HIGH COURT OF JUSTICE (QUEEN'S BENCH DIVISION)—
16 AND 17 FEBRUARY 1999

COURT OF APPEAL—16 NOVEMBER AND 21 DECEMBER 1999

HOUSE OF LORDS—25, 26 APRIL AND 23 MAY 2001

R. v. Commissioners of Inland Revenue *ex parte* Newfields Developments Ltd.[1]

Corporation tax—Reliefs—Small companies relief—Amount of relief—Restrictions on amount of relief—Restriction where company has one or more associated companies—Control of companies—Attribution to individual of rights and powers of associates—Individual associated to two sets of trustees who respectively controlled two companies—Whether the two companies associated—Whether attribution of rights and powers of associates a matter of general discretion to be exercised by Revenue only if considered appropriate to facts of the particular case—Income and Corporation Taxes Act 1988, *s* 13, 416 *and* 417.

ND was under the control of the trustees of W's will trust, under which Mrs. W had a life interest. LP was under the control of the trustees of a discretionary trust of which W had been the settlor.

ND was entitled to small companies relief under s 13 Income and Corporation Taxes Act 1988 for accounting periods ending from 30 June 1989 to 30 June 1993. Under the detailed provisions of s 13 the relief falls to be reduced (or eliminated) in respect of a company which has one or more associated companies.

Under s 13(4) companies are associated if they are both under the control of the same person, "control" being construed in accordance with s 416. Under s 416(6) "... there may also be attributed to any person all the rights and powers of any company of which ... he and associates of his have ... control ... and any such attributions shall be made under this subsection as will result in the company being treated as under the control of five or fewer participators if it can be so treated".

The meaning of "associate" for the purposes of s 416 is provided for in s 417(3). The trustees of the will trust were associates of Mrs. W under s 417(3)(c) and the trustees of the discretionary trust were her associates under s 417(3)(b).

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[1] Reported (QBD) [1999] STC 373; (CA) [2000] STC 52; (HL) [2001] UKHL 27; [2001] 1 WLR 1111; [2001] 4 All ER 400; [2001] STC 901.

The Inland Revenue took the view that under s 416(6) the rights and powers possessed by each set of trustees had to be attributed to Mrs. W, so that she controlled both ND and LP. ND challenged that decision by judicial review, contending that s 416(6) conferred a general discretion on the Revenue, enabling consideration on the facts of each particular case whether it was appropriate to make an attribution.

The Queen's Bench Division held, dismissing ND's application, that:—

(1) in adopting the mechanism of s 416 to determine whether a company is associated for the purposes of small companies relief, Parliament imported a wide definition of control which was not confined to actual control, it was not possible to discern any underlying policy in the legislation which restricted or tended to restrict the concept of control of those who had an interest or might benefit from companies over which they were deemed to have control, on the contrary it would be inconsistent with the wide approach adopted by the legislation in s 416(2)–(4) to conceive that Parliament conferred on the Revenue an unfettered power to attribute, that is, a power which is not to be exercised in order to achieve any particular result;

(2) in the context of close companies the power of attribution was not unfettered, but had to be exercised in a way which would identify a company as being a close company if possible; when importing the statutory concept of control from s 416 to s 13, Parliament did not alter the nature or character of the power from that which in s 416 was fettered by a statutory purpose into a power unfettered by any statutory purpose at all; the power had to be exercised for the statutory purpose for which it was conferred, which, in the context of s 13, was to ascertain whether in the instant case two companies were under the control of the same person pursuant to s 13(4); if it were possible to answer that statutory question in the affirmative by an exercise of the power of attribution, then that power had to be exercised, and conversely, if the question could only be answered in the affirmative by refraining from exercise of the power, the power should not be exercised.

ND appealed.

The Court of appeal held, allowing ND's appeal, that, *per* Peter Gibson and Sedley L.JJ. (Sir Christopher Staughton agreeing with the result, but by different reasoning), s 416(6) had no application; the first part of s 416(6) was not capable of having effect even though the second part was inapplicable; on its natural construction, s 416(6) was a single provision; the first part recognised that more than one attribution could be made: it could not be worded as a mandatory instruction, given that several combinations of attributions of the rights and powers of associates to a person might be possible and the same rights and powers might be attributed to more than one person; the second part dictated which, if any, of the attributions possible under the first part should be made, viz. that which would result in the company being treated as under the control of five or fewer participators. if such treatment were possible, that was the sole test provided for any attribution to be mandatory; so construed the subsection was limited to the purpose specified, viz. for the purpose of determining whether a person is to be taken to have control of a company (s 416(2)) and for the purpose of determining whether two or more persons were to be taken to have control

of a company (s 416(3)); the first part did not confer a general power or discretion independent of the second part.

The Crown appealed

Held, in the House of Lords allowing the Crown's appeal, that the concluding words subs (6) do not form part of the definition of "control" which is applied by s 13(4) and other sections; they are a special qualification of that definition for the specific purpose of deciding whether one limb of the definition of a close company is satisfied; the concluding words take effect only when one has applied the general definition of control s 416(2) or (3) as extended by the preceding part of the subsection and found that it can yield groups of participators of varying numbers who can each be treated as being in control; the concluding words then require only such attributions to be made as will result in the company being treated as under the control of five or fewer participators; but this qualification has no relevance to any case in which the general definition of control, as set out in the rest of s 416(2) to (6), is sufficient to answer the statutory question.

The Company's application for Judicial Review was heard in the Queen's Bench Division before Moses J. on 16 February 1999 when judgment was reserved. On 17 February 1999 judgment was given in favour of the Crown, with costs.

Kevin Prosser Q.C. and *Ms Elizabeth Wilson* for the Company.

Timothy Brennan for the Crown.

The cases referred to in the judgment are as follows:—*R.* v. *Sampson (Inspector of Taxes) and Others*, ex parte *Lansing Bagnall Ltd.* (1986) 61 TC 112; [1986] STC 453; [1986] STC 117; *Wicks* v. *Firth* [1983] 2 AC 214; [1983] 1 All ER 151; (1982) 56 TC 318; [1983] STC 25.

The following case was cited in oral/skeleton argument:—*Baylis (H.M. Inspector of Taxes)* v. *Roberts* (1989) 62 TC 384; [1989] STC 693.

Moses J.:—The applicant, Newfields Developments Ltd. ("Newfields"), claims entitlement to Small Companies Relief given by s 13(2) of the Income and Corporation Taxes Act 1988 ("the 1988 Act") in accounting periods ending from 30 June 1989 to 30 June 1993. The amount of relief, if any, to which it is entitled turns on whether Newfields is an associated company of Lawrek Properties Ltd. ("Lawrek"). That question itself depends upon whether Newfields and Lawrek are under the control of a Mrs. Walker within the meaning of s 13(4). Under s 13(4) control is to be construed in accordance with s 416 of the 1988 Act. The proper construction of s 416 in the context of s 13 lies at the heart of this issue.

The statutory provisions

"13. Small companies' relief

(1) Where in any accounting period the profits of a company which—

A (a) is resident in the United Kingdom, and

(b) is not a close investment-holding company (as defined in section 13A) at end of that period, do not exceed the lower relevant maximum amount, the company may claim that the corporation tax charged on its basic profits for that period shall be calculated as if
B the rate of corporation tax (instead of being the rate fixed for companies generally) were such lower rate (to be known as the 'small companies' rate') as Parliament may from time to time determine.

(2) Where in any accounting period the profits of any such company exceed the lower relevant maximum amount but do not exceed
C the upper relevant maximum amount, the company may claim that the corporation tax charged on its basic profits for that period shall be reduced by a sum equal to such fraction as Parliament may from time to time determine of the following amount—

$$(M - P) \times \frac{I}{P}$$

D

where—

M is the upper limit relevant maximum amount;

P is the amount of the profits; and

E I is the amount of the basic profits.

(3) The lower and upper relevant maximum amounts mentioned above shall be determined as follows—

(a) where the company has no associated company in the
F accounting period, those amounts are [£150,000] and [£750,000] respectively;

(b) where the company has one or more associated companies in the accounting period, the lower relevant maximum amount is [£150,000] divided by one plus the number of those associated companies, and the upper relevant maximum amount is [£750,000]
G divided by one plus the number of those associated companies."

Thus relief may be reduced or eliminated according to the number of companies associated with the taxpayer company claiming relief. The relevant part of s 13(4) reads:

H "... for the purposes of this section a company is to be treated as an 'associated company' of another at a given time if at that time one of the two has control of the other or both are under the control of the same person or persons.

In this subsection 'control' shall be construed in accordance with section 416."

I

The provisions of s 416 form part of the code contained in Part XI of the 1988 Act dealing with close companies. A close company is defined, with certain exceptions, as a company under the control of five or fewer participators (see s 414(1)). Section 416(1) provides the definition of an associated company for the purposes of Part XI and is not relevant to

entitlement to small companies relief. The definition of associated company for the purpose of that relief is to be found in that s 13(4). But the remaining subss of 416 are relevant for determining whether one company has control of another, or whether two companies are under the control of the same person or persons, for the purposes of small companies relief.

Sections 416(2) to (6) provide:

> "For the purposes of this Part, a person shall be taken to have control of a company if he exercises, or is able to exercise or is entitled to acquire, direct or indirect control over the company's affairs, and in particular, but without prejudice to the generality of the preceding words, if he possesses or is entitled to acquire—
>
> (a) the greater part of the share capital or issued share capital or voting power in the company; or
>
> (b) such part of the issued share capital of the company as would, if the whole of the income of the company were in fact distributed among the participators (without regard to any rights which he or any other person has as a loan creditor), entitle him to receive the greater part of the amount so distributed; or
>
> (c) such rights as would, in the event of the winding-up of the company or in any other circumstances, entitle him to receive the greater part of the assets of the company which would then be available for distribution among the participators.
>
> (3) Where two or more persons together satisfy any of the conditions of subsection (2) above, they shall be taken to have control of the company.
>
> (4) For the purposes of subsection (2) above a person shall be treated as entitled to acquire anything which he is entitled to acquire at a future date, or will at a future date be entitled to acquire.
>
> (5) For the purposes of subsections (2) and (3) above, there shall be attributed to any person any rights or powers of a nominee for him, that is to say, any rights or powers which another person possesses on his behalf or may be required to exercise on his direction or behalf.
>
> (6) For the purposes of subsections (2) and (3) above, there may also be attributed to any person all the rights and powers of any company of which he has, or he and associates of his have, control or any two or more companies, or of any two or more associates of his, including those attributed to a company or associate under subsection (5) above, but not those attributed to an associate under this subsection; and such attributions shall be made under this subsection as will result in the company being treated as under the control of five or fewer participators if it can be so treated."

Section 417(1) defines a 'participator'. Section 417(3) defines an 'associate'. It reads:

> "For the purpose of this Part, 'associate' means, in relation to a participator—
>
> (a) any relative or partner of the participator;

A (b) the trustee or trustees of any settlement in relation to which the participator is, or any relative of his (living or dead) is or was, a settlor ('settlement' and 'settlor' having here the same meaning as in section 681(4));

(c) where the participator is interested in any shares or obligations
B of the company which are subject to any trust, or are part of the estate of a deceased person—

(i) the trustee or trustees of the settlement concerned or, as the case may be, the personal representatives of the deceased; and

(ii) if the participator is a company, any other company
C interested in those shares or obligations;

and has a corresponding meaning in relation to a person other than a participator."

The facts relevant to the issue

D Newfields and the Revenue agree that Mrs. Walker is the widow of the late Mr. Walker. It is further agreed that the trustees of the late Mr. Walker's will trust control Newfields Development Ltd. The trustees of the late Mr. Walker's discretionary trust control Lawrek Properties Ltd. The late Mr. Walker was the settlor of the discretionary trust. Mrs. Walker has a life interest under his will trust. Thus, the trustees of the will trust controlling
E Newfields are *associates* of Mr. Walker by virtue of s 417(3)(c). The trustees of the discretionary trust controlling Lawrek are *associates* of Mrs. Walker because her late husband was a settlor of the discretionary trust by virtue of s 417(3)(b).

The Essential Question

F The issue is whether the Revenue is bound by s 416(6) to attribute to Mrs. Walker all the rights and powers of the trustees in respect of Newfields and of the Trustees in respect of Lawrek, so that for the purposes of s 416(2) she is to be taken to have both of those companies under her control and thus both those companies are associated under s 13(4). The Revenue contends that, since the process of attributing the rights of the Trustees to
G Mrs. Walker will achieve the result that both companies are under her control and thereby associated, it is bound to attribute those rights to her. The taxpayer contends that the Revenue has a discretion whether to exercise the power of attribution or not.

A power not a duty

H It is important to stress at the outset that both parties accept that the opening words of subs (6) of s 416 confer a power and not a duty. The Revenue was not asserting that in every case it was bound to make an attribution. But it was fundamental to its submissions that the decision whether to exercise the power of attribution or not depends upon whether the exercise of the power would achieve the result that the person under
I consideration satisfies the test under s 416(2). In other words, if the consequences of the exercise of the power of attribution are that a person shall be taken to have control of a company, then the power to attribute must be exercised. Equally, if the consequences of not exercising the power are that a person shall be taken to have control of a company, then the power should not be exercised. Thus it is that, the Revenue's case depends

upon the existence of a power to be exercised in accordance with a statutory purpose namely, to establish control within s 416(2) or (3) if that is possible.

The foundation for this submission lies in the words in s 416(6) which follow the semi-colon, "and such attribution shall be made under this subsection as will result in the company being treated as under the control of five or fewer participators if it can be so treated." By those words, in the context of the close companies code, the power must be exercised in a way which will achieve the result that the company in question will be treated as a close company, i.e. one with five or fewer participators. Since the power under subs (6) is to be exercised to achieve, if possible, a statutory result, so too, it is contended by Mr. Brennan on behalf of the Revenue, it must be exercised to achieve the statutory result of control in the context of small companies relief under s 13(4).

Therein, says the taxpayer, represented by Mr. Prosser Q.C., lies the fallacy. The words following the semi-colon in s 416(6) have no application in the context of s 13. The specified purpose according to which the power is to be exercised is to determine whether a company is a close company. If by attribution a company can be treated as a close company, then the power must be exercised. The statutory quest on the other hand under s 13(4) is not to determine whether a company is a close company but rather whether it is under the control of another company, or of the same person or persons. Moreover, Mr. Prosser Q.C. points out that the concept of associate and participator are not necessarily linked (see the final words of s 417(3)). Section 13(4) makes no provision for applying *mutatis mutandis* the final words of s 416 which, on their face, are irrelevant to s 13(4). The Revenue's argument, he says, requires the last words of s 416(6) to be rewritten where they apply to s 13(4).

It seems to me that the solution of the question whether the power must be exercised in a way which will lead to a result envisaged by the statute resolves the question in this motion. It does not turn upon the question whether "may" means "shall". This is because the Revenue does not contend that there is a duty to attribute. This is not surprising. Section 416(2) and (3), which are mutually exclusive, envisage that more than one person or group of persons might, at the same time, be taken to have control. Thus, to take the example of six people:

1. A has the greater part of the share capital.

2. B has the greater part of the voting power.

3. C has the right to the greater part of distributions made by the company.

4. D is a loan creditor who has rights to the greater part of the assets of the company in the event of the winding up.

5. E is entitled to acquire a greater part of the share capital, but does not hold it at present.

6. F is entitled to acquire the greater voting power but does not hold it at present.

Any one of these six may be taken to have control.

The number of possible controlling persons or groups will frequently be enlarged if attributions are made under s 416(6). Both parties accept that in any case there may be many possible combinations of the attributions of the same rights and powers. To take an example proffered by the Revenue: In relation to two companies, A Ltd. and B Ltd. and the shares in A Ltd. are owned by X and Y equally, but the shares in B Ltd. are owned by X, Mrs. X and Y equally (Mrs. X being an Associate of X pursuant to s 417(3)). A Ltd. and B Ltd. will be associated companies, if they are both under the control of the same person or persons.

A Ltd. is under the control of X and Y. But the question is, can X and Y be said to control B Ltd.? There will be many different possible combinations of the attribution of the rights and powers of associates which could be considered in order to determine whether X and Y have control of B Ltd. Thus:

1. B Ltd. is under the control of X alone (if, but only if, the rights and powers of Mrs. X are attributed to him). Thus, B Ltd. would not be under the same control as A Ltd. Any attribution would not result in A and B Ltd. being associated companies.

2. B Ltd. is under the control of Mrs. X (if, but only if, the rights and powers of X are attributed to her). This, again, would not result in B Ltd. being under the same control as A Ltd. and thus the attribution would not result in A Ltd. and B Ltd. being associated companies.

3. B Ltd. is under the control of X and Mrs. X (if no attributions at all are made). Again, there is no common control of A and B Ltd.

4. B Ltd. is under the control of Y and Mrs. X. Again no attributions are made. Again, there is no common control.

5. B Ltd. is under the control of X and Y taken together if no attributions are made. This combination, which results from refraining from the exercise of the power of attribution, gives X and Y control of B Ltd.

The control of both A Ltd. and B Ltd. would be under X and Y and both therefore would be associated companies. In that example it is to be noted that under item 5 the Revenue chooses not to exercise the power to attribute because *non-attribution leads to the result and A and B Ltd. are associated companies.* Hence it accepts that it is under a power and not a duty. The taxpayer, on the other hand, submits that there is no warrant for exercising the power (*in casu* refraining from attribution) in a way which leads to common control of A and B Ltd. In the context of small company relief there is conferred upon the Revenue a general discretion whether to attribute or not.

In support of that submission the taxpayer contends that the underlying policy of the provisions in relation to small company relief is to avoid the possibility that a taxpayer may enlarge the relief to which a company he controls may be entitled by fragmenting his businesses between associated companies. It makes sense to reduce that relief in cases where a person may benefit, or a close relative may benefit, from a number of associated small companies. But, Mr. Prosser Q.C. says, it makes no sense to regard such a

person as Mrs. Walker as having control over a company such as Lawrek in which she has no interest or from which she may derive no benefit. He gave other useful examples; where A owns all the shares in X Ltd. he says it would make no sense to regard B as having control of X Ltd. where B has no interest or influence over X Ltd. for example, where A is a Junior Partner in a large firm of City solicitors and B is the Managing Partner. Both are associated for the purposes of s 417(3). A owns all the shares in X Ltd. which has nothing to do with the firm or with B. He gave another example where A and B, although married, are separated by court order. Since the separation A has acquired shares in X Ltd. but B has nothing to do with X Ltd.

In recognition that the exercise of the power of attribution may lead to unfair results, the taxpayer points to extra statutory concession C9 which provides at 5:

> "The Revenue will, by concession, treat the definition of a relative (in the Taxes Act 1988, section 417(4)) for the purposes of the Taxes Act 1988 section 13 as including only a husband or wife or child who is a minor. This part of the concession applies only in respect of companies where there is no substantial commercial interdependence between them."

Mr. Prosser says that subs (6) should be construed in a way which will avoid the obvious unfairness demonstrated in the examples he gave. The very existence he says, of the extra-statutory concession at C9 suggests that the result for which the Revenue contends was not the intention of Parliament (see the speech of Lord Bridge in *Wicks* v. *Firth* (1982) 56 TC 318, at page 359; [1983] STC 25, at page 29).

Conclusion

Parliament has adopted the mechanism of s 416 to determine whether a company is associated for the purposes of small company relief. In so doing it has imported a wide definition of control which is not confined to actual control. No better support for that proposition can be found than in the use by the legislature by the words *shall be taken to have* and in subs (4) the reference to future entitlement.

In those circumstances, I am of the view that it is not possible to discern any underlying policy in the legislation which restricts or tends to restrict the concept of control to those who have an interest or may benefit from companies over which they are deemed to have control. On the contrary, it seems to me inconsistent with the wide approach adopted by the legislature in s 416(2) to (4) to conceive that Parliament conferred on the Revenue an unfettered power to attribute, that is a power which is not to be exercised in order to achieve any particular result.

It would be odd if Parliament had conferred an unfettered power designed, as the taxpayer contends, to restrict the width of the statutory concept of control. In the context of close companies, no such unfettered power exists. It must be exercised in a way which will identify a company as being a close company if possible. In my judgment, when importing the statutory concept of control from s 416 into s 13, Parliament did not alter the nature or character of the power from that which in s 416 is fettered by a statutory purpose into a power unfettered by any statutory purpose at all. True it is that the final words after the semi-colon in s 416(6) have no application. But, in my judgment, it is not to be supposed that the nature of

the power has changed. Like so many statutory powers, it is to be exercised for the statutory purposes for which it was conferred. In the context of s 13, that purpose is to ascertain whether, in the instant case, two companies are under the control of the same person pursuant to s 13(4). That is the statutory question. If it is possible to answer that in the affirmative, by exercising the power of attribution, in my judgment, that power must be exercised. Conversely, if that question, namely, are the two companies under the control of the same person, can only be answered in the affirmative by refraining from the exercise of the power, then the power should not be exercised. To characterise that power is not to rewrite the last words of s 416(6) or add the words *mutatis mutandis* to s 13(4), rather it is to retain the nature of the power and to recognise the statutory purpose for which it is to be exercised. It is of course possible, as Mr. Prosser painfully reminds me, for the legislation to confer a power, whilst providing no guidance as to how it is to be exercised. An example is to be found in *R.* v. *Sampson (Inspector of Taxes) and Others,* ex parte *Lansing Bagnall Ltd.* [1986] STC 453; (1986) 61 TC 112. That case, in a different statutory context, is authority for the proposition that a general discretion may be conferred upon the Revenue without any statutory guidance as to how it is to be exercised. It is true that it concerned a Schedule, namely Sch 16 to the Finance Act 1972, which formed part of a chapter which contains the precursor to s 416 of the 1988 Act. But I do not think that case assists me. In *Lansing Bagnall* the Revenue contended for a duty to apportion covenanted donations of a close company among its participators. I have been at pains, at the risk of some repetition, to emphasise that in this case it is accepted that only a power has been conferred. But I am driven to the conclusion that it is a power which must be exercised for a discernible statutory purpose, namely to determine whether it is possible to identify the common control of the companies under consideration. The power must be exercised in a way which enables that identification to be made. In this case it is possible, by exercising the power of attribution, to categorise Newfields and Lawrek as being under the common control of Mrs. Walker. Accordingly, I conclude that the Revenue is bound to exercise the power under s 416(6) and this application fails.

Application dismissed, with costs.

The Company's appeal was heard in the Court of appeal (Peter Gibson, Sedley L.JJ and Sir Christopher Staughton) on 16 November 1999 when judgment was reserved. On 21 December 1999 judgment was given against the Crown, with no order as to costs.

Kevin Prosser Q.C. and *Ms Elizabeth Wilson* for the Company.

Timothy Brennan for the Crown.

The Cases referred to in the Judgment are as follows:—*Regina* v. *Sampson (Inspector of Taxes) and others,* ex parte *Lansing Bagnall Ltd.* (1986) 61 TC 112; [1986] STC 453; [1986] STC 117; *Wicks* v. *Firth* [1983] 2 AC 214; [1983] 1 All ER 151; (1982) 56 TC 318; [1983] STC 25.

The following case was cited in oral/skeleton argument:—*Commissioners of Inland Revenue* v. *R. Woolf & Co (Rubber), Ltd.* 39 TC

611; [1962] Ch 35; *Baylis (H.M. Inspector of Taxes)* v. *Roberts* 62 TC 384; [1989] STC 693; Regina v. H.M. Inspector of Taxes, Reading ex parte Fulford-Dobson 60 TC 168; [1987] Q.B.D 978.

Peter Gibson L.J.:—

The taxpayer company, Newfields Developments Ltd. ("Newfields"), with the leave of Moses J. appeals from the order made by him on 17 February 1999 dismissing the taxpayer's application for judicial review. Newfields sought to challenge a decision of the Commissioners of Inland Revenue contained in a letter dated 22 September 1997 that no discretion was conferred on them by s 416(6) Income and Corporation Taxes Act 1988. Newfields claimed a declaration that the Commissioners had failed to exercise their discretion and sought an order of mandamus requiring them to exercise their discretion.

The appeal gives rise to a short question of statutory construction. The context in which it arises is that Newfields claims entitlement to small companies' relief. A more favourable rate of corporation tax is chargeable in respect of companies which satisfy the conditions of s 13. The amount of relief, if any, to which a company is entitled turns on whether the taxpayer has an associated company or associated companies and that in turn depends on who has control of the companies in question.

The Judge's judgment is now reported ([1999] STC 373; TC leaflet 3581) and it is unnecessary to set out in full the elaborate provisions in s 13 governing qualification for the relief. It is sufficient to note that this depends (among other things) on the company being resident in the U.K. and not being a close investment-holding company and on its profits falling within certain specified brackets. The upper and lower amounts depend on whether or not the company has an associated company or associated companies. By s 13(4) (so far as material)

> "... for the purposes of this section a company is to be treated as an 'associated company' of another at a given time if at that time one of the two has control of the other or both are under the control of the same person or persons.
>
> In this subsection 'control' shall be construed in accordance with section 416."

Section 416 contains certain provisions which set out, for the purposes of Part XI of the Act (relating to close companies), the meaning of the terms "associated company" and "control". The meaning there given for "associated company" is not relevant for the purposes of small companies' relief. But the provisions of s 416 relating to control are material.

They are as follows:

> "(2) For the purposes of this Part, a person shall be taken to have control of a company if he exercises, or is able to exercise, or is entitled to acquire, direct or indirect control over the company's affairs, and in particular, but without prejudice to the generality of the preceding words, if he possesses or is entitled to acquire—

A (a) The greater part of the share capital or issued share capital of the company or of the voting power in the company; or

(b) such part of the issued share capital of the company as would, if the whole of the income of the company were in fact distributed among the participators (without regard to any rights B which he or any other person has as a loan creditor), entitle him to receive the greater part of the amount so distributed; or

(c) such rights as would, in the event of the winding-up of the company or, in any other circumstances, entitle him to receive the greater part of the assets of the company which would then be C available for distribution among the participators.

(3) Where two or more persons together satisfy any of the conditions of subsection (2) above, they shall be taken to have control of the company.

D (4) For the purposes of subsection (2) above a person shall be treated as entitled to acquire anything which he is entitled to acquire at a future date, or will at a future date be entitled to acquire.

(5) For the purposes of subsections (2) and (3) above, there shall be attributed to any person any rights or powers of a nominee for him, that is to say, any rights or powers which another person possesses on his E behalf or may be required to exercise on his direction or behalf.

(6) For the purposes of subsections (2) and (3) above, there may also be attributed to any person all the rights and powers of any company of which he has, or he and associates of his have, control or any two or more such companies, or of any associate of his or of any F two or more associates of his, including those attributed to a company or associate under subsection (5) above, but not those attributed to an associate under this subsection; and such attributions shall be made under this subsection as will result in the company being treated as under the control of five or fewer participators if it can be so treated."

G Section 417 (1) defines the meaning of a participator in relation to any company, being a person having a share or interest in the capital or income of the company, and that meaning is expanded by the subsection. Subsection (3) defines the meaning of "associate" in this way:

H "(3) For the purposes of this Part "associate" means, in relation to a participator—

(a) any relative or partner of the participator;

(b) the trustee or trustees of any settlement in relation to which the participator is, or any relative of his (living or dead) is or was, a I settlor ("settlement" and "settlor" having here the same meaning as in section 681 (4)); and

(c) where the participator is interested in any shares or obligations of the company which are subject to any trust, or are part of the estate of a deceased person—

(i) the trustee or trustees of the settlement concerned or, as the case may be, the personal representatives of the deceased; and

(ii) if the participator is a company, any other company interested in those shares or obligations;

and has a corresponding meaning in relation to a person other than a participator.

(4) In subsection (3) above, "relative" means husband or wife, parent or remoter forebear, child or remoter issue, or brother or sister."

The late Henry Walker was the settlor of a discretionary trust, the trustees of which hold the share capital of and so control Lawrek Properties Ltd. ("Lawrek"). The trustees of Mr. Walker's Will hold the share capital of and therefore control Newfields. Under the Will Mrs. Walker has a life interest. Mrs. Walker is not a participator in relation to Newfields, but the Will trustees by virtue of s 417(3)(c)(i) and the concluding words of subpara (c) are her associates, and the trustees of the discretionary trust are by virtue of s 417(3)(b) and (4) also her associates. Mrs. Walker is not a participator in Lawrek. Nor is she a trustee of or beneficiary under the discretionary trust.

Newfields is a company resident in the U.K. and is not a close investment-holding company. There was correspondence between the accountants for Newfields and the Revenue as to whether Lawrek was an associate company of Newfields for the purposes of s 13. On 22 September 1997 the Revenue informed the accountants that it was their view that the two companies were associated and that there were no circumstances to justify a departure from the Revenue's policy of attributing the rights and powers of the trustees to Mrs. Walker. Newfields then applied for leave to apply for judicial review of the decision in that letter. Leave to apply was granted by Lightman J. and the case came before Moses J.

The Judge posed the essential question in this case as follows ([1999] STC 373, at page 377; TC Leaflet 3581, at page 5): "The issue is whether the Revenue is bound by s 416(6) to attribute to Mrs. Walker all the rights and powers of the trustees in respect of Newfields and of the trustees in respect of Lawrek, so that for the purposes of s 416(2) she is to be taken to have both of those companies under her control and thus both those companies are associated under s 13(4)."

The Judge emphasised that both parties accepted that the opening words of subs (6) conferred a power and not a duty. The contention of the Revenue was that since the power of attribution of the rights of the trustees to Mrs. Walker would achieve the result that both Newfields and Lawrek were under her control and thereby associated, it was bound to attribute those rights to her. The Judge noted that the Revenue's case depended upon the existence of a power to be exercised in accordance with a statutory purpose, namely to establish control within s 416(2) or (3) if that were possible. He said that the foundation for that submission lay in the second part of subs (6), though the Revenue only relied on that as showing that the power under subs (6) was to be exercised to achieve, if possible, "a statutory result". That result, in a close company context, was that the company would be treated as a close company if that were possible. In the context of small companies' relief, the Revenue contended, the power was to be exercised to achieve the statutory result of control.

A Newfields contended before the Judge that the Revenue was given a discretion by the first part of s 416(6) whether to exercise the power of attribution or not. It was contended that the second part of s 416 (6) had no application in the context of s 13.

B The Judge thought that the solution of the question whether the power must be exercised in a way which would lead to a result envisaged by the statute resolved the issue in the case. He was of the view that it was not possible to discern any underlying policy in the legislation which restricted or tended to restrict the concept of control to those who had an interest or might benefit from companies over which they were deemed to have control. C He said that the power of attribution had to be exercised in the context of close companies in a way which would identify a company as being a close company if possible. He said ([1999] STC 373, at page 380; TC Leaflet 3581, at page 9):

> D "In my judgment, when importing the statutory concept of control from s 416 into s 13, Parliament did not alter the nature or character of the power from that which in s 416 is fettered by a statutory purpose into a power unfettered by any statutory purpose at all. True it is that the final words after the semi-colon in s 416(6) have no application. But, in my judgment, it is not to be supposed that the nature of the power has changed. Like so many statutory powers, it is to be exercised for the E statutory purposes for which it was conferred. In the context of s 13, that purpose is to ascertain whether, in the instant case, two companies are under the control of the same person pursuant to s 13(4). That is the statutory question. If it is possible to answer that in the affirmative; by exercising the power of attribution, in my judgment, that power must be exercised. Conversely, if that question, namely, are the two companies F under the control of the same person, can only be answered in the affirmative by refraining from the exercise of the power, then the power should not be exercised."

G In this case, the Judge said, it was possible by exercising the power of attribution to categorise Newfields and Lawrek as being under the control of Mrs. Walker. Accordingly he concluded that the Revenue was bound to exercise the power, and he dismissed Newfields' application.

H Before this Court in substance the same arguments as were advanced before the Judge are put forward, though Mr. Brennan for the Crown was somewhat more equivocal as to whether the first part of s 416(6) was a power. He drew attention to the absence from s 416(6) of any identification of a person in the Revenue to exercise the power, and submitted that the explanation of the language "may be attributed" was that those words provide for the possible attributions which could be made. He pointed out that there might be many possible combinations of attributions of rights and I powers to different people. Although he does not contend that "may" means "shall", he does not rely on the second part of s 416 (6), which on his contention has no application. Thus, in arguing for the purposes of s 13(4) that there must be an attribution of the rights and powers of associates to Mrs. Walker because this would give her control of both companies, he relies only on the first part of s 416.

Mr. Prosser Q.C. for Newfields submits that the first part of s 416(6) is worded as a discretion in contrast with the mandatory language of the second part, as that, he says, must have been intended by Parliament to enable the Revenue by a proper exercise of discretion to avoid attribution in the cases where it makes no sense to treat a person as being in control. He points to the extraordinary width of the language in ss 416 and 417 which if applied literally would produce results so strange that they could not have been intended by Parliament. He refers to the fact that the Revenue has published Extra-Statutory Concession C9 to mitigate the results of its interpretation, and he reminds us of the remarks of Lord Bridge in *Wicks* v. *Firth* [1983] STC 25 at page 29; [1983] 2 AC 214; (1982) 56 TC 318 that in choosing between competing constructions of a taxing provision, it is legitimate to lean against a construction which is mitigated by way of extra-statutory concession. He points out that control by five or fewer participators is only one of 16 contexts in which the concept of control is used in Part XI and that the mandatory part of subsection (6) says nothing at all about the exercise of the power to attribute in relation to any of the other 15 contexts, nor in relation to s 13(4).

I have to say that I have found neither side's arguments wholly persuasive. Both treat the first half of s 416(6) as capable of having effect even though the second half is treated as inapplicable because the context is other than one requiring the determination of the question whether the company is under the control of five or fewer participators. Mr. Prosser in arguing for a general discretion in the Revenue to make attributions divines that the policy of the statute is that attribution should be made so far as it is sensible to do so. That is so vague a notion that I should be extremely reluctant to conclude that this must have been Parliament's intention. Mr. Brennan is no less bold in asserting that what is worded as a possible attribution becomes an obligatory attribution not by force of the mandatory words in the second part of the subsection but, as it were, by analogy without any corresponding mandatory words. He called the technique used in s 13 to import s 416 as "economical". A less kind description, if he is right, might be thought more apt.

For my part, I do not think that the true construction of s 416 (6) does give rise to any difficulty. On its natural construction it seems to me to be a single provision, the second half closely related to the first as can be seen by the conjunction "and" following the semi-colon and the reference to the attributions under the subsection which are to be made. If one asks the question whether, for the purpose of determining whether a company is a close company, Parliament envisaged that attributions under the first part of the subsection would be made in circumstances to which the second part did not apply, the answer would surely be "No". The contrary would be a prescription for confusion.

I do not regard the first half as creating a power or discretion. A power is an authority enabling a designated person to choose whether and in what manner to act or not to act and a discretion similarly requires the identification of a person to exercise the discretion. Draftsmen of taxing statutes are normally meticulous in designating whether it is the Inspector of Taxes or the Board of Inland Revenue who is or are to exercise a power or discretion. The 1988 Act itself provides examples of both distinct types of designation (compare, for example, s 12(8)(a) and s 13(9) with s 747(1)). Here it is significant that no one is designated. The subsection seems to me to

provide an instruction to the Revenue and the taxpayer alike as to how control of a company for the purposes of s 416(2) and (3) is to be determined. The first part of the subsection recognises that more than one attribution could be made. It could not be worded as a mandatory instruction, given that several combinations of attributions of the rights and powers of associates to a person may be possible and the same rights and powers might be attributed to more than one person. Hence the use of the word "may" in "may be attributed". The second part of the subsection dictates which, if any, of the attributions possible under the first part of the subsection will be made, *viz.* that which will result in the company being treated as under the control of five or fewer participators if such treatment is possible. That is the sole test provided for any attribution to be mandatory.

So construed, the subsection is limited to the purpose specified, *viz.* for the purpose of determining whether a person is to be taken to have control of a company (subs (2)) and for the purpose of determining whether two or more persons are to be taken to have control of the company (subs (3)). The first part of subs (6) is not a general power or discretion conferred on the Revenue or anyone in the Revenue or independent of the second part but a recognition of the possibilities of attribution, and the obligation to attribute is dependent on the single criterion of whether the company can by such attribution be treated as under the control of five or fewer participators. Without such obligation no attribution is to be made. While an unfettered discretion may be conferred on the Revenue (and *Regina* v. *H.M. Inspector of Taxes and Others* ex parte *Lansing Bagnall Ltd.* [1986] STC 453; (1986) 61 TC 112 provides a rare example of such a discretion conferred on the Inspector of Taxes), the courts, not surprisingly, have generally been reluctant to find that Parliament so intended, as Balcombe L.J. in *Lansing Bagnall* [1986] STC 453 at page 458 stated. I would not be prepared so to find unless ineluctably driven to that conclusion, as I was in *Lansing Bagnall.*

Mr. Prosser drew our attention to para 3 (2) Sch 18 Finance Act 1965. This is part of the group of provisions which were the predecessors to ss 415 and 416. Paragraph 3(1) corresponds with s 416(2) but refers to "members" rather than participators. Paragraph 3(2) gives the meaning of member in subpara (1) as including any person having a share or interest in the capital or income of the company and provides that a person "shall be treated" as entitled to acquire anything which he is entitled to acquire at a future date or will at a future date be entitled to acquire. Paragraph 3 (2) then continues: "... but ... any such loan creditor as is mentioned in paragraph 4(1)(b) below may be treated as a member ..." Mr. Prosser submitted that not only is this another example, of a general discretion conferred on the Revenue but that it was particularly significant because para 3(4) was the predecessor of s 416 (6) in virtually identical language.

I do not think it permissible to construe what to my mind is the clear language of a consolidation Act by reference to earlier statutory provisions. The wording of para 3(2) seems to me to have been something of an aberration which was not repeated once the Income and Corporation Taxes Act 1970 was enacted. It did not designate who might decide to treat a loan creditor as a member or in what circumstances; further para (3)(2), unlike para 3(4) contained no provision requiring such treatment by virtue of the satisfaction of a stated test.

More difficulty is perhaps occasioned by the bare importation of s 416 into s 13 for the construction of "control". The context of s 13, small companies' relief, is not the same as that of s 416, close companies. But there is nothing in s 13(4) to indicate that radical adaptations must be made to any part of s 416. In particular s 13(4) contains nothing to suggest that the second part of s 416(6) falls to be ignored as inapplicable, nor need it be treated as inapplicable if it is recognised as only providing the applicable test for mandatory attribution for the purpose of determining control of a company, *viz.* will the attribution cause the company to be under the control of five or fewer participators? For the reasons already given, I regard s 416(6) as containing a single provision which cannot sensibly be divided up into independent parts. There is no difficulty in applying that test for the purposes of s 13(4): unless the possible attributions lead to there being five or fewer participators no attribution shall be made.

It may be thought surprising that that test, appropriate to close companies, should be made applicable to small companies' relief. But it does not produce a nonsensical result. It merely means that the test for making attributions for determining whether a company is under the control of five or fewer participators is being used for determining whether a company is under the control of another company or both are under the control of the same person or persons. Further as Mr. Prosser pointed out, in another part of the same Act, s 756(3), where s 416 has been applied to controlled foreign companies, s 416(6) has been specifically adapted to the particular circumstances relevant to such companies and substitute wording has been introduced in place of "five or fewer participators". In marked contrast no such adaptation is to be found in s 13. The absence of such adaptation must, in my opinion, be taken to be deliberate.

On the application of the test of the second part of s 416(6) it is not in dispute that, as Mrs. Walker is not a participator, attribution to her of the rights and powers of her associates is not required. Unless therefore the first part of the subsection is to be treated as creating a free-standing provision either creating an obligation to make an attribution in particular cases not within the second part or a power or discretion which the Revenue can exercise (without Parliament indicating who within the Revenue can do so or on what criteria), there can be no question of Lawrek being treated as an associate company of Newfields. For the reasons already given, neither of those possibilities is in my judgment correct.

I differ from the Judge with his great experience of tax matters with unease and that discomfort is increased by my inability to accept the arguments of either counsel with such extensive knowledge in this field as Mr. Prosser and Mr. Brennan. But for the reasons which I have given I fear that that is my conclusion. I would for my part hear counsel on what order should follow.

Sedley L.J.:—I agree with the conclusion of Peter Gibson L.J. If I set out in my own words my reasons for doing so, it is because I have found this a baffling case in which Sir Christopher Staughton's solution has many attractions.

One starts, conventionally, with the plain meaning of the words on the page—or if "plain" is too sanguine an adjective for present purposes, with their grammatical and logical meaning. One then asks whether this meaning

A can be taken without more as conveying the legislature's intentions or whether some subtler intent has to be sought.

A facial reading of subs (6) in the context of s 416 seems for all the world to describe a two-tier function: a power to attribute to a person more rights and powers than he or she immediately possesses, and an obligation to B do so where a particular result will follow.

But the Commissioners submit and Moses J. whose experience in this field is very great, agreed that properly understood the subsection means something different. It is not, Mr. Brennan says, that "may" means "shall": neither the language of the statute nor the purpose for which he contends C requires or permits such a reading. Nor, however, does it mean "may", at least in the ordinary sense of the verb. It can be paraphrased, Mr. Brennan says, by the words "...there shall also be attributable...". The purpose is not to place the process of attribution at large: it is to allow for the sifting of alternative combinations of rights and powers in order to establish which are and which are not to be attributed to the person in question. "The D mandatory word *shall*," Mr. Brennan submits in writing, "appears in s 416(6) itself so as to direct consideration of all the possible tests of attribution; the relevant attributions are those which give the result that there are 5 or fewer participators, and they *shall* be made."

The objection that the drafter, if this was what he or she was getting at, E could have put it a lot more simply is admittedly a doomed one in the field of taxation statutes; but I venture it all the same. Complexity may not in the end matter where, once unravelled, tangled words reveal their meaning. But where on the face of them the words have an intelligible, or at least an apparent, meaning, the obscurity of a proffered alternative meaning inevitably counts against it. F

Moses J., however, did not find the meaning particularly obscure. He began with the unexceptionable proposition that the section "imported a wide definition of control which is not confined to actual control". From this premise he reasoned that Parliament cannot have intended to introduce "an unfettered power designed ... to restrict the width of the statutory concept of G control". The principal power in the subsection, he concluded, was therefore "to be exercised for the statutory purposes for which it was conferred", namely to decide upon the attribution of control, deciding it affirmatively where that was possible. "Conversely," he went on, "if that question, namely are the two companies under the control of the same person, can only be answered in the affirmative by refraining from the exercise of the power, then H the power should not be exercised."

The difficulty I have had with this reasoning, with great respect, is that it proceeds from its premise (the wide meaning of control), across a bridge (that an unfettered power to cut down the wide meaning is unthinkable), to its conclusion (that the power is to be exercised for the statutory purpose); I but the bridge will not bear the weight, and the conclusion, when one reaches it, begs the original question. I will try to explain why.

An unfettered power to cut down the statute's wide meaning is not (whatever the width of his submission) the necessary consequence of Mr. Prosser Q.C.'s argument: only that a function governed by ordinary public

law principles, including that of statutory purpose, is created and in specified circumstances has to be exercised. The Revenue's argument from supposed consequences is correspondingly unconvincing. More than this, however, the Judge's conclusion that the power is to be exercised or withheld in order to achieve the statutory purpose, in itself a legal truism, is of significance only if the statutory purpose can be seen to be something which the Appellant's reading of the subsection would subvert. For the reason I have given, as well as for the reasons given by Peter Gibson L.J., I do not believe that it is. Nor is it illogical to find such a provision lodged at the end of a series of mandatory requirements: its natural place is where it will sweep up situations that have escaped the antedecent rules. What would be odd is to find a mandatory requirement (the last three lines of subs 416(6)) qualifying something which is expressed as an elective function but which turns out to be another mandatory requirement.

These are reasons why I have been drawn towards Sir Christopher Staughton's solution. But their irresistible force finally encounters the immovable object pointed out by Peter Gibson L.J.: who is supposed to exercise the power in the first part of the subsection? Not only might it be the Inspector or the Board; why should it not be the taxpayer? The omission is so inexplicable that one is thrown back on the only alternative solution: that the purpose of s 416(6) is not to create an elective power at all but to set out a single test for attribution which tells Crown and taxpayer alike where they stand.

From this premise, which I reach with considerable diffidence, the course proposed by Peter Gibson, L.J. will follow. It is the least worst solution of a problem created by a mode of drafting which rewards readers who desire clarity by offering them riddles.

Sir Christopher Staughton:

We have to decide whether Lawrek Properties Ltd. is associated with Newfields Developments Ltd. That depends, according to s 13(4), on whether one of the two has control of the other, or both are under the control of the same person.

Mrs. Walker has as associates the trustees of her late husband's will. That is a consequence of s 417(3)(c). Those trustees hold the share capital of Newfields.

Again, Mrs. Walker has as associates the trustees of a discretionary trust set up by her late husband: Section 417(3)(b). Those trustees hold the share capital of Lawrek.

If then the rights and powers of the two sets of trustees are attributed to Mrs. Walker under s 416(6), because they are her associates, then she will be taken to control both Lawrek and Newfields: s 416(2). That in turn will mean that the two are associated companies, with the consequence that each may be deprived, in whole or in part, of small companies relief.

What then are the circumstances which will or may give rise to attributions, so as to lead to those consequences?

A The first part of s 416(6) provides that there *may* be attributed to any person the rights and powers of her associates. The second part of the subsection tells one that such attributions *shall* be made "as will result in the company being treated as under the control of five or fewer participants if it can be so treated".

B That test in the second part of the sub-section is quite inappropriate if it is applied in the course of determining whether, for the purposes of small companies relief and s 13 of the 1988 Act, the two companies are associated. Whether a company is or is not under the control of five or fewer participators is of no discernible relevance to the question whether it is associated with another company. So far as I can detect, it is an entirely C adventitious test for deciding that question.

What is to be done? The three possible solutions are—(1) to ignore the second part of subs (6) when one is referred to s 416 by s 13,(2) in addition, to substitute a different criterion as to when subs (6) must be operated, or (3) to apply the sub-section as it stands, including the second part, warts and all. D

There are two other places where Parliament has expressly adopted the second solution. The first is in Part XVII of the same Act's 756(3):

> "(3) The following provisions of Part XI apply for the purposes of this Chapter as they apply for the purposes of that Part— E
>
> (a) section 416; and
>
> (b) section 417(7) to (9);
>
> but, in the application of subsection (6) of section 416 for the purposes of this Chapter, for the words 'five or fewer participators' F there shall be substituted the words 'persons resident in the United Kingdom'."

The second case is s 96(10)(a) of the Taxation of Chargeable Gains Act 1992.

> G "(10) For the purposes of this section—
>
> (a) the question whether a company is controlled by a person or persons shall be construed in accordance with section 416 of the Taxes Act, but in deciding that question for those purposes no rights or powers of (or attributed to) an associate or associates of a person shall be attributed to him under section 416(6) if he is not a H participator in the company."

Parliament was thus aware, both in 1988 and since, that s 416(6) might need some alteration when applied by reference to other situations. But no alteration has expressly been provided for in the present case, where the reference is in s 13 of the 1988 Act. I

I forbear to say that a taxing statute should be construed against the party who proposed the wording in it, even if that was most probably the Inland Revenue. There was once a principle, and there may still be to some extent, that subjects are not to be taxed upon an ambiguity. But that too I can leave out of account. In the end I am driven to the conclusion like Peter

Gibson and Sedley L.JJ., that we should apply the wording of s 416(6) as it stands. It may make little sense to do so, which goes to show that we do need a Revising Chamber—at least a revising person—in Parliament.

If we do that, the second part of the sub-section does not require attributions to be made in this case. That is because Mrs. Walker is not a participator in either company, and no amount of attribution to her can, as far as I can see, *cause* there to be five or fewer participators. The number of participators, it would seem, will remain five, or more, or less, despite any attributions to Mrs Walker.

It remains to consider whether the Inland Revenue may make attributions even when they are not compelled to do so by the second part of s 416(6). In my judgment the conspicuous use of the word "may" in the first part of s 416(6), as opposed to "shall" in subs (5) and in the second part of subs (6), demonstrates that there can be attribution which is not commanded by subs (6). I hesitate to use the words "power" and "discretion", as there seems to be a view that those words have some technical meaning in this context. But I do consider that the Revenue have a choice to exercise, a decision to take, on whether to attribute in non-mandatory cases. Indeed, both parties to this appeal argue that there is a choice to be made. They differ whether that choice should be exercised in a similar way to that required by the second part of s 416(6), so as to ensure that more tax is paid rather than less; or should be exercised upon all the circumstances of the case, including for example the fact that some remote associate does not in practice have anything to do with the company which he is said to control.

I have found that a very difficult question. But in the end I conclude that to say that the choice of the Inland Revenue is required to be exercised in such a way as to make tax paid to a maximum extent is, in effect, to insert a revised mandatory second part in s 416(6) such as I have already rejected. So I would answer that there is a general discretion in the Commissioners of Inland Revenue. As they have not exercised it, this appeal must be allowed.

Application allowed, with no order as to costs. Leave to appeal to the House of Lords refused.

The Crown's appeal was heard in the House of Lords (Lords Bingham of Cornhill, Steyn, Hoffmann, Cooke of Thorndon and Scott of Foscote) on 25 and 26 April 2001 when judgment was reserved. On 23 May 2001 judgment was given in favour of the Crown, the Appellant to pay the Respondent's costs.

Lord Goldsmith Q.C., *Timothy Brennan Q.C.* and *David Ewart* for the Crown.

Kevin Prosser Q.C. and *Elizabeth Wilson* for the Company.

No cases are referred to in the speeches but the following cases were cited in argument:—*Commissioners of Inland Revenue* v. *Park Investments Ltd.* [1966] 1 WLR 540; 43 TC 200; *Commissioners of Inland Revenue* v. *R. Woolf & Co. (Rubber) Ltd.* [1961] 1 WLR 177; 39 TC 611; *Pepper* v. *Hart*

[1993] AC 593; 65 TC 421; *Regina* v. *Sampson (H.M. Inspector of Taxes) and others ex parte Lansing Bagnall Ltd.* 61 TC 112; [1986] STC 453; *Wicks* v. *Firth (H.M. Inspector of Taxes)* [1983] 2 AC 214; 56 TC 318; [1983] STC 25.

Lord Bingham of Cornhill

My Lords,

1. For reasons given by my noble and learned friends, Lord Hoffmann and Lord Scott of Foscote, which I have had the benefit of reading in draft, I would allow this appeal and restore the order of the Judge.

Lord Steyn

My Lords,

2. I have had the advantage of reading in draft the speeches of my noble and learned friends, Lord Hoffmann and Lord Scott of Foscote. For the reasons which they have given I would also allow the appeal.

Lord Hoffmann

My Lords,

3. The Finance Act 1972 introduced a relief for small companies in the form of a reduced rate of corporation tax. The full relief can be claimed if the company's profits in the relevant accounting year do not exceed one specified amount and partial relief can be claimed if they do not exceed another specified amount. The conditions for obtaining the relief and the specified amounts are now contained in s 13 of the Income and Corporation Taxes Act 1988 as amended. The reduced rate is 20 per cent., as against the full rate of 30 per cent.

4. The relief would be open to obvious abuse if a business could be divided among two or more companies so that each earned profits below the specified amount. Section 13(3) therefore provides that if a company has one or more associated companies, the relevant specified amount shall be divided by the number of associated companies plus one. Thus a company with one associated company can claim the relief in full or in part only if its profits in the relevant accounting period do not exceed half the relevant specified amount.

5. The question in the present appeal is whether the taxpayer company (Newfields Developments Ltd., which I shall call "Newfields") has an associated company or not. The Revenue contend that it has an associated company as defined in the Act, namely a company called Lawrek Properties Ltd. ("Lawrek"). I shall in due course describe what the Revenue say is the relevant relationship between the two companies but, in order to explain why the Revenue say that their relationship is relevant, I must first go into the details of the rather complicated definition of an associated company.

6. Associated companies are defined in s 13(4) as companies of which one controls or is controlled by the other or both under the control of the

same person or persons. Crucial to this definition is therefore the concept of control, which the subsection says "shall be construed in accordance with section 416".

7. The primary purpose of s 416 is to define the expressions "associated company" and "control" for the purposes of Part XI of the Act, which deals with close companies. The term "close company" appeared for the first time in the Finance Act 1965, which introduced the corporation tax, but had its roots in earlier concepts: the company "under the control of not more than five persons" in respect of which income could be apportioned to its members for surtax purposes under s 21 of the Finance Act 1922 and the "company whereof the directors have a control interest therein" which was limited in the deductions it could make in respect of directors' salaries for the purposes of profits tax by para 11 of Sch 14 to the Finance Act 1937. The close company is defined by s 414(1), subject to exceptions, as "one which is under the control of five or fewer participators, or of participators who are directors". Part XI provides that in certain respects close companies are to be subject to a special fiscal regime. Thus the definition of control in s 416, which originally appeared in para 3 of Sch 18 to the Finance Act 1965, was for a purpose quite different from its use in s 13(4), which made its first appearance in the Finance Act 1972.

8. The definition of a close company made it necessary to provide definitions of "participator" and "control". Participator is defined by s 417(1):

> "For the purposes of this Part, a 'participator' is, in relation to any company, a person having a share or interest in the capital or income of the company, and, without prejudice to the generality of the preceding words, includes—
>
> (a) any person who possesses, or is entitled to acquire, share capital or voting rights in the company;
>
> (b) any loan creditor of the company;
>
> (c) any person who possesses, or is entitled to acquire, a right to receive or participate in distributions of the company (construing 'distributions' without regard to section 418) or any amounts payable by the company (in cash or in kind) to loan creditors by way of premium on redemption; and
>
> (d) any person who is entitled to secure that income or assets (whether present or future) of the company will be applied directly or indirectly for his benefit.
>
> In this subsection references to being entitled to do anything apply where a person is presently entitled to do it at a future date, or will at a future date be entitled to do it."

9. Control is defined in s 416, of which the relevant subs are (2) to (6):

> "(2) For the purposes of this Part, a person shall be taken to have control of a company if he exercises, or is able to exercise or is entitled to acquire, direct or indirect control over the company's affairs, and in particular, but without prejudice to the generality of the preceding words, if he possesses or is entitled to acquire—

A (a) the greater part of the share capital or issued share capital of the company or of the voting power in the company; or

(b) such part of the issued share capital of the company as would, if the whole of the income of the company were in fact distributed among the participators (without regard to any rights which he or any other B person has as a loan creditor), entitle him to receive the greater part of the amount so distributed; or

(c) such rights as would, in the event of the winding-up of the company or in any other circumstances, entitle him to receive the greater part of the assets of the company which would then be available for distribution among the participators.

C

(3) Where two or more persons together satisfy any of the conditions of subsection (2) above, they shall be taken to have control of the company.

(4) For the purposes of subsection (2) above a person shall be D treated as entitled to acquire anything which he is entitled to acquire at a future date, or will at a future date be entitled to acquire.

(5) For the purposes of subsections (2) and (3) above, there shall be attributed to any person any rights or powers of a nominee for him, that is to say, any rights or powers which another person possesses on his behalf or may be required to exercise on his direction or behalf

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(6) For the purposes of subsections (2) and (3) above, there may also be attributed to any person all the rights and powers of any company of which he has, or he and associates of his have, control or any two or more such companies, or of any associate of his or of any two or more associates of his, including those attributed to a company F or associate under subsection (5) above, but not those attributed to an associate under this subsection; and such attributions shall be made under this subsection as will result in the company being treated as under the control of five or fewer participators if it can be so treated."

10. It will be seen that although this definition starts in subs (2) with a G concept of control which reflects its meaning in ordinary speech ("a person shall be taken to have control of a company if he exercises, or is able to exercise or is entitled to acquire, direct or indirect control over the company's affairs"), that fairly simple notion is enormously widened by subsequent subsections. Subsection (4) deems the person in question to already have interests which have not yet vested and subs (5) attributes to him the rights H or powers of his nominees. Subsection (6) goes much further in providing that for the purposes of deciding whether a person falls within the definition in (2) (or the definition of joint control in (3)) any person may have attributed to him the rights or powers of any associate or of any company which he or his associates or both have control. The full breadth of this extension can be seen from the definition of "associate" in s 417(3):

I "For the purposes of this Part 'associate' means, in relation to a participator—

(a) any relative or partner of the participator;

(b) the trustee or trustees of any settlement in relation to which the participator is, or any relative of his (living or dead) is or was, a settlor

('settlement' and 'settlor' having here the same meaning as in section 681(4)); and

(c) where the participator is interested in any shares or obligations of the company which are subject to any trust, or are part of the estate of a deceased person—

(i) the trustee or trustees of the settlement concerned or, as the case may be, the personal representatives of the deceased; and

(ii) if the participator is a company, any other company interested in those shares or obligations;

and has a corresponding meaning in relation to a person other than a participator."

11. "Relative" is defined in s 417(4) to mean "husband or wife, parent or remoter forebear, child or remoter issue, or brother or sister". The effect of these cumulative definitions is that for the purpose of deciding whether a person "shall be taken to have control of a company" under s 416(2), it may be necessary to attribute to him the rights and powers of persons over whom he may in real life have little or no power of control. Plainly the intention of the legislature was to spread the net very wide.

12. Against this statutory background one can turn to what the Revenue say is the relevant relationship between Newfields and Lawrek. The issued share capital of Newfields is held by the trustees of the will of the late Mr. Walker. Under the trusts of that will, his widow Mrs. Walker has a life interest. Her life interest in the shares means that she is a "participator" in Newfields (s 417(1)(c)) and, more to the point, the trustees are her "associates" (s 417(3) the trustees plainly have power to control Newfields and if that power is attributed to Mrs. Walker under s 416(6), she must be taken under s 416(2) to have control of Newfields.

13. The issued share capital of Lawrek is held by the trustees of a discretionary settlement established by the late Mr. Walker in his lifetime. Mrs. Walker has no interest under that settlement-to avoid the income being deemed to be that of Mr. Walker, she was expressly excluded from taking any benefit. She is therefore not a participator. Nevertheless, she is a relative of the settlor and therefore it is said that under s 417 (3)(b), as applied to non-participators by the concluding words of the subsection, the trustees of that settlement are also her associates. If their powers are attributed to her under s 416(6), then she must be taken to have control of Lawrek as well. It follows that Newfields and Lawrek are under the control of the same person and are associated companies.

14. The first ground upon which the taxpayer objected to this conclusion was that s 416(6) does not say that the powers of associates must be attributed to Mrs. Walker. The subsection says "may". Therefore the taxpayer submits that the Revenue has a discretion as to whether to make an attribution or not. The discretion should be exercised to prevent taxpayers from abusing the relief under s 13. In this case, however, the taxpayer says that it would be unfair to make an attribution because there is no abuse. Mrs. Walker has no interest in Lawrek and no real control over its affairs. It and Newfields are quite separate companies.

15. The Revenue denied that s 416(6) conferred a discretion. They said that the word "may merely indicated that such an attribution would not always be made. It should be made if the result was that a given person or persons would be taken to have control within the meaning of s 416(2) or (3). Otherwise not. But this depended upon the consequences of the attraction and not upon the discretion of the Revenue. On 22 September 1997 the inspector wrote to the taxpayer's accountant saying that the Revenue had no discretion and proposed to refuse small companies' relief.

16. Newfields issued proceedings for judicial review of this decision. It sought a declaration that there was a discretion and an order of mandamus requiring it to be exercised.

17. Moses J. [1999] STC 373 TC Leaflet 3581 held that the Revenue were right. He recorded, at Page 377, that both parties had agreed that "the opening words of subs (6) of s 416 confer a power and not a duty". But he said, at page 380, that the Revenue were obliged to exercise the power for the purpose for which it was conferred. That purpose was "to ascertain whether, in the instant case, two companies are under the control of the same person". If an attribution will produce an affirmative answer, an attribution should be made.

18. The taxpayer appealed to the Court of Appeal [2000] STC 52; TC Leaflet 3598 where a majority (Peter Gibson and Sedley L.J. agreed on this point with the judge. Sir Christopher Staughton, on the other hand, thought that the Revenue had a discretion which ought to have been exercised. In rejecting the notion of a discretion, Peter Gibson L.J. said that it was significant that no one was designated as the person in whom the discretion was vested. Was it the inspector, the Commissioners or the taxpayer? It seemed to him to "provide an instruction to the Revenue and the taxpayer alike as to how control of a company for the purposes of s 416(2) and (3) is to be determined.": Page 59. Sedley L.J. said that, although he was tempted by the notion of discretion, he agreed that the absence of anyone upon whom it purported to be conferred was an irremovable objection.

19. In my opinion the judge and the majority in the Court of Appeal were right. In addition to the absence of any person identified as entrusted with a discretion, there is the absence of any grounds upon which the discretion should be exercised. Even without subs (6), the definition of control is wide and can apply to people who have no real control over the company's affairs. This makes it difficult to apply the reality of control as a criterion for exercising a discretion. If real control were to be the test, the opening words of s 416(2) would be enough. The purpose of the extended definition appears to be to make it unnecessary for the Revenue to have to make detailed factual inquiries.

20. Sir Christopher Staughton, in taking the opposite view, naturally attached importance to the word "may". But the word appears in an impersonal construction- "there may also be attributed" - and I think that its force is not facultative but conditional, as in "VAT may be chargeable". The question of whether VAT is chargeable does not depend upon anyone's choice but on whether the conditions for charging VAT are satisfied: are the goods or services subject to VAT, is the trader registrable and so on. Likewise, the question of whether rights or powers should be attributed

depends upon whether the necessary conditions have been satisfied. As Peter Gibson L.J. pointed out at page 59 the draftsman could not sensibly have said "there shall also be attributed" because s 416(6) permits a wide range of attributions. Some will result in a given person or persons being in control within the meaning of subs (2) or (3) and others will not.

21. It should be noted that while subs (2) specifies the conditions under which "a person" shall be taken to have control, subs (6) says that for the purposes of subs (2), there may be attributed to "any person" all the rights and powers of companies under his control, associates and so forth. The possible subject of attribution is therefore not confined to the candidate for control. Thus, while subs (6) would permit the attribution to the candidate of powers exercisable by his wife, it would also permit the attribution to his wife of powers exercisable by him. In the first case, the result might be to treat the candidate as being in control when otherwise he would not be. In the second, it might be to treat him as not being in control when otherwise he would be. If all the attributions possible under subs (6) were mandatory, it could not be applied without absurdity and contradiction.

22. Although the point may be merely verbal, I do not think that it is right to say, as the parties appear to have done before Moses J., that "may" confers a "power". It is true that there are powers which in certain circumstances must be exercised. But I think it is clearer, having regard to the impersonal use of "may" in the subsection, to say that it expresses conditionality.

23. If the force of the word "may" is conditional, the next stage in the argument is to identify the conditions under which an attribution must be made. The argument before the judge seems to have proceeded on the basis that although the conditions were not spelled out in subs (6), they could be inferred from the purpose of subs (6) as an adjunct to subss (2) and (3), namely to specify what counts as being in control of a company. In the same way, if it said in a catalogue "VAT may be chargeable", it would not be necessary to spell out that it would be chargeable if the conditions for charging VAT were satisfied. That would be obvious from the nature of VAT.

24. The judge therefore concluded, as I have already stated, that an attribution should be made if the result would be to treat the candidate or candidates as being in control of the company, but not otherwise. He did say at one point that the purpose of s 416(6) was to "ascertain whether ... two companies are under the control of the same person pursuant to section 13(4)": page 380. Mr. Prosser objected that this involved illegitimately reading the purpose of s 13(4) into a general definition of control which served a number of different provisions, each having its own purpose. But I do not think that the judge meant to say more than that the general purpose of s 416 was to tell one whether a given person could be said to be in control of a given company and that subs (6) was part of the hypothesis on which one answered that question. Section 13 (4) requires one only to ask whether an affirmative answer can be given in respect of both companies.

25. On this point, however, the Court of Appeal disagreed. They said that one could not treat subs (6) as subject to conditions which could be inferred from subs (2) and (3) because the conditions under which

attributions should be made were already spelled out in the concluding words of the subsection itself:

> "such attributions shall be made under this subsection as will result in the company being treated as under the control of five or fewer participators if it can be so treated".

26. The Court of Appeal treated these words as laying down exhaustively the conditions under which attributions could and should be made. It followed that unless the attributions would result in the company being treated as under the control of five or fewer participators, they could not be made at all. Mrs. Walker was not a participator in Lawrek and the effect of an attribution would therefore not result in Lawrek being under the control of five or fewer participators. On the other hand, if coincidentally it would have had that effect, the attribution could have been made for the purposes of refusing small companies' relief.

27. This construction produces a very arbitrary result and would appear to make s 416(6) an unsuitable element in any definition of control for the purposes of s 13(4). Small companies' relief does not depend upon whether the company is a close company or not. No doubt most companies which qualify for the relief will be close companies but that is not essential. The question, or rather one of the questions, raised by s 13(4) is whether a person who controls a company applying for relief also controls one or more other companies. In deciding what counts as controlling another company, it would be illogical to attribute additional powers only if the effect was to bring that other company within the definition of a close company. That would seem an irrelevant consideration. Mr. Prosser said that one could avoid this illogicality by treating the whole of subs (6) as applicable only to the question of whether a company was a closed company. But this would leave it open to anyone to claim small companies' relief by dividing his business between companies controlled by himself and his wife, or himself and the trustees of discretionary settlements for the benefit of his family. The absence of the attribution provisions of subs (6) would leave a large gap in the defence which s 13(4) provides for the public revenue.

28. The Court of Appeal were fully aware that their construction produced a rather odd result. Peter Gibson L.J. spoke of unease and discomfort and Sedley L.J. said he reached the answer with considerable diffidence.

29. In my opinion, if the concluding words were not there, one would have no difficulty in inferring from subs (2) and (3) that the conditions for attribution are whether or not it resulted in the person or persons under consideration being treated as being in control. Once one has rejected the notion of a discretion, there can be no other intelligible construction. The question is whether this conclusion is displaced by the concluding words or whether those words serve some other purpose.

30. In my opinion, they do serve another purpose. Section 416(2) to (6), up to the commencement of the concluding words, provides a definition of control. If one wants to know of any person or persons whether he or they must be treated as having control of a given company, those parts of the section will provide the answer. For many of the purposes for which the

concept of control is used, that is all that one requires. In the present case, for example, all one wants to know is whether Mrs. Walker can be said to be in control of Newfields and of Lawrek. But there are cases in which it is not enough to know that it can be said of a certain person, or certain people, that they control company A. An example is the question of whether company A is a close company, which involves not only asking whether participators control the company but also whether they are directors or number five or fewer.

31. There is no difficulty about applying the definition to answer the question of whether the company is controlled by participators who are directors. If one or more people who answer that description control the company within the meaning of s 416(2) or (3), as extended if necessary by the other subsections including (6), the definition is satisfied. But the question of whether the controlling participators are five or fewer is different. If one simply said that an attribution should be made under subs (6) if it resulted in a given participator or participators being treated as in control, it could yield the result that various numbers of participators were in control. With some attributions it could be five or fewer, without them or with others, more.

32. In my opinion, therefore, the concluding words of subs (6) do not form part of the definition of "control" which is applied by s 13(4) and other sections. They are a special qualification of that definition for the specific purpose of deciding whether one limb of the definition of a close company is satisfied. The concluding words take effect only when one has applied the general definition of control in s 416(2) or (3) as extended by the preceding part of the subsection and found that it can yield groups of participators of varying numbers who can each be treated as being in control. The concluding words then require one to make only such attributions as will result in the company being treated as under the control of five or fewer participators. But this qualification has no relevance to any case in which the general definition of control, as set out in the rest of s 416(2) to (6), is sufficient to answer the statutory question.

33. In the present case, as I have said, the general definition is sufficient to answer the question. I would therefore allow the appeal and restore the order of Moses J.

Lord Cooke of Thorndon

My Lords,

34. I have had the advantage of reading in draft the speech of my noble and learned friends Lord Hoffmann and Lord Scott of Foscote. For the reasons which they have given I would also allow the appeal.

Lord Scott of Foscote

My Lords,

35. I have had the advantage of reading in advance the opinion of my noble and learned friend, Lord Hoffmann. I agree with his analysis of the relevant statutory provisions and with his reasons for allowing the appeal.

A 36. One of the issues of construction that was debated before the Court of Appeal was whether or not s 416(6) of the 1988 Act should be treated as a single provision. The relevance of this Issue was that if it were to be treated as a single provision, then, so it was argued, the whole of the subsection, including the passage after the semi-colon, i.e. "; and such attributions shall be made ..." etc., would have to be applied when answering the question B whether Mrs. Walker was to be treated as in control of Lawrek. If that were right, the passage would then have a limiting effect, preventing the attributions prescribed by the subsection from having any function other than to allow a company to be treated as under the control of five or fewer participators and, consequently, a close company. Peter Gibson L.J. [2000] STC 52, at page 59; TC Leaflet 3598, at page 7 concluded that the subsection C should be treated as a single provision:

> "On its natural construction it seems to me to be a single provision, the second half closely related to the first as can be seen by the conjunction 'and' following the semi-colon and the reference to the attributions under the subsection which are to be made."

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37. He held that, since Mrs. Walker was not a participator *vis-á-vis* Lawrek, none of the subs (6) attributions could be used in order to treat her as in control of Lawrek and to enable Newfields and Lawrek to become, for s 13(4) purposes, associated companies.

E 38. The purpose of subs (6) when originally enacted in para 3 of Sch 18 to the Finance Act 1965 enable such attributions to be made as would result in a company becoming a close company for the purposes of that Act. In that context it seems to me accurate to treat the subsection as a single provision. It required, and still does require, to be applied as a single provision for the purpose of enabling a company to be treated as a close F company.

39. But s 13(4) of the 1988 Act has nothing to do with close companies. It is concerned ether or not companies are "associated" with one another. They are to be treated as associated if "one of the two has control of the other or both are under the control of the same person", and, s 13(4) G declares, "'control' shall be construed in accordance with s 416."

40. In applying s 416 in order to construe "control" in s 13(4) and to determine whether companies are "associated", the whole of s 416 must be applied. To omit subs (6) would make no sense and defeat an important part of the statutory intention underlying s 13. But, in applying subs (6), the H passage after the semi-colon, which has relevance only to the identification of close companies and no relevance to whether or not companies are "associated", should simply be ignored. It has no part to play.

41. Subsection (2) of s 416 provides that:

I > "a person shall be taken to have control of a company if he exercises, or is able to exercise or is entitled to acquire, direct or indirect control over the company's affairs ..."

The words I have cited prescribe a test of actual control. But s 416 goes on, in the remaining part of subs (2) and in subs (4), (5) and (6), to describe circumstances in which whether or not a person has actual control, the

person "shall be taken to have control". It is worth emphasising the word "shall" in subs (2). There is no element of discretion. A

42. Subsection (6) describes a number of circumstances in which, for the purposes of subs (2), control "may ... be attributed" to a person. The particular circumstances that permit an attribution of control to a person are not necessarily exclusive of the circumstances that permit an attribution of B control of the same company to some other person. The facts relating to two companies may, under subs (6), permit the attribution of control to several different people.

43. This, in my opinion, explains the use of the word "may" in subs (6). The use of the word "may" does not lead to the conclusion that the subsection creates a discretionary power. The absence of any indication of the criteria by which the discretion is to be exercised or any identification of the person by whom the discretion is to be exercised seems to me to make that plain. In my opinion, the use of the word "may" was an acceptable linguistic means of indicating that not every permutation of control thrown up by subs (6) attributions has to be applied when the question whether a particular person has control of a particular company is being considered. Subsection (6) supports subs (2). Subsection (2) says that "a person *shall* be taken to have control of a company if ..." (Emphasis added). This mandatory provision, supplemented by subs (6) attributions requires, in my opinion, that when the circumstances of a particular person are being examined in order to determine whether that person has control of a particular company, that person "shall be taken" to have control if any of the possible subs (6) attributions give him or her control.

44. For these reasons and those given by Lord Hoffmann I, too, would allow this appeal.

Appeal allowed, Appellant to pay Respondent's costs incurred in respect of this appeal to the House of Lords.

[Solicitors:—Solicitor of Inland Revenue; Messrs. Allen and Overy.]

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