative of trading, the reality was that the Appellant did not sell the rights and pay off the loan, but rather the loan remained to be paid off by the future income stream.

108. Both parties agreed that the item purchased was resold as it stood and resold in one lot, which points away from trade. We therefore do not comment further on these factors.

109. As to whether the purchaser intended to sell at the time of purchase; if the transactions are viewed, as urged by the Appellant, as a sale and subsequent resale of the Rights, it points to trade. However, in our view, to ignore the role of the income stream as part of the composite transaction would not reflect the reality of the situation which, properly viewed following analysis of the documents and from a realistic perspective the transactions were a composite whereby Mr Degorce made

payment of a lump sum in return for the potential income stream and there was no evidence upon which we could be satisfied that there was any intention to sell at the time of purchase.

110. We agreed with the submission on behalf of the Appellant that only through the sale of the Rights could income be produced; the Appellant only held the asset for a very short period, during which he had no power to interfere with it or use it to obtain income and was obliged to immediately assign the rights as part of the overall transaction. That said, the purchase and assignment was executed simultaneously and we could not ignore the potential income stream which formed part of the transaction and which was, in reality, the asset acquired by the Appellant and which provided no income for the Appellant. Looking at the reality of the whole picture, we found that the asset was indicative of non-trading activity.

111. We concluded that the overall indication in applying the badges of trade is that the nature of the composite transactions was not of a trading nature. However, this is not necessarily decisive of the issue and we therefore went on to consider what Mr Degorce actually did.

What was the transaction? What did Mr Degorce actually do?

Time Line

112. The following represents a brief overview of the process by which Mr Degorce acquired the film rights. We should note that this time line was devised by us and is designed to provide an overview to assist the reader; not all of the information contained in this chart would have been known to the Appellant nor is it intended as an exhaustive list of the sequence of events.

Date	Event
February 2007	Mr Petzel visited the Appellant at home and had general discussions regarding the Appellant's interest in the film industry
5 March 2007	Email from Mr Kulick to Ward Consultancy which stated "How has the Friday announcement affected your selling season? We have counsel's opinion on another structure…that still works despite the recent changes. We're aiming to roll it out in the next week or so."
8 March 2007	Email Phoros Group to Mr Kulick dated 8 March 2007 which stated "What is the write down on your scheme insofar how much tax back. Also what fees are you paying on the gross earnings to be sheltered?"
31 March 2007	Email from Mr Kulick to Ward Consultancy which stated "…please confirm whether your numbers below

	are the amounts to shelter or gross amounts to pay…"
1 April 2007	Email from Mr Kulick to Paynter Granby requesting assistance in closing a deal "the matter is of some urgency as we are aiming to close on Wednesday"
2 April 2007	Letter from Ms Challons at HSBC Specialist Tax Group setting out the "Goldcrest Pictures Business Proposal" including the taxation position and the Appellant's capacity to shelter income for the tax year 2006-07
2 April 2007	Acceptance form of GPics signed by the Appellant and witnessed by Ms Challons which included the irrevocable agreement at clause 3.4 that the acceptance once submitted "cannot be cancelled, rescinded or revoked".
2 April 2007	Loan Application from GPics signed by Mr Degorce and confirmed by Ms Challons
2 April 2007	Minutes of telephone meeting between Mr Degorce and Mr Petzel which confirm that Appellant had signed acceptance form and was considering acquiring the rights to Star Trek. Mr Petzel informed the Appellant that he was very familiar with the deal structures of Goldcrest and had been in discussions to assist them with the valuation of distribution rights. The Appellant agreed a fee of $20,000 for Mr Petzel to assist with an economic analysis. Mr Petzel agreed to inform Goldcrest of the conflict and the Appellant would inform Goldcrest of Mr Petzel's engagement.
3 April 2007 (11.46 and 11.51)	Two Emails; one from Ms Zitouni (HSBC) to the Appellant requesting confirmation of the amount to transfer from Appellant's capital account to his new Sole Trader account as £4,854,534. Second email from Ms Zitouni to Mr Dodds at HSBC confirming the amount of the transfer as £4,862,234.
4 April 2007 (09.57)	Email from Mr Kulick at Goldcrest Films to Mr Degorce explaining that *Star Trek* was no longer an appropriate film for the structure.
4 April 2007 (12.09)	Email from Mr Kulick to Mr Degorce setting out information on *Love Guru, Tropic Thunder* and *Angus.* The email states that once the territories are selected by Mr Degorce, Goldcrest aim to execute all

	documentation on that day (4 April 2007).
4 April 2007	Email from Mr Degorce to Mr Kulick stating that he would like to discuss the film options as soon as possible and has asked Mr Petzel to call when he wakes up. Mr Degorce states: "I guess we will do a blend of both movies given size".
4 April 2007 (15.36)	Email from Mr Kulick confirming that Mr Degorce's cash contribution has been received.
4 April 2007 (16.00)	Minutes of telephone call between Mr Degorce and Mr Petzel in which Mr Degorce requested that his engagement agreement with Mr Petzel be amended to replace *Star Trek XI* with *Tropic Thunder* and *Love Guru*. Mr Petzel confirmed that he would provide an economic analysis and that Mr Kulick would be informed of the intention to proceed with *Tropic Thunder* and *Love Guru* (subject to valuation.)
4 April 2007 (17.45)	Minutes of telephone meeting between Mr Degorce and Mr Petzel in which it was stated that the transaction involving *Tropic Thunder* and *Love Guru* would be conditional on Mr Petzel's valuation which would be provided later that day.
4 April 2007 (22.30)	Minutes of telephone meeting between Mr Degorce and Mr Petzel in which draft valuations for *Tropic Thunder* and *Love Guru* were discussed. Mr Degorce felt that the analysis of Mr Petzel supported the transaction and agreed to inform Mr Kulick of the same.
4 April 2007 (23.00)	Minutes of telephone meeting between Mr Degorce, Mr Kulick and Mr Petzel in which Mr Degorce confirms that he is content with the price and territories on *Love Guru* but is looking for a discount *on Tropic Thunder*. Mr Kulick indicates that he is unwilling to reduce the price on *Tropic Thunder*.
4 April 2007 (23.33)	Email from Mr Kulick to Mr Degorce indicating one last amendment: the total purchase price was lowered by £313,500 and Switzerland substituted for Easter Europe on *Love Guru.* Mr Kulick states "it's a good deal, honest."
5 April 2007 (14.09)	Email from Mr Kulick to Mr Degorce confirming that "we closed today".

28 June 2007	Letter from GPics to the Appellant enclosing his accounts in respect of film distribution rights which have been reviewed by Mazars LLP

113. The Business Proposal of GPics explained that "you must rely on your own examination of the legal, taxation, financial and other consequences of undertaking the trade..." and included a disclaimer in respect of the accuracy or completeness of information contained within the proposal, for which GPics assumed no responsibility. Under the heading "Exploitation of Rights" it was stated that:

> "You will sell your distribution rights to Goldcrest Distributor, a wholly owned subsidiary of Goldcrest Film Finance LLP, who will purchase and distribute your rights under the terms of the Distribution Agreement."

114. The Proposal explained that while a profit was expected over time, the business is likely to realise a loss in its First Accounting Period and that GAAP requires that an asset shown as stock or work in progress are included in a balance sheet at the lower cost and net realisable value; the sum of the values is expected to be substantially lower than cost as revenues from the exploitation of distribution rights will not yet be realised and will therefore be uncertain.

115. In addition to advice provided by Goldcrest, Mr Degorce also took advice from Mr Petzel, Howard Kennedy Solicitors and HSBC Private Bank. An assistant was employed by Mr Degorce to assist in managing the trade.

116. Reliance was placed by the Appellant on the discretion used by Mr Degorce in deciding which films or territories to acquire, whereupon he would negotiate the price to be paid for the rights.

Mr Degorce's Evidence

117. Mr Degorce explained in his oral evidence that he understood Ms Challons to be in charge of HSBC's tax department. Ms Challons had contacted him upon being made aware that the *Star Trek* rights were available as she was aware of his interest in the film business. In March 2007 Ms Challons introduced Mr Degorce to Mr Kulick at Goldcrest. Mr Degorce accepted that the agreement he had entered into with Goldcrest contained a disclaimer, for example in relation to the accuracy of financial illustrations, but stated that he was provided with advisory services by one of the Goldcrest companies. He stated in oral evidence (transcript 01/05/12) that one of the reasons for hiring Mr Petzel was to "review all the models, all the assumptions" as he did not want to rely solely on Goldcrest's opinion. In addition, he received advice from HSBC and Howard Kennedy.

118. Mr Degorce understood that the rights he acquired would have to be re-sold. He did not agree that the trade put forward to him was the purchase of the rights, which were sold as part of the package and thereafter he did nothing; he clarified that the business was still continuing as he had instructed audits to be carried out. He accepted

in oral evidence (transcript 01/05/12) that there was no option to avoid entering into an agreement with Goldcrest in relation to film advice, or that he could obtain a loan elsewhere: "No, it was – it's a package, as you say".

119. Mr Degorce did not rely on the comparables provided by Goldcrest, preferring instead to rely on Mr Petzel and therefore the financial illustrations provided by Goldcrest had not formed part of his consideration. He understood that the law allowed him to engage in a risky industry with the safety net provided by tax relief. He agreed that there was a downside protection and only an upside if the film was a large success. As to what he understood from the Goldcrest documents and figures provided at the time, Mr Degorce stated in oral evidence (transcript 01/05/12):

> "...I understood that the law and the structure will allow me to buy movie rights with a safety net which is exactly what I did...I made no money whatsoever from the return of those movies...I made no money from any forms of tax."

120. In cross-examination as to whether or not Mr Degorce understood that the scheme was a tax avoidance scheme within the meaning of the 2006 Regulations and therefore disclosable, the evidence was unclear. Mr Degorce understood that the tax benefit could be viewed as a tax avoidance scheme and consequently he sought advice from HSBC and read legal advice on the issue. He accepted in oral evidence (transcript 02/05/12) that if the tax treatment was not as suggested by Goldcrest, then the transaction would not be worth entering into, nor would he have entered into the scheme without the loan from Goldcrest:

> Mr Gibbon QC: "…You fully understood, therefore, that if the tax treatment was not as Goldcrest suggested, this wouldn't be worth entering into?
>
> Mr Degorce. Yes."

121. Mr Degorce accepted that it was part of the package offered by Goldcrest that his accounts were prepared on the instructions of Goldcrest, which provided figures to be inserted into Mr Degorce's accounts.

122. In respect of the short time frame over which the documents were executed, Mr Degorce stated to the Tribunal (transcript 02/05/12) that as long as he had sufficient time to be comfortable with the transaction, the time frame was irrelevant, although he accepted that potentially Goldcrest were attempting to put together a package for a number of people before the end of the tax year and later in his oral evidence he stated that "there was some rush put on us by Goldcrest...I have a recollection at least for one document that I have to sign the document before my lawyers were 100% comfortable with the loan agreement." He stated that HSBC had ample time to review the scheme and he had relied on their advice. There were no documents to show exactly when Mr Degorce received advice from Howard Kennedy. A note of a telephone meeting with Mr Petzel on 2 April 2007 implied that Howard Kennedy had not, at that point, provided a legal opinion, however Mr Degorce could not recall the sequence of events.

123. We were referred to an email from Mr D. Webster at Phoros Management Limited to a partner, Mr J. Stephenson, at Howard Kennedy Solicitors dated 26 March 2007 the subject of which was "Phoros/Goldcrest" and which stated:

> "Goldcrest have requested you sign their confidentiality agreement."

124. The reply from Mr Stephenson on the same date stated:

> "Rather odd to ask a law firm. The agreement doesn't make a great deal of sense and probably doesn't work the way Goldcrest wanted to. There's also a technical conflict of interest...If they want an agreement that any document is applied to me ahead of HK being instructed by the investors to provide a tax opinion will be kept confidential and only used for the purposes of providing legal advice to persons who are or may become clients of HK, which they inform me are potential investors and presumably have signed up to NDAs with Goldcrest then I can do that...What I am being asked to sign up to is a general NDA [non disclosure agreement] in relation to discussions between the parties in connection with their respective business affairs. Without wishing to be pedantic, there are no such discussion and, based on our conversations, I doubt that we'll ever need to as all I am doing is advising individual investors on the tax aspects…"

125. A further email dated 27 March 2007 from Mr Stephenson to Mr Kulick stated:

> "Either Goldcrest or Tim will be supplying me with documentation relating to the Goldcrest scheme. This is being sent to me as background information on the basis that I will be instructed by potential investors to provide tax opinions…"

126. It was put to Mr Degorce that Howard Kennedy were recommended to him by Goldcrest to provide tax advice on this scheme (inferring that the advice was not wholly independent) to which he clarified that although Howard Kennedy may have been recommended to him, possibly by HSBC, he had paid Howard Kennedy, not Goldcrest and the main advice he received related to the loan documentation which was complex.

127. Mr Degorce stated that there was an understanding, in his signing the agreement with Goldcrest which was, on the face of it "irrevocable", that the deal would be void if his lawyers were not comfortable with the document. There is no documentary evidence to support his contention, however Mr Degorce stated that he trusted Goldcrest to be honest and true to their word, although he accepted that Goldcrest could have forced his position once he had signed the power of attorney document.

128. Mr Degorce was referred to the letter from Ms Challons dated 2 April 2007 which he stated he had not read prior to engaging with Goldcrest as the advice he had received from Ms Challons had been provided orally to him. In particular, Mr Degorce was referred to the statement by Ms Challons that "As requested, I have considered you capacity to shelter income for 2006-2007 tax year, which I have

summarised below...” Mr Degorce stated that this referred to the amount of capital which he could potentially invest as defined by the tax environment of that investment. He did not accept that he had specifically asked for calculations in respect of sheltering income, but rather had sought to understand the tax safety net.

129. A number of documents were put to Mr Degorce which, it was suggested in cross-examination, showed that the scheme was promoted by Goldcrest primarily on a tax basis. Mr Degorce had not seen a number of the documents and confirmed that although there was an undeniable tax benefit in investing in the films, he used it as a way to invest in movies with limited risk.

130. He believed he had acquired the rights for *Star Trek* and instructed payment to be made either on the evening of 3 April 2007 or morning of 4 April 2007. By the time he was informed that *Star Trek* was not available, the payment had been instructed and so he had two options; either to take the money back or wait. He made it clear to Goldcrest that he would not pay any more and, as a businessman, he was able to make a quick commercial decision, leaving the other issues to his advisors. Mr Degorce stated that he discussed the economics of the profit with HSBC and asked Mr Petzel to check the assumptions relating to revenue and profit. On the issue as to the comparables used, Mr Degorce could only make limited comment. He stated that there was a great deal of consideration as to whether Goldcrest had used the correct comparables, but he accepted that there was no evidence in the documents provided to the Tribunal to show that any comparables other than those provided by Goldcrest (for which Goldcrest assumed no responsibility) had been used.

131. Mr Degorce highlighted the fact that he had rejected other films, such as *Angus Thongs and Full Frontal Snogging*, in which to invest, stating in his oral evidence (transcript 02/05/12):

> “…my only focus on those transaction, and you might qualify me as a careless businessman but I think my track record speaks for itself, was about the commerciality of those movies and how much I will have to pay for the movies…I don't need three months…to value a movie…It took me exactly 10 seconds to reject Angus.”

132. In respect of the final purchase prices, Mr Degorce agreed that he had agreed the final price in respect of *Love Guru*, but had sought movement on the price for *Tropic Thunder*. Mr Gibbon QC on behalf of HMRC queried why, subsequently, Mr Kulick had lowered the price of *Love Guru* (having refused to move on the price of *Tropic Thunder*) and suggested that this was done for convenience to meet the difference required for Mr Degorce to reach the same overall price that he was going to pay for *Star Trek* (and thereby the amount Mr Degorce sought to shelter). Mr Degorce disagreed, stating that it was in the interests of Mr Kulick, in order to get the deal completed to balance the two figures. Mr Degorce agreed that the films were looked at globally and it did not matter where a reduction was given.

133. Mr Degorce appeared to agree that he had understood the economics of what would be paid to him in the event the rights produced a distribution both during the

loan repayment and after, which was 15% either way, although he could not recall the exact percentage figures.

Mr Petzel's Evidence

134. Mr Petzel confirmed in evidence that he had been employed by Goldcrest as a sales executive from 1996 to 1997. He had an ongoing connection to the Company but not a particularly close business connection. In February 2007 he was contacted by Mr Johnston of Goldcrest to provide ultimate projections and financial modelling assistance for a number of studio films. He had discussions with Mr Kulick as to the methodology to use from which he built a generic model to use in film valuations. The model was not provided to Goldcrest and there was no formal engagement.

135. Mr Petzel explained that his role was to verify that the information given to Mr Degorce was accurate and whether the performance assumptions would lead to the waterfall portrayed in the Goldcrest documents. Mr Petzel agreed that this could be broken down into three elements; the ultimates, the cash flow assumptions (as to when the money from the ultimates would come in – the timing model) and knowledge as to how the waterfall works.

136. He had spoken to Mr Degorce about opportunities in the film industry in February 2007. Mr Degorce later explained the general terms of the scheme, but his involvement really began when he spoke to Mr Kulick in April 2007, having been engaged by Mr Degorce. In his oral evidence (transcript 03/03/12) he described the transaction as:

> "It is basically -- you know, Patrick actually very, you know, sort of astutely sort of describes it as a kind of -- the acquisition of a call option on future revenues. So, you know, options are derivatives that are there to manage risk of a portfolio. So, in other words, what the studio is -- if you just sort of step aside from the structure and the implementation on an economic level, the studio is giving up a share of its future revenue in return for an amount of cash."

137. Mr Petzel was aware of the urgency for finalising the transaction due to the tax year deadline however he stated that this did not affect his task.

138. Mr Petzel had used in his analysis performed on 4 April 2007 the comparables provided by Goldcrest and the same numbers contained in Goldcrest's financial analysis in respect of domestic box office figures, but had differed in respect of international box office figures.

139. The minutes of meetings between Mr Degorce and Mr Petzel were prepared after the event by Mr Petzel from his contemporaneous handwritten notes following a request being made by Mr Degorce in March/April 2007 that detailed notes were taken. The notes were then checked by Mr Degorce. It was put to Mr Petzel that the later minutes, unlike the earlier ones, contained times of meetings which were suggestive of a deliberate paper trial. Mr Petzel explained that he had gained experience over time and his Company, as a result, had become more organised. Mr

Petzel agreed that a number of the documents were similar, if not identical in parts as a result of using the older documents over which he typed the new minutes. He could not recall why on a number of documents the wording was similar but not identical, and therefore could not be the result of writing over an old document. He stated that he understood that it was important to Mr Degorce that proper records be kept and, depending on what else was going on at the time, the notes were made a day to a week after the discussions took place.

140. Mr Petzel confirmed that he was not aware of the percentages which, from the documentation between Paramount and Goldcrest, showed that the studio obtained 85%. His role was to look at the figures provided to him, work out the waterfall and that was the valuation he carried out. Similarly, the tax position did not feature in his valuation until the final result was reached. He had relied principally on the oral summary of the transaction provided to him by Mr Kulick, but had also requested that documents be sent to him. He was not concerned with the definitions contained in the contractual documents in order to carry out his task, nor how the agreements were put together which did not affect the waterfall that he applied. It was suggested that by failing to take into account the payment directions, Mr Petzel's waterfall ignored an integral part of the transaction and therefore did not reflect the whole picture. Mr Petzel disagreed, stating that the payment directions were not part of the economics of the deal and did not make an impact on his valuation exercise.

141. We were taken through the figures provided by Mr Petzel, in respect of both films, which he acknowledged contained calculation errors, more about which we will say in due course.

142. As regards the comparables provided by Goldcrest, Mr Petzel stated that they appeared commercially sensible on the basis that they were similar in genre, release patterns and actors. It was pointed out to Mr Petzel that two of the comparables for *Love Guru*, a movie featuring the actor Mike Myers, were films which featured Ben Stiller, however even though there are a number of movies featuring Mike Myers, Mr Petzel did not find the comparables odd. Mr Petzel stated that he did look at sequels to Mike Myers films but that his task was not to research the comparables and he did not undertake any detailed analysis of alternatives to those provided in the Goldcrest document. He had not discussed with Mr Degorce whether the comparables were reasonable, stating in his oral evidence:

> "…we didn't really talk about whether those comparables were reasonable, it was basically what Patrick asked of me is to say, if we assume, can you please check that the logic that follows from this level of performance is the right performance because of the summary nature of this piece of paper."

143. Mr Petzel confirmed that of the eight films in which Mr Degorce had acquired rights between 2007 to date, only one film, *Twilight*, has made a return.

Findings of Fact on the Issue of Trade

144. We were referred to an email dated 8 March 2007 from Phoros Group to Mr Kulick of Goldcrest which made the fiscal advantages of the scheme clear:

> "What is the write down on your scheme insofar how much tax back. Also what fees are you paying on the gross earnings to be sheltered?"

Whilst we note that Mr Degorce would not have been privy to the email, we inferred from the email dated 4 April 2007 from Mr Degorce to Mr Kulick that the purpose of Mr Degorce entering into the transaction was to shelter his income and that the email referred to the amount of money which he sought to shelter:

> "I guess we will do a blend of both movies given size"

145. We found that this inference which we had drawn was reinforced by the advice received by Mr Degorce from Ms Challons, in her specific capacity of a tax specialist within HSBC. Mr Degorce stated that he had not read the letter from Ms Challons dated 2 April 2007; we found this unlikely given the value of the transaction. Accepting, however, that this was the case, we had no doubt that the information contained within the letter had been, at the very least, verbally communicated to Mr Degorce. The letter states:

> "…As requested I have considered your capacity to shelter income for the 2006-07 tax year, which I have summarised below…The loss required to shelter your partnership income for 2006-07 is £18,785,905…"

We were satisfied that part of the advice provided by Ms Challons related to the amount of income Mr Degorce could shelter and that this advice was provided as a result of Mr Degorce's query. In our view, this was the only logical conclusion for the letter to read "as requested..."

146. It was submitted on behalf of the Appellant that Mr Degorce had received advice from HSBC about Goldcrest and the deal structure. We saw no evidence to support this assertion; in our view the advice received was limited to the tax issues surrounding the transaction and the fee of £438,469.10 (plus VAT) paid by Mr Degorce to HSBC was more likely to be an introductory fee.

147. Mr Degorce's evidence as to the role played by Howard Kennedy was vague. We inferred from the documentary evidence to which we were referred that Howard Kennedy were not a firm independently chosen by Mr Degorce to provide advice, but rather it was more likely that Goldcrest had suggested the firm to Mr Degorce. In our view, this was another example of the structured nature of the scheme in which Mr Degorce, and others, participated and there was no evidence upon which we could be satisfied that Mr Degorce had taken any independent steps to receive advice on the scheme.

148. The transaction took place over an extraordinarily short period. We did not accept Mr Degorce's evidence that there had been no rush to complete the deal; whilst it was open to Mr Degorce not to participate, once the decision had been taken to join

the scheme, we were satisfied that it was in the interests of Mr Degorce to complete the transaction prior to the end of the financial year, a fact acknowledged by Mr Petzel. It was also clear from the emails between Mr Kulick and the Appellant, both the speed at which the exchanges took place and their content, that it was intended that the transaction had to be executed within a very short space of time.

149. We inferred from the time over which Mr Degorce and Mr Petzel were involved that the asset subject of the transaction was, in reality, unimportant. Mr Degorce had initially paid on the basis that he was to acquire the rights to *Star Trek*. As can be seen from the timeline, Mr Degorce signed the agreement and loan application with GPics on 2 April 2007. It was only after having done so that Mr Degorce engaged Mr Petzel to analyse certain aspects of the scheme. Payment was made on 3 April 2007, after which Mr Degorce was informed (on 4 April 2007) that the rights to *Star Trek* were no longer available. Mr Degorce was then provided with information relating to *Love Guru, Angus* and *Tropic Thunder*. The email from Mr Kulick dated 4 April 2007 states that once territories were selected Goldcrest aimed to complete the scheme on the same date. Although Mr Degorce stated that his signing the acceptance form was not, as stated on the document, irrevocable, there is no indication that Mr Degorce contemplated withdrawing from or delaying his participation in the scheme once informed that the rights to *Star Trek* were unavailable; to the contrary, the documents suggest that this was a transaction with which Mr Degorce would go ahead, irrespective of the films involved.

150. We noted that having agreed a price for *Love Guru*, which had been accepted by Mr Degorce, Mr Kulick subsequently reduced the price. Mr Degorce's oral explanation (transcript 02/05/12) that it was in the interests of Mr Kulick to complete the deal was vague and, in our view, lacked commerciality:

> Mr Degorce: "Let me rephrase it properly, as I told this morning: the amount of capital I invested were determined by the risk I was willing to take on that trade, and obviously the risk I'm taking on that trade is by definition defined by the law because there is a tax safety net defined by the law."

It seemed to us that the only logical inference was that the films, individually, were of little importance but rather the aim was to provide Mr Degorce with an asset or assets by which Mr Degorce could shelter the amount of income as advised by Ms Challons.

151. We were satisfied that at the time of signing the documents, Mr Degorce had a limited understanding of the detail of the scheme and in particular the valuation aspect otherwise there would have been little point in engaging Mr Petzel.

152. The precise role of Mr Petzel was unclear from his evidence. Mr Degorce stated that he engaged Mr Petzel to review all of the models provided by Goldcrest as he did not wish to rely solely on the information provided by Goldcrest however Mr Petzel's evidence did not support this contention as he accepted that he did not analyse or question the comparables provided by Goldcrest. We concluded that the exercise carried out by Mr Petzel in reality provided little assistance to Mr Degorce beyond that already obtained from Goldcrest and HSBC.

153. Mr Petzel also appeared to suggest that his task was to analyse the waterfall from the point of view of Mr Degorce. It was unclear which documents Mr Petzel had been provided with at the time of his engagement, and we were satisfied that he had, in the main, relied on oral information communicated to him by Mr Degorce and Mr Kulick as he stated in evidence. It was certainly clear, and accepted by Mr Petzel in his oral evidence to the Tribunal (transcript 03/05/12) that he was not aware of specific details of the scheme such as step-down after repayment of the loan, which he stated had no impact on his analysis:

> "No, I sort of -- like I said, I was not kind of analysing the transaction sort of at those levels. I was sort of looking at what to value sort of from Patrick's perspective. So kind of following through these kind of definitions to levels where, you know, I simply didn't have the information at the time, in any event."

We could not understand how in those circumstances, without being aware of the details of each part of the scheme, how Mr Petzel could provide Mr Degorce with any meaningful analysis of the overall benefit of the scheme to the Appellant or true value of the film rights.

154. By way of example, it was highlighted by Mrs Farquharson during Mr Petzel's oral evidence (transcript 04/05/12) that there were errors in Mr Petzel's calculations:

> Mr Petzel: Okay. There was -- hold on. Somewhere in there there is sort of a calculation mistake which sort of makes the number, the actual number higher, it was either in Love Guru or Tropic Thunder. Where is the plus sign here? Yeah, so this is -- there is a -- let me see, I can tell you exactly what happened there. The actual international box office would've been higher had I calculated it properly, and actually there's some calculation mistakes in the total column, although the total column has no bearing on the model. It's not used anywhere, so because...
>
> Mrs Farquharson: I can see there is a number duplicated.
>
> Mr Petzel: Yeah, basically it's kind of when the formula refers to the wrong thing."

155. Given the value of the transaction, we found it unlikely that had Mr Degorce intended to rely on Mr Petzel's advice in any meaningful way, he would have been content to proceed on the limited documentation provided to Mr Petzel and an analysis which contained errors which were clear. We concluded that the only real understanding Mr Degorce had of the scheme at the time he entered into it and soon thereafter was in respect of the tax implications.

156. We will say more about the price paid for the Rights by the Appellant in due course, however in our view it is relevant to the issue of trade in that when we looked at what Mr Degorce did, he purchased film rights for £20,299,495, which he then sold on the same day at a loss of £19,417,698 (not taking into account professional

fees/finance charges). In our view, this cannot be viewed as a purchase and subsequent sale of an asset; the transactions were inextricably linked and there was no regard to the true value of the Rights. When we asked ourselves "what was Mr Degorce trading" we concluded that his activities were, in reality, focussed on the close of the financial year and that his activity was limited to obtaining fixed receipts as proscribed by the Agreement signed which cannot be deemed as "trade". We concluded from the evidence that the asset purchased was irrelevant for the purpose of the scheme; the sole requirement was a lump sum figure which was initially paid for *Star Trek*, and thereafter matched for *Love Guru* and *Tropic Thunder,* in return for the potential income stream. We concluded that this was not an adventure in the nature of trade.

Trade "Denatured"

157. HMRC made a second, alternative submission; even if the transaction could be said to have the character of trading, whilst the presence of a motive of securing tax recovery does not cause a trading transaction to cease to be one:

> "some transactions may be so affected or inspired by fiscal consideration that the shape and character of the transaction is no longer that of a trading transaction" (relying on *Lupton (Inspector of Taxes) v FA &AB Ltd*.)

158. HMRC say that the Appellant's activities and the Goldcrest Scheme as a whole were entirely (or almost entirely) affected by fiscal considerations. HMRC rely on the manner in which the scheme was structured and the uncommercial nature of many of its working parts. HMRC also point to the date on which the Scheme operated, namely the last day of the 2006-2007 tax year, the documentation surrounding the Scheme such as a letter dated 2 April 2007 from Ms Challons of the Specialist Tax Group within HSBC Private Bank which set out, it says, the real aims of the transaction from the taxpayer's point of view, the fact that the transaction only made commercial sense if the tax loss was taken into account, the Appellant's admissions in respect of the tax benefit, the price paid for the film rights and documentation from which the Tribunal was invited to infer that those involved in implementing the Scheme felt that it may prompt a change in the law.

159. In response the Appellant relied on *Lupton v FA & AB Ltd* [1972] AC 634, 47 TC 580, ("*Lupton*") per Lord Morris on the question of motive:

> "There may be occasions when it is helpful to consider the object of a transaction when deciding as to its nature. In the Harrison case my view was that there could be no room for doubt as to the real and genuine nature of the transaction. The fact that the reason why it was entered into was that the provisions of the revenue law gave good ground for thinking that welcome fiscal benefit could follow did not in any way change the character of the transaction."

160. The Appellant argued that not only is motive irrelevant, but also that it is the transaction itself (in particular that of the Appellant), its form and content, which must be examined, relying on *Ensign* and *Lupton*:

> "...once it is accepted, as it must be, that motive does not and cannot alter or transform the essential and factual nature of a transaction it must follow that it is the transaction itself and its form and content which are to be examined and considered. If the motive or hope of later obtaining a tax benefit is left out of account, the purchase of shares by a dealer in shares and their later sale must unambiguously be classed as a trading transaction."

161. The Appellant argued that even accepting HMRC's contentions (which they do not) the factors are, as a matter of law, incapable of denaturing the Appellant's trade; The structure of the scheme does not focus on the Appellant's activities, the date may in certain circumstances cast light on a person's motivation for completing a transaction, but motive is irrelevant. Similarly tax advice received and reference to potential changes in legislation may go to the motive for entering into the transaction which is irrelevant.

Findings of Fact on denatured

162. We have already concluded that the Appellant's activities were not an adventure in the nature of trade, but if we are incorrect in our findings, we accepted the submissions made by HMRC that if the Appellant's activities could be deemed to be trade, that trade was denatured. Our findings set out above in respect of what Mr Degorce actually did are relevant to this point and we do not simply repeat the findings made thereon.

163. In reaching our conclusions, we did not unduly focus on the scheme as a whole, but rather the specific activities of Mr Degorce. Viewed realistically, we found that this was a scheme designed and planned to take place over the course of a very short period of time. In our view, Mr Degorce's only activity was to participate in a scheme suggested to him (other than on the advice of his tax advisor) without any real understanding of it. He did not negotiate in the sense that, in our view, would be expected in a normal commercial trading transaction, nor was he responsible for selling. No service was provided by him, nor did he seek out or deal with a customer. We concluded that the sole purpose of the scheme, and therefore the sole purpose of Mr Degorce's participation therein was to shelter his taxable income. In those circumstances we found that the transaction was so affected by fiscal consideration that "it affects not just the shape or structure of the transaction, but its commerciality so that, in Lord Morris' words "the shape and character of the transaction is no longer that of a trading transaction." (per Millett J in *Ensign Tankers).*

Commercial Basis/View to Profit

164. The second issue we were invited to consider was, irrespective of our findings on whether the Appellant was carrying on a trade, whether the trade was carried on on a commercial basis and in such a way that profits in the trade could reasonably be expected to be realised in that period or within a reasonable time thereafter/with a view to the realisation of profits.

165. We therefore address this issue on the basis that, contrary to our conclusions, the Appellant was carrying on a trade.

HMRC's Case

166. HMRC submitted that the term "commercial" should be viewed as per Robert Walker J in *Wannell v Rothwell* [1996] STC 450 as the antithesis of "uncommercial" with the distinction being between "the serious trader who, whatever his shortcomings in skill, experience or capital, is seriously interested in profit and the amateur or dilettante."

167. Mr Gibbon contended that the amount paid for the rights by the Appellant of £20,299,495, when viewed against the amount paid earlier the same day of £3,704,271 and the amount the Appellant sold the same rights for on the same day of £881,797 was clearly an uncommercial basis upon which to carry on a trade. Furthermore, neither film has made the Appellant a profit or an amount by which he could recoup the loss.

168. It is only when the tax relief is taken into account that the transaction makes commercial sense and to apply the test including potential tax relief would defeat the purpose of any analysis as to whether the trade was carried on on a commercial basis.

169. We were invited to only take account of the Appellant's activities relating to the scheme completed on 5 April 2007 as the issue relates to relief for trading losses in that year.

170. HMRC did not accept that Mr Petzel had made a meaningful attempt to provide true valuations of the rights, but rather he had used the US box office figures provided by Goldcrest and produced broadly comparable prices to those of Goldcrest by applying sensitivities of 10%. It was contended by HMRC that there was no arms length negotiation of the prices ultimately paid by Mr Degorce as would be expected in an independent commercial transaction; the total of the amounts paid for *Love Guru* and *Tropic Thunder* were the same as that paid for *Star Trek*. The reduction given by Goldcrest to the amount already agreed by Mr Degorce for *Love Guru* was designed to facilitate the correct amount of money being invested into the scheme by Mr Degorce.

171. HMRC also relied on the oral evidence of Mr Degorce (transcript 02/05/12) as a further indication that he did not fully understand the detail of the transaction in which he was participating, nor did he care about the detail of the documents which defined what he was actually buying, which HMRC submitted was not the attitude of a person carrying on trade on a commercial basis and who is seriously interested in profit:

Mr Gibbon QC: "I am talking about the crunch in this deal here. There's the whole range of documents where you're having to place reliance on your lawyers, and we don't know how long precisely your lawyers had those documents.

Mr Degorce: You --

Mr Gibbon QC: From early April, was it?

Mr Degorce: I don't know. It's -- my only focus on those transaction, and you might qualify me as a careless businessman but I think my track record speaks for itself, was about the commerciality of those movies and how much I will have to pay for the movies. The rest, I can't care less. That's what I pay an advisor, to do that. So to make a judgment on that, I don't need three months, nor Christopher need three months to value a movie. He's been 15 years in business. It took me exactly 10 seconds to reject Angus...At the time when we're discussing those things, I knew for a fact that not only Christopher will review and discuss with Mr Kulick how the economics work, but that job has been done previously, not, you know, by you know HSBC beforehand, and once again you know those waterfall could be complex, you know those documents are not easy to read and I was not -- I mean I've no capacity to understand, so I much more likely to rely on experts to tell me how things work than do it by myself."

172. As to whether the trade was carried on with a view to profit, HMRC invited us to note that the requirements of sub-s 381 (4) and 384 (1) ICTA 1988 are to be tested by reference to the trade carried on in that year and not by reference to individual transactions.

173. The Appellant cannot rely on any subsequent income received from his purchase of the rights in the film *Twilight* to demonstrate that his trade in the year ended 5 April 2007 was carried on with a view to profit; the activities making up the trade must be considered as a whole.

174. On the basis of the Appellant's own documentary evidence which set out his pre and post tax position for the years 2006-2007 and 2007-2008, the Appellant's activities were demonstrably not profitable on a pre-tax basis and therefore cannot be said to have been carried on with a view to profit.

175. Even looking at the longer term position, there was no reasonable expectation of profit. On the basis of the valuation produced by Mazars, instructed by Goldcrest and adopted by the Appellant into his accounts, each film had only a 1 in 20 chance of being successful. The remoteness of the possibility of receiving income through the Potential Income Stream was confirmed by the Appellant who accepted in evidence that neither film *(Love Guru or Tropic Thunder)* has provided an economic return for the Appellant.

176. The Appellant's activities were carried on with a view to obtaining a loss for tax relief purposes and there was never any view to the realisation of profits or so as to afford a reasonable expectation of profit.

Appellant's Case

177. The requirement that the trade be carried on on a commercial basis looks to the manner in which the trade is conducted. The Appellant also relied on *Wannell v Rothwell* and the distinction between an amateur fashion and commercial manner.

178. The Appellant carried on his trade in a highly organised and expert manner; he received advice from HSBC, engaged Mr Petzel and instructed Howard Kennedy in addition to applying his own "financial sophistication" to the transactions.

179. The tax considerations can properly be regarded as part of the commerciality of the trade and it is the manner in which the trader conducts his trade which is the relevant test, not the workings of a scheme carried on by others.

180. The price paid was, and was intended by Mr Degorce, to be a reasonable and commercial price; furthermore Mr Degorce has made "massive profits" on *Twilight*.

181. It was not put to Mr Degorce that he was certain to make a loss or indifferent to profit and the Tribunal, as a matter of law, cannot reach such a finding.

182. As to the issue of whether the trade was carried on with a view to profit, the Appellant submitted that this was a question of fact.

183. It is not accepted that each film had only a 1 in 20 chance of being successful; HMRC's expert took the view that this was in fact 1 in 5. Furthermore, the "success" of a film is not synonymous with a trade being carried on with a view to profit; there can be a view to profit equally on a small chance of large profit or vice versa.

184. The Appellant relies on a quote from Mr Heathcote-Amory, former Chancellor of the Exchequer, in a Parliamentary debate on the Finance Bill 1960 in which he said:

> "We are after the extreme cases in which expenditure very greatly exceeds income or any possible income which can ever be made in which, however long the period, no degree of profitability can ever be reached."

185. It was submitted (relying on the Goldcrest Distribution Rights Proposal) that the transactions were presented to Mr Degorce on the basis that he would trade profitably over time, as has happened with the profits generated by *Twilight* and is likely to happen with *Eagle Eye*, from which Mr Degorce expects to receive at least £10,000,000. As such, the Tribunal was invited to accept Mr Degorce's view as to the likely profitability of the two films relevant to this appeal.

Findings of fact on the issue of whether the trade was carried on on a commercial basis and in such a way that profits could reasonably be expected to be realised in

that period/within a reasonable time thereafter/with a view to the realisation of profits

186. We respectfully agreed with the comments in the case of *Samarkand Film Partnership No 3 v HMRC* [2012] UKFTT 610 (TC) ("*Samarkand*"), which we adopted as our preliminary approach to this issue:

> "The activity of a partner in investing in a partnership may well be part of a commercial enterprise, but if it is that does not mean that the partnership business is necessarily carried on on a commercial basis. It may well be that a partner's borrowing, investment in the partnership and use of tax reliefs is as a whole commercial, but that is irrelevant to the assessment of the commerciality of the partnership's business...
>
> Thus the question for us is whether the activities of the partnership were carried on on a commercial basis...
>
> It seems to us that this decision does not compel the conclusion that profitability is irrelevant to whether a venture is commercial...It seems to us that the serious interest in a profit is at the root of commerciality. Christmas is commercialised when it is used for profit. The hobby art gallery is not run with a serious eye to making money; nor is the loss making market garden. But a serious interest in profit does not to our mind mean simply an interest in an excess of receipts over expenditure especially where longer term cashflows are involved. In those cases the well known and well understood technique of discounting future cashflows to derive their present value would be used to evaluate the project or investment.
>
> It seems to us that if an entity enters into a transaction which has a negative net present value the transaction cannot be descried as commercial unless there are other collateral benefits expected or hoped for which are expected to outweigh the negative effect of the transaction. If you buy an asset for £10 and exchange it for something worth £7 that is not a commercial transaction unless you have a collateral hope for at least £3 profit elsewhere."

187. It seemed to us relevant to look at the payments made by the Appellant and compare the entitlements he received in order to assess the commercial aspect of the transaction.

188. The Film Advisory Agreement, pursuant to which GPictures provided the Appellant with advisory services, required a fee of £1,623,959.60 plus a performance fee equal to 2% of Mr Degorce's receipts from the exploitation of the distribution rights.

189. The Loan Agreement with GFunding, by which GFunding agreed to provide the sum of £17,100,295, was exclusively for the purpose of Mr Degorce acquiring certain distribution rights. Interest was to accrue on the loan at a rate of 8% p/a.

190. We noted that Clause 3.4 of the Loan Agreement entitled Mr Degorce to prepay the loan, however we accepted HMRC's submissions on this point. We concluded that the possibility of the loan being prepaid was so remote as to render the Clause ineffective in practice on the basis that the need to pay back the loan only arose when distributions received and, as Mr Degorce himself acknowledged, the loan was part of the *"package"*. In those circumstances, viewing the transaction as a composite we concluded that the loan was effectively non-recourse.

191. The Sub-Acquisition Deed with GFilm assigned Mr Degorce the rights, title and interest in the two films for a term of 60 years commencing on 5 April 2007 for a total price of £20,299,495. On the Appellant's figures, those same rights were sold on the same day for £881,797. 15.76% of the £20,299,495 was funded by the Mr Degorce's cash contribution and the remainder by the loan. Of Mr Degorce's contribution in the sum of £4,823,160, 66.33% was spent on the acquisition of the film rights and the remainder was paid by way of fees to Goldcrest.

192. The Distribution Agreement assigned to GDistribution the distribution rights in the films. The consideration for the assignment was:

- 100% of all Distribution Receipts until those receipts equalled 32.3% of the purchase price (i.e. £20,299,495); and

- Thereafter 100% of the remaining Distribution Receipts to be on the basis of Net Proceeds (as defined in the Distribution Agreement as "all sums actually and indefeasibly received by [GDistribution] from the exploitation of the Distribution Rights pursuant to the Sub-Distribution Agreements).

193. Payment Directions with GDistribution, GFunding and GPictures agreed that of the monies to which Appellant was entitled under the Distribution Agreement would be paid:

- 55% to GFunding until the loan was repaid;

- 2% to GPictures for the performance fee under the Film Advisory Agreement; and

- 43% to Mr Degorce.

194. GDistribution entered into Sub-Distribution Agreements by which it agreed to assign film rights to Paramount Pictures Corporation "in consideration for an entitlement to Defined Proceeds in Respect of the Rights" , "Defined Proceeds" were applied as follows:

- Until Defined Proceeds equalled 97% of the Purchase Price, Paramount Pictures Corporation was to retain 66.67% of 100% of the Defined Proceeds;

- Until Defined Proceeds equalled 97% of the Purchase Price, Paramount Pictures Corporation was to pay amounts equal to 33.33% of the Defined Proceeds to or at the direction of GDistribution;

- Once Defined Proceeds equalled 97% of the Purchase Price, 100% of the remaining Defined Proceeds are retained by Paramount Pictures Corporation;

- Paramount Pictures Corporation was thereafter to pay to or at the direction of GDistribution, an amount equal to 33.33% of Net Proceeds, until repayment of the 5555 Loan in full; and

- Upon repayment of that loan in full, Paramount Pictures Corporation was to pay to or at the direction of GDistribution, an amount equal to 15% of the Net Proceeds until the end of the 60 year term.

195. In effect, this meant that when the 5555 loan was repaid, Mr Degorce continued to be entitled to a maximum 15% share of the proceeds of the film rights.

196. In our view, taking into account the figure at which the Appellant purchased and then re-sold the rights in the same day, combined with the limitations contained within the documents as to the monies to which the Appellant was thereafter entitled, there was little likelihood that the Appellant would obtain significant receipts, such as would either recoup the loss made on the sale price of the rights or would provide the Appellant with any real expectation of making a return.

197. We did not find the Appellant's reliance on his receipts from *Twilight* assisted him; an appendix annexed to HMRC's written closing submissions showed that even where the film was a worldwide success, the returns made by Mr Degorce were only profitable on a post-tax basis. In our view, whilst the tax benefits were no doubt a sensible consideration from Mr Degorce's perspective in deciding whether to enter into the scheme, such allowances cannot be decisive of the issue of whether the trade was carried on on a commercial basis.

198. We did not accept that the price paid for the rights was intended by Mr Degorce to be a reasonable and commercial price; having looked at his activities in purchasing and assigning the rights, we could find no basis upon which Mr Degorce could be satisfied that the price paid was commercial; there was no detailed independent valuation prior to Mr Degorce signing the agreements and making payment nor was such a matter within his own knowledge. When viewed against the loss at which the rights were sold, for which again there was no independent assessment, we concluded that the entire focus of the transaction was on the potential tax relief and that this was not a trade that was carried on on a commercial basis.

199. HMRC did not put (although we note to do so would be speculative as there was no direct evidence on the point) that Mr Degorce was certain to make a loss or indifferent to profit, but we did not accept that this prevented us from reaching a conclusion on the issue of profit on the basis of the evidence before us. Mr Degorce accepted in his oral evidence (transcript 02/05/12) that he only cared about the

"commerciality of those movies and how much I will have to pay" yet there was no evidence of any in depth analysis as to how he assessed "commerciality" or how this was balanced against the amount he paid. Added to the limitations in what Mr Degorce could expect and the lack of any evidence that Mr Degorce ever queried or took the time to fully understand the potential receipts or the timeframe within which he could expect to make a profit, we concluded that this was not the attitude or actions of a person carrying on a trade on a commercial basis with a serious view to profit.

200. We could not ignore the view of Mazars, which was used in the Appellant's accounts. Even if the view that each film had a 1 in 20 chance of being successful was not correct, this was the most current information which Mr Degorce had at the end of the tax year and, at the very least, it gave rise to a concern that the likelihood of potential receipts was remote. That this was never queried by Mr Degorce was, in our view, indicative of Mr Degorce's failure to exercise the prudence and diligence we would expect of a professional man entering into a commercial transaction.

201. As to the submission that the "success" of a film is not synonymous with a trade being carried on with a view to profit, in our view there must be some evidence of a serious interest in profit of some description (whether large or small) and which, in order to be achieved by Mr Degorce, would require recouping any loss. The films did not necessarily need to be worldwide successes in order to achieve this, but given the restricted potential receipts, combined with the amount paid and received for the rights, taken together with the evidence that to date, Mr Degorce has made no economic return on the two films we concluded that the trade was not carried on on a commercial basis and in such a way that profits in the trade could reasonably be expected to be realised in that period or within a reasonable time thereafter and there was, in reality, no basis upon which Mr Degorce could have had a reasonable expectation of financial benefits/profit (beyond the fiscal benefits).

The Profit/Loss position on the Trade

202. The parties agreed that the issues to be determined under this heading are as follows:

(i) Whether the profits for the year of assessment 2006-2007 were calculated in accordance with generally accepted accounting practice ("GAAP");

(ii) If the profits of the trade were not calculated in accordance with GAAP, what would those profits have been had they been calculated in accordance with GAAP.

203. HMRC submitted that the profits of the trade for the year of assessment 2006-2007 were not calculated in accordance with GAAP. The accounts of the Appellant were prepared by Mazars and were certified as having "been properly prepared in accordance with technical guidance issued by the Institute of Chartered Accountants in England and Wales". They stated that they were "prepared under the historical cost convention and in accordance with UK Accounting Standards". The accounts showed:

- Expenditure on professional fees of £1,609,426;
- A provision of £19,417,698 against the cost of film rights acquired;
- A net loss of £21,028,124; and
- A loan falling due after more than one year of £17,100,294.

204. There are three accounting debates between the parties:

(a) At what value should the deferred Consideration be shown in the Appellant's accounts at 5 April 2007? (the "Valuation point");

(b) Ought one to adopt a linked presentation in accounting for the Loan and the Consideration (or should one write down the face value of the Loan for other reasons)? (the "Linked Presentation point"); and

(c) Are the Rights properly accounted for as trading stock? ("the Trading Stock point").

GAAP and FRS 5

Financial Reporting Standard 5

"Objective
The objective of this FRS is to ensure that the substance of an entity's transactions is reported in its financial statements. The commercial effect of the entity's transactions, and any resulting assets, liabilities, gains or losses, should be faithfully represented in its financial statements."

The Witnesses

205. HMRC's first witness was Mr Michael Thornton, a partner and head of Valuation Services at Grant Thornton UK, LLP. Mr Thornton is a Chartered Accountant with over 20 years' experience in valuation and significant experience of working with companies in the media sector.

206. We found Mr Thornton to be truthful and reliable witness. In particular, we did not devalue Mr Thornton's expert evidence on the basis that he had not applied to become a fellow of the Institute of Chartered Accountants as we were invited to do by the Appellant.

207. The second witness on behalf of HMRC was Mr Richard Cannon, a Chartered Accountant with 16 years' experience, currently (since 2007) employed by HMRC.

208. The Appellant contended that Mr Cannon is a relatively junior employee of HMRC, having not attained the status of Responsible Individual in auditing terms which goes to the weight attached to his evidence. We do not agree; we accepted Mr Cannon as a truthful and reliable witness and did not find that his employed status

with HMRC or lack of title as Responsible Individual was a matter which undermined his credibility as a witness or affected the weight to be attached to his evidence. We found that Mr Canon's evidence was unbiased and professional and there was no basis upon which we could conclude that his independence had been compromised by his employment by HMRC, consequently we rejected the Appellant's submission and we did not attach any less weight to his evidence for the reasons urged by Mr Peacock QC.

209. We considered the Appellant's submission that Mr Cannon's evidence was not fair and frank and that:

> "…when his analysis of linked transactions was exposed as fundamentally flawed, he advanced an alternative route to the same end result. His analysis of both the trading stock and the linked presentation points were…simply untenable and were characterised by an inability to articulate the conceptual basis for his view and/or a refusal to contemplate the possibility that he might simply be wrong."

We did not accept this submission; to the contrary, our interpretation of Mr Cannon's evidence was that he had adopted a very fair approach by considering dual (as opposed to alternative) possibilities.

210. The Appellant called one expert witness to give evidence; Mr John Graydon. Mr Graydon is a Chartered Accountant with 18 years post qualification experience. He is employed by RSM Tenon Limited, an accountancy and advisory firm, where he is head of the Film Team. We found Mr Graydon to be a truthful and reliable witness.

Issues agreed between the parties

211. We were provided with a joint statement prepared by Mr Graydon and Mr Cannon which set out a list of issues upon which agreement had been reached and those upon which the experts remained in dispute. It may be helpful at this point to set out the contents of that document.

212. The issues agreed by Mr Graydon and Mr Cannon were:

> (a) Mr Degorce's accounts for the period ended 5 April 2007 should follow UK GAAP;
>
> (b) The transaction entered into by Mr Degorce as described by the Sub-Acquisition Deed dated 5 April 2007 represents the acquisition of an asset of circa £20 million (although there was no agreement as to the exact nature of this asset);
>
> (c) The resultant asset in the accounts of Mr Degorce at 5 April 2007 was a financial asset.

213. The issues where no agreement was reached between Mr Graydon and Mr Cannon were as follows:

(a) Whether the acquisition represented the purchase of stock in trade or an intangible fixed asset;

(b) The treatment of the transaction described in the Distribution Agreement;

(c) Whether the financial asset should be classified as a Fixed Asset or Current Asset;

(d) Whether the transactions entered into by Mr Degorce should be viewed as a whole;

(e) Whether the loan and asset should be treated using the provisions of FRS 5 for linked presentations.

214. Using the Appellant's terminology, the issue can be divided into the following points:

- The "Valuation" point;
- The "Linked Presentation" point; and
- The "Trading Stock" point.

(a) The Valuation Point

215. The rights in the films held by the Appellant at the end of April 2007 were valued by Mazars LLP as part of their preparation of financial statements for the Appellant for the period 2 April to 5 April 2007. The financial statements were prepared to give a true and fair view. There was some debate as to what the asset to be valued or included in the accounts was: Mazars reported to the board of GPictures that they valued the rights in the films held by the Appellant at the end of 5 April 2007. Mr Graydon, for the Appellant, tested this valuation by valuing the deferred consideration. Mr Thornton, for HMRC, valued the rights acquired by the Appellant. We refer to the asset to be valued hereinafter as "the rights". We took the view that the asset to be valued and included in the accounts was the rights to further income streams.

216. The rights were valued by HMRC's expert, Mr Thornton, as at April 2007 on a market value basis. A third valuation was prepared for the rights in Love Guru by Mr Graydon, the Appellant's expert witness, on 14 October 2011. This valuation was subsequently amended due to a calculation error on 2 May 2012.

217. The valuations were as follows: (percentage of purchase price shown in brackets)

	The Love Guru	**Tropic Thunder**	**Total**
Mazars	501,310 (4.35%)	380,487 (4.33%)	881,797 (4.34%)

Mr Thornton	1,656,449 (14.38%)	1,300,389 (14.81%)	2,956,798 (14.57%)
Mr Graydon (as amended)	837,803 (7.27%)	-	-
Purchase Price	11,520,375	8,779,120	20,299,495

218. All valuations were performed on a Net Present Value basis. There was no adjustment for the NPV methodology but differences arose in the assumptions used in the calculations, such as the discount rate. We note that there is no Accounting Standard on the valuation of rights and that the valuation is subjective.

219. We consider that all of these valuations were diligently performed by qualified Chartered Accountants with the necessary expertise to do so.

220. Mr Graydon's valuation of the rights in Love Guru is 2.85% of the purchase price higher than Mazar's valuation in respect of that film. Mr Graydon stated in his oral evidence that, in his opinion, Mazar's valuation is not unreasonable.

221. HMRC's case is that Mr Thornton's valuation is to be preferred, not least because Mr Graydon stated in his oral evidence "I'm not a market valuer". Mr Graydon suggested that Mr Thornton had valued the rights acquired by the Appellant whereas he (Mr Graydon) had valued the rights to deferred consideration. His evidence was that his was the correct approach for inclusion in the accounts under UK GAAP. This was the main reason that the difference in valuations arose.

222. Mr Thornton agreed that the rights acquired were a highly risky investment and that estimating the revenues that they would generate is a highly subjective exercise. Nevertheless, he felt that Mazars had been too cautious in their valuation.

Findings on the Valuation Point

223. While we have no issue with Mr Thornton's methodology or calculation, we preferred the arguments of Mr Graydon; however we do not agree that the difference of 2.85% in the case of Love Guru between his and Mazar's valuation is not material. We consider that Mr Graydon's valuation of the deferred consideration is to be preferred. In this respect the valuation to purchase price percentage of 7.27% calculated in respect of *Love Guru* should be applied to *Tropic Thunder*.

(b) Linked Presentation

224. FRS 5 ("Reporting the substance of transactions) reports that, subject to certain conditions, where a transaction involving an item previously recognised as an asset is in substance a financing, but the financing "ring fences" the item, the finance should be deducted from the gross amount of the item it finances on the face of the Balance Sheet within a single asset caption ("a linked presentation") i.e. the finance should be

shown deducted from the gross amount of the item it finances on the face of the Balance Sheet.

225. The objective of FRS 5 is to ensure that the substance of an entity's transactions is reported in its financial statements. The commercial effect of an entity's transactions and any resulting assets, liabilities, gains or losses, should be faithfully represented in its financial statements.

226. FRS 5 is prescriptive as to when linked presentation is appropriate. The criteria are set out in paragraphs 26 and 27:

> "Where a transaction involving an item previously recognised as an asset is in substance a financing – and therefore meets the condition of paragraph 21 regarding no significant change in the entity's access to benefits or exposure to risks – but the financing "ring-fences" the item such that –
> The finance will be repaid only from proceeds generated by the specific item it finances (or by transfer of the item itself) and there is no possibility whatsoever of a claim on the entity being established other than against funds generated by that item (or the item itself),there is no provision whatsoever whereby the entity may either keep the item on repayment of the finance or re-acquire it at any time, and all of the conditions given in paragraph 27 are met, the finance should be shown deducted from the gross amount of the item it finances on the face of the balance sheet with a single asset caption (a "linked presentation"). The gross amounts of the item and the finance should be shown on the face of the balance sheet and not merely disclosed in the notes to the financial statements. A linked presentation should also be used where an item that is financed in such a way that all of the above three conditions are met has not been recognised previously as an asset.
>
> A linked presentation should be used only where all of the following are met:
> (a) the finance relates to a specific item (or portfolio of similar items) and, in the case of a loan, is secured on that item but not on any other asset of the entity;
> (b)the provider of the finance has no recourse whatsoever, either explicit or implicit, to the other assets of the entity for losses and the entity has no obligation whatsoever to repay the provider of finance;
> (c) the directors of the entity state explicitly in each set of financial statements where a linked presentation is used that the entity is not obliged to support any losses, nor does it intend to do so;
> (d) the provider of the finance has agreed in writing (in the finance documentation or otherwise) that it will seek repayment of the finance, as to both principal and interest, only to the extent that sufficient funds are generated by the specific item it has financed and that it will not seek recourse in any other form, and such agreement is noted in each set of financial statements where a linked presentation is used;
> (e) if the funds generated by the item are insufficient to pay off the provider of the finance, this does not constitute an event of default for the entity; and;
> (f)there is no provision whatsoever, either in the financing arrangement or otherwise, whereby the entity has a right or an obligation either to keep the item

upon repayment of the finance or (where title to the item has been transferred) to re-acquire it at any time."

227. Further guidance is given in paragraphs 76 to 78 and paragraph 5 of the summary.

228. There was no disagreement between the parties that FRS 5, on the face of it, applied to the Appellant's financial accounts. We agree that FRS 5 is applicable in this case.

229. We heard evidence on linked presentation from Mr Graydon for the Appellant and Mr Cannon for HMRC.

230. Mr Graydon's opinion was that if any of the criteria set out in paragraphs 26 and 27 of FRS 5 are not met, then linked presentation cannot be used.

231. In his oral evidence, Mr Graydon stated that FRS 5 would apply (in respect of linked presentation) but for the existence of Clause 7.2 of the loan agreement (see below). In particular, Mr Graydon refers to Clauses 3.1, 3.4, 3.5 and 7.2 of the Loan Agreement which state:

Clause 3.1:

"Lender's entitlement to repayment in full of the Loan together with all interest and other sums due hereunder (together the "debt")…is with recourse only to distribution revenues and other sums…received by you in respect of the Assigned Rights under the Distribution Agreement together with the Collateral…This recourse only to the Distribution Revenues and Collateral does not apply to amounts under Clause 7.2."

Clause 3.4:

"Notwithstanding your requirement to prepay in clause 3.3, you may prepay the Debt at any time in whole or in part without penalty."

Clause 3.5:

"If any of the following acceleration events (Acceleration Event") occur…"

Clause 7.2:

"You shall on demand indemnify and keep indemnified the Lender from and against all costs, expenses, claims, losses, damages, liabilities or proceedings suffered by the Lender whatsoever arising directly or indirectly as a result of: …The occurrence of any Acceleration Event…"

232. According to Clause 7.2, under certain circumstances specified in Clause 3.5 the Lender does have recourse to Mr Degorce personally and is therefore not limited solely to receipts from the deferred consideration asset. Such circumstances include default on the normal repayment terms, breach of any of the undertakings of Mr Degorce under the loan agreement and where Mr Degorce or other entities party to the transactions in rights are deemed insolvent for the purposes of s 123 (1) of the Insolvency Act 1986.

233. Clause 3.4 of the Loan Agreement states that the Appellant has the right to prepay the loan at any time in whole or in part without penalty, but in any such event he does have the right to keep the item on repayment of the finance.

234. Paragraph 81 of FRS 5 provides further guidance on the conditions necessary in order to use linked presentation. In this paragraph it states: "the entity must have no right or obligation to repay the finance from its general resources." The loan agreement states in Clause 3.4 that Mr Degorce has the right to repay the loan at any time in whole or in part without penalty.

235. Mr Graydon submitted that because of the above, linked presentation is not appropriate. Mr Graydon also argued that the general principles of FRS 5 should also be taken into account. The Financial Reporting Standard was specifically created in order to stop the practices of some entities engaging in complex arrangements designed to allow them to remove liabilities from the balance sheet. He argued that we should be wary of linking transactions or balances together in such a way as to remove assets and liabilities from the balance sheet.

236. Mr Cannon for HMRC argued that the asset and limited recourse loan should be presented in the balance sheet in a linked presentation. He accepted that the Loan Agreement (at Clause 3.4) entitles Mr Degorce to prepay the loan. However, in his opinion the possibility of Mr Degorce prepaying the loan from his general resources is so remote that the clause will not have a commercial effect in practice and should not determine the correct accounting treatment. He relied on the fact that the loan is effectively non-recourse in that repayment is only made out of proceeds of the distribution and the fact that Mr Degorce entered into the Payment Directions.

Findings on Linked Presentation

237. We note that FRS 5 paragraph 14 states that:

> "A reporting entity's financial statements should report the substance of the transactions into which it had entered. In determining the substance of a transaction, all its aspects and implications should be identified and greater weight given to those more likely to have a commercial effect in practice. A group or series of transactions that achieves or is designed to achieve an overall commercial effect should be viewed as a whole."

238. Further, FRS 5 states:

"The objective of FRS 5 "is to ensure that the substance of an entity's transactions is reported in its financial statements. The commercial effect of the entity's transactions and any resulting assets, liabilities, gains or losses, should be faithfully represented in its financial statements."

Where the substance of a transaction falls within the scope of FRS 5 and also directly within the scope of another accounting standard or statutory requirement, "the standard or statute that contains the more specific provision(s) should be applied…Nevertheless, the specific provisions of any standard or statute should be applied to the substance of the transaction and not merely to its legal form and, for this purpose, the general principles set out in FRS 5 will be relevant.""

239. We preferred the arguments of Mr Cannon. In our opinion the financial accounts of the Appellant at 5 April 2007 do not show a true and fair view of his state of affairs and have not been produced in accordance with UK GAAP. The asset and loan should have been presented as a linked presentation in the Balance Sheet. We also preferred his evidence for the reason that he had tested his opinion with an alternative approach which resulted in the same accounting treatment.

240. We should note that the fact that GFunding did not recognise the loan as an asset in its Balance Sheet did not impact on our conclusion on this issue.

(c) The Trading Stock Point

241. There was no disagreement that the purchase of rights represents an asset. The nature of the asset acquired is the subject of dispute between the parties.

242. Mr Canon for HMRC argued that the asset acquired by the Appellant on 5 April 2007 was an intangible fixed asset and the accounting treatment should be consistent with that.

243. Mr Graydon for the Appellant argued that as the film rights were purchased with the intention of resale, they cannot meet the criteria for a fixed asset. Mr Graydon's view is that the purchase of rights should be treated as a purchase of stock in trade and shown as purchases of stock in trade within cost of sales in the profit and loss account and as a stock asset on the Balance Sheet. Similarly the sale (or assignment) of rights should be shown as a sale of stock in trade and treated accordingly in the profit and loss account, to the value of the consideration recoverable.

244. We noted that Mr Graydon did not agree with how the value of the consideration was shown in the financial statements of the Appellant but that this did not change the overall profit and loss shown in the accounts.

245. Mr Graydon argued that because the rights were purchased with the intention of resale and sold prior to the year end they do not meet the criteria for a fixed asset.

246. Mr Cannon's opinion is that as the rights were purchased and sold on the same day this does not represent "a view to resale"; the sale was pre-ordained as part of a series of transactions which took place on 5 April 2007.

Findings on the Trading Stock Point

247. Paragraph 14 of FRS 5 states that "a group or series of transactions that achieves or is designed to achieve an overall commercial effect should be viewed as a whole". We preferred the argument on behalf of HMRC on the trading stock point. We concluded that the Appellant acquired the rights to a future income stream as part of a series of transactions designed to achieve this commercial outcome. As such, he acquired an intangible fixed asset with a life of 60 years, which does not have the substance of a trading stock item. For the reasons outlined above and under the section dealing with badges of trade, we did not consider that the original purchase and assignment of the rights should be viewed separately but as a part of a series of transactions designed to achieve an overall commercial effect.

If the profits of the trade were not calculated in accordance with GAAP, what would those profits have been had they been calculated in accordance with GAAP?

248. The parties invited the Tribunal to consider what the profits would have been if they had been had they been calculated in accordance with GAAP. As we have already stated we found all of the expert witnesses to be reliable, however we have, in respect of the valuation issue, preferred the evidence of Mr Graydon on the basis that, in our view, his role as head of the Film Team within an accountancy and advisory firm attaches weight to his evidence within this specialised area.

249. We do not propose to set out our own calculation within this decision as the parties have not had the opportunity to comment on any such calculation, however we concluded that the linked presentation method as proposed by Mr Cannon should be adopted in calculating the profits and the valuation method of Mr Graydon (which was only presented in evidence in respect of Love Guru) would be applicable in order to calculate the profits relating to each film in accordance with GAAP.

Whether expenditure was incurred wholly and exclusively for the business

The Parties' Submissions

250. Section 34 ITTOIA 2005 provides that for any deduction to be obtained in the computation of trade profits, the expenditure must be incurred wholly and exclusively for the purposes of the trade.

251. It was submitted by HMRC that the loan is limited recourse and that, relying on Lord Walker in *TowerMCashback LLP and another v HMRC* [2011] STC 1143 ("*Tower MCashback*") although there was a loan, there was not in any meaningful sense, an incurring of expenditure or other associated costs, but rather it went into a loop in order that the Appellant could participate in a tax avoidance scheme. HMRC contended that the Appellant had failed to address this key conclusion (which is, in

the view of HMRC, unanswerable) but instead cited uncontroversial propositions taken from the judgment.

252. The Appellant highlighted the following key propositions from *Tower MCashback*:

> (a) The question is whether there was real expenditure on the acquisition of the rights;
>
> (b) It is not enough for HMRC to point to the money going round in a circle; and
>
> (c) It is material that the acquisition of the rights was on fully commercial terms.

253. In written submissions the Appellant contended that HMRC had altered its argument, HMRC having initially submitted that:

> "Given the tax avoidance motivation of the scheme, it cannot be said that the charge in the taxpayers' accounts for the cost of the film rights was wholly and exclusively laid out or expended for the purposes of trade (sic.), and so the charge falls to be disallowed under section 74 (1) (a) of ICTA."

Subsequently HMRC sought to rely on the "facts surrounding the acquisition of the rights" rather than the "tax avoidance motivation."

254. Section 74 ICTA did not apply for income tax purposes in the year in question. The purpose to be determined is that of incurring the expenditure, not the consideration of whether to contribute capital to the trade. The surrounding facts of which the Appellant had no knowledge cannot form part of the Tribunal's determination of this issue.

Conclusion on whether expenditure was incurred wholly and exclusively for the business

255. Lord Walker in *Tower MCashback* provides helpful guidance on this issue and it may be helpful to set out the relevant extracts which formed the basis of our conclusion at this point:

> "I have already…quoted Lord Goff in Ensign… The facts of that case were different, since in that case there was not "in any meaningful sense" a loan at all. In this case there was a loan but there was not, in any meaningful sense, an incurring of expenditure of the borrowed money in the acquisition of software rights. It went into a loop in order to enable the LLPs to indulge in a tax avoidance scheme…
>
> …Here the issue was whether there was real expenditure on the acquisition of software rights…The transfer of ownership (or at least of rights) indicated the

> reality of some expenditure on acquiring those rights, but was not conclusive as to the whole of the expenditure having been for that purpose…
>
> …it is not enough for HMRC, in attacking a scheme of this sort, to point to the money going round in a circle..."

256. We concluded that there had been expenditure in this case; in applying the words of Lord Walker "the transfer of ownership (or at least of rights) indicated the reality of some expenditure on acquiring those rights". However, Lord Walker also noted that this was not decisive of the issue as to whether that expenditure was incurred wholly and exclusively for that purpose.

257. We did not agree with the submissions on behalf of the Appellant that the loan was full recourse on the basis of clause 7.2; to construe the loan as such would, in our view, render clause 3.1 redundant. For that reason we accepted the submission of HMRC that the loan was limited recourse.

258. In reaching our conclusion we did not consider any facts unknown to the Appellant. The loan in this case was paid directly from GFunding to GPictures (of which the Appellant was aware) and we concluded that the loan was a limited recourse loan. In the words of Lord Walker there was no "economic activity" produced by the loan until the potential income stream came into effect. As such, we accepted HMRC's submission that the money went into a loop to enable the Appellant to "indulge in a tax avoidance scheme" and that, irrespective of whether the terms were fully commercial or not, there was not, in reality, an incurring of expenditure of the borrowed money in the acquisition of the rights.

Ancillary Matters

259. We have already dealt with the submissions made on behalf of the Appellant in respect of the evidence of Mr Cannon, his "relatively junior" status within HMRC (having not obtained the status of Responsible Individual in auditing terms) and our assessment of the weight to attach to his evidence.

260. On behalf of the Appellant it was also submitted that HMRC failed to cross-examine the witnesses on behalf of the Appellant on a numbers of matters and it therefore must follow that the evidence is not challenged.

261. The Appellant relies on *Markem v Zipher* [2005] EWCA Civ 267 ("*Markem*") in which it was stated:

> "Where the court is to be asked to disbelieve a witness, the witness should be cross-examined; and a failure to cross-examine a witness on some material part of his evidence or at all, may be treated as an acceptance of the truth of that part or the whole of his evidence."

262. The Appellant submitted that this rule is necessary (and applicable to witnesses of fact and expert witnesses equally) as a matter of basic procedural fairness; the only

possible exception being where it is "perfectly clear that (the witness) has had full notice beforehand that there is an intention to impeach the credibility of the story that he is telling."

263. In response, HMRC submitted that there is no rule by which each and every statement made by a witness must be specifically challenged in cross-examination if it is not to be treated as accepted; the Appellant has overstated the breadth of the general proposition.

264. With reference to *Markem,* HMRC submitted that the essence of the rule is that:

> "Procedural fairness not only to the parties but to the witnesses requires that if their evidence were to be disbelieved they must be given a fair opportunity to deal with the allegation."

265. However, the rule is subject to the qualification that the allegation needs only to be put if no prior notice of the nature of the case upon which it is proposed to rely in contradiction of the witness has been given. In support of its argument, HMRC relied on *Browne v Dunn* (1894) 6 R 67 (HL):

> "…it will not do to impeach the credibility of a witness upon a matter on which he has not had any opportunity of giving an explanation by reason of there having been no suggestion whatever in the course of the case that his story is not accepted."

266. HMRC suggested that there is no requirement of the parties to engage in a "tick box" exercise notwithstanding that HMRC's case was fully set out in the pleadings and other documents, such as witness statements.

Conclusion on ancillary matters

267. We accept that it is a long established principle that parties in proceedings must put their case fairly and allow witnesses the opportunity to comment where their evidence in to be disbelieved. This, however, is not a case in which witnesses were to be disbelieved or their evidence impeached. All of the witnesses were professional and credible men and we had no basis upon which to disbelieve them. This was a case in which expert evidence and the recollections of witnesses of fact were evaluated and preferred on the basis of the written reports and oral explanations provided to us.

268. We analysed the wording of the requirement set out in *Markem* and we were satisfied that a number of factors had to be considered (emphasis added):

- Where the court is to be asked to <u>disbelieve</u> a witness, the witness should be cross-examined
- a failure to cross-examine a witness on some <u>material part</u> of his evidence <u>or at all</u>
- <u>may</u> be treated…

269. We have already indicated that the witnesses in this case were not disbelieved and in that respect we distinguish this case from, for example a criminal court trial in which witnesses of fact give inconsistent evidence thereby requiring a jury to disbelieve a witness in order to reach a verdict.

270. We noted that the failure to cross-examine must be in respect of a material part of the witness' evidence. We were satisfied that HMRC had cross-examined each witness for the Appellant in respect of matters which were material and upon which the witness was able to comment.

271. Even where there is a failure to cross-examine on a material part of the evidence or at all, the power to accept that evidence as accepted is discretionary.

272. We considered the purpose of the rule; being to achieve procedural fairness by allowing parties to comment where they may be disbelieved. Even applying a broad interpretation of this rule – i.e. where the witness may not be disbelieved but his evidence is not preferred – and we concluded that HMRC had cross-examined each witness appropriately. The case for HMRC was set out in detail in its pleadings and written submissions. We were entirely satisfied that all of the witnesses had a clear understanding of the issues in the case and how their respective evidence related to particular issues. We noted that the experts had not only disclosed their reports to the other but there had also been discussions between Mr Graydon and Mr Cannon in an attempt to narrow the issues between them. In those circumstances it cannot be said that there has been procedural unfairness to the Appellant by failing to list each and every point with which HMRC did not agree; the purpose of the cross-examination was to test the evidence and all parties were fully aware prior to giving evidence where the dispute regarding their evidence lay.

Decision

273. In summary we concluded:

(i) During the year ended 5 April 2007 the Appellant was not carrying on a trade.

We considered the remaining questions as if our answer to (i) above was that the Appellant had carried on a trade.

(ii) That the trade was not carried on on a commercial basis;

(iii) That the trade was not carried on with a view to the realisation of profits/so as to afford a reasonable expectation of profits;

(iv) That the profits/losses of the trade were not calculated in accordance with GAAP;

(v) That the profits/losses should be calculated using the valuation method of Mr Graydon;

(vi) That the expenditure on the rights in the films was not wholly and exclusively laid out or expended for the purposes of the trade.

274. The reference is determined accordingly.

275. 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.

J. BLEWITT
TRIBUNAL JUDGE

RELEASE DATE: 4 March 2013