Press Summary

16 July 2024

Centrica Overseas Holdings Ltd (Appellant) v Commissioners for His Majesty's Revenue and Customs (Respondent)

[2024] UKSC 25

On appeal from [2022] EWCA Civ 1520

Justices: Lord Hodge (Deputy President), Lord Stephens, Lady Rose, Lord Richards, Lady Simler

Background to the Appeal

This appeal concerns section 1219 of the Corporation Tax Act 2009 ("the 2009 Act") which enables a company with investment business to deduct the expenses of management of that business in calculating its profits for the purpose of calculating corporation tax. However, by section 1219(3)(a) of the 2009 Act, expenses of management cannot be deducted if they constitute capital expenditure.

The appellant ("COHL") is an investment holding company in the Centrica Plc group. Its principal activity is holding capital investments for the purpose of long-term investment from which it derives value, and significantly, its business is to manage its capital assets, not to trade with them. The question in the appeal is whether professional advisory fees incurred by COHL, which are accepted to have been expenses of management, were revenue expenditure and therefore deductible, or capital expenditure and therefore not deductible by virtue of section 1219(3)(a) of the 2009 Act.

In July 2005, COHL acquired a Dutch company, Oxxio BV ("Oxxio"), with four subsidiaries. The investment in Oxxio proved unsuccessful and generated significant losses. In June or July 2009, Centrica Plc resolved to sell Oxxio and took immediate steps to achieve that aim, including instructing professional advisers. In March 2011, following a lengthy process, the assets of two of the Oxxio subsidiaries and the shares in a third subsidiary were sold by COHL. Between July 2009 and March 2011, COHL paid professional fees in connection with the sale of Oxxio to Deutsche Bank AG London, PricewaterhouseCoopers ("PwC") and De Brauw, which totalled £2,529,697 (the "Disputed Expenditure"). COHL claimed relief for the Disputed Expenditure in its tax return for the accounting period ending 31 December 2011. However, HMRC denied the claim on the basis that the Disputed Expenditure was not deductible because it was not an expense of management and, even if it was, it was capital in nature.

COHL appealed to the First-tier Tribunal ("FTT"), which found that most (but not all) of the Disputed Expenditure was expenses of management, but dismissed the appeal on the basis that the Disputed Expenditure was not incurred by COHL. In respect of the capital expenditure question, the FTT found that some of the Disputed Expenditure was revenue expenditure and would have been deductible, and some capital expenditure and not deductible. COHL appealed to the Upper Tribunal, which allowed the appeal, finding that all of the Disputed Expenditure was both expenses of management of COHL and revenue expenditure, and therefore deductible. HMRC appealed to the Court of Appeal, which found that the Disputed Expenditure was expenses of management, but allowed HMRC's appeal on the basis that the Disputed Expenditure was capital in nature and therefore not deductible. It is now agreed that the Disputed Expenditure was expenses of management, and COHL appeals to the Supreme Court only on the question whether the Disputed Expenditure was capital in nature.

Judgment

The Supreme Court unanimously dismisses COHL's appeal. It holds that the Disputed Expenditure was capital in nature, and therefore not deductible under section 1219(3)(a) of the 2009 Act. Lady Simler gives the only judgment, with which the other Justices agree.

Reasons for the Judgment

As an investment business, COHL is entitled to deduct expenses of management under section 1219(1) of the 2009 Act when calculating its total profits to calculate its liability to corporation tax. However, expenses of a capital nature may not be deducted as they are excluded by section 1219(3)(a) of the 2009 Act. This is similar to the position of ordinary trading companies which cannot deduct expenses of a capital nature in calculating their profits: see section 53(1) of the 2009 Act. **[12]-[16]**, **[19]**.

COHL argues that as a matter of statutory interpretation, the words "expenses of a capital nature" in section 1219(3)(a) of the 2009 Act have a more limited meaning than the similar phrase in section 53(1), and were intended only to exclude the acquisition costs of investments themselves (together with expenditure not separable from those costs) and a limited category of fixed capital costs such as buildings. The Supreme Court disagrees. The words of section 1219(3)(a) are clear and straightforward, as is their statutory context. The words "expenses of a capital nature" in s1219(3)(a) and "items of a capital nature" in section 53(1) must mean the same thing. Both were intended to carve out expenses which are capital in nature by reference to the concept of expenditure of a capital nature already well-established in the tax code and the case law **[51]-[52]**.

Parliament can be taken to have been aware of the established capital/revenue case law when it first legislated to introduce the capital bar in 2004, by section 38 of the Finance Act 2004. It would be surprising if the exclusion for capital expenditure was intended to have a special narrower meaning without anything to signal that this was so. The supporting material, legislative history and timing of the introduction of the capital exclusion all demonstrate an intention in the legislation to align the trading company and investment company rules in relation to capital expenditure. The same legislative purpose is readily inferred from the fact that the capital exclusion was re-enacted in section 1219(3)(a) of the 2009 Act using the same words "of a capital nature" as those found in section 53(1) of the 2009 Act without any limit or qualification signalling a contrary intention. Section 1219(3)(a) is to be interpreted in accordance with well-established capital/revenue principles accordingly **[53]-[55], [61]**.

The question whether expenditure is capital or revenue in nature is a question of law. The previously decided cases reflect the fact that items of expenditure on the borderline can be

difficult to assign between these two broad categories. There is no single test that can be applied to decide which items are capital expenditure and which are revenue in every case. Rather, much depends on the circumstances. Nonetheless, the capital/revenue case law is useful in providing illustrations of the approach adopted and of the factors regarded as relevant in a particular set of circumstances. The principles derived from the cases are useful, provided it is recognised that they cannot automatically be applied to a different fact pattern or circumstance **[62]-[64]**.

A good starting point is to identify the purpose for which the payment is made; in other words, what the money is being spent on. This must be assessed objectively, and not according to the subjective motive or purpose of the taxpayer. There are cases, particularly those involving trading companies, where difficulties can arise in determining on which side of the revenue/capital line the expenditure in question falls. In these cases, a helpful starting point is to identify whether some form of asset has been obtained. However, there is no such difficulty in this appeal: whereas the investments of an investment dealing company are revenue assets (or circulating capital) with which it trades, the investments of a holding company are capital assets (or fixed capital), and its business is to manage those assets. COHL's investments are capital assets, and this includes its investment in Oxxio. Where a capital asset is identified, it can generally be assumed that money spent on the acquisition or disposal of the asset should be regarded as capital expenditure **[65]-[67], [70]-[71], [75]**.

Applying these principles to the facts found by the FTT, the Disputed Expenditure was incurred on professional and advisory services and was expenses of management. Fees for such services are capable of being either revenue or capital in nature. Such fees take their character from the commercial or business transaction for which they are incurred. Here, Oxxio was an onerous capital asset. The transaction achieved in substance the disposal of this loss-making investment from the Centrica group. Looked at objectively, once a commercial decision was taken to dispose of the Oxxio business, the services of Deutsche Bank, PwC and De Brauw were obtained to enable management to achieve that disposal. The Disputed Expenditure was both directed at and focused on bringing about the disposal, in whatever form that transaction ultimately took. Since money expended to achieve the disposal of a capital asset is properly regarded as being of a capital nature, the Disputed Expenditure was capital in nature. It was not therefore deductible as an expense of management for corporation tax purposes **[80]-[83], [87], [89]-[90]**.

References in square brackets are to paragraphs in the judgment.