



TC03251

Appeal number: TC/2013/01623

CORPORATION TAX – Closure Notice and Amendment – whether the Appellant Company is associated with another company for corporation tax purposes – appeal dismissed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

**GHELANIS SUPERSTORE AND
CASH AND CARRY LIMITED**

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE J. BLEWITT
MR. R. CROSLAND**

Sitting in public at Bradford on 15 January 2014

Mr A. D. Wells, Partner of AVN Venus Tax LLP for the Appellant

Mrs H. Drayson, Officer of HM Revenue and Customs, for the Respondents

DECISION

Appeal

5 1. This is an appeal against a Closure Notice for the year ending 31 March 2010
which gave rise to additional corporation tax in the sum of £13,125 and a Revenue
Amendment for the year ending 31 March 2009 which also gave rise to additional
corporation tax in the same amount. The Appellant appealed against the Closure
Notice, which was issued on 18 December 2012, on 25 February 2013. The grounds
10 of appeal relied upon were set out in the Notice of Appeal as: “The Appellant
company is entitled to the full relief for small companies and the additional tax
claimed is not due.”

2. We were helpfully provided with skeleton arguments by both parties prior to the
hearing, which were expanded upon in oral submissions by Mr Wells and Mrs
15 Drayson at the hearing.

3. The question to be determined by the Tribunal is whether the Appellant is
associated with a company called Eco Efficient Energy Limited (“EEE”). It was not
disputed that the relief is due to the Appellant if the companies are found not to be
associated and that conversely, the relief is not due if the companies are associated.

20 Undisputed Background Facts

4. The Appellant is a wholesaler and retailer of grocery, food, consumables and
related products. On 1 November 2011 an enquiry was opened into the Appellant’s
return for the year ending 31 March 2010. The return stated that there were no
associated companies in the period.

25 5. One area of the enquiry was whether the Appellant was associated with EEE,
which in the year ended 31 August 2009 had traded and made a small loss. The issued
share capital of the Appellant and EEE is owned by the same 7 shareholders in the
following ratios:

Group	Shareholder(s)	Relationship	Shareholding in Appellant	Shareholding in EEE
A	Mr GG Ghelani	Father and	12.5%	9%
	Mrs GG Ghelani	Mother	12.5% (=25%)	8% (=17%)
B	Mr HG Ghekani	Son and daughter-in-	12.5%	17%

	Mrs Ghelani	MP law	12.5% (=25%)	16% (=33%)
C	Mr HG Ghelani Mrs Ghelani	Son and daughter-in- law	12.5% 12.5% (=25%)	17% 16% (=33%)
D	Mrs Ghelani	BR Daughter-in- law (widowed)	25% (=25%)	17%

Legislation

6. There was no dispute between the parties as to the legislation applicable to this case; the dispute between the Appellant and HMRC lies in the interpretation of that legislation.

Section 13 ICTA 1988

7. Section 13 of ICTA 1988 provides that a company can claim a reduction in the full rate of corporation tax payable (Marginal Relief). That relief, which is determined by reference to a formula, is reduced where a company has one or more associated companies.

8. Section 13(4) of the same Act provides that “...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 section “control” shall be construed in accordance with section 416...”

9. Section 416 (2) ICTA 1988 provides a number of tests for determining the issue of “control.” The parties agreed that the following provisions of s 416 (2) (a) applies to this case:

“A person shall be taken to have control of a company...if he possesses or is entitled to acquire...(a) the greater part of the share capital or issued share capital of the company or of the voting power in the company.”

10. Section 416 (3) provides that “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.”

11. Section 416 allows the rights and powers of any associate to be attributed to a person. There was no dispute between the parties that as the shareholders include 3

married couples, the shareholding of one spouse can be attributed to the other meaning that there are effectively 4 groups of participators in each company, shown in the table above as A, B, C and D.

The Appellant's Case

5 12. It is submitted by Mr Wells on behalf of the Appellant that the greater part of the share capital of EEE was possessed by B and C together. Consequently it is submitted that EEE is not associated with the Appellant for the purposes of Section 13 ICTA 1988 as the Appellant was not controlled by these same persons.

10 13. Mr Wells referred us to HMRC's guidance manuals CTM 03730 and CTM 60250 in which the concept of "minimum controlling combination" for any company was developed.

CTM 03730

15 *"More than one person (or group of persons) may have control of a company at the same time. For example, one person may have the greater part of the voting power, while another holds the greater part of the issued share capital and yet a third is entitled to the greater part of the assets in a winding-up*

20 *Whether or not two companies are under the control of the same person will appear after applying the control tests in **CTA10/S450 and S451** (formerly **ICTA88/S416 (2) to (6)**) to both companies. However, to determine whether two companies are under the control of the same **persons** it is necessary to look at which group or groups of persons control each company.*

Two companies are only under the control of the same persons if:

- *a group which controls one company is identical with a group which controls the other, and*
- 25 • *for each company, that group is a 'minimum controlling combination'.*
A 'minimum controlling combination' means a group of persons which has control of the company but which would not have control of it if any one of the persons were excluded from the group.

30 *For example, if three unconnected persons, A, B and C, each hold one third of the shares in a company, there are three minimum controlling combinations; A and B together, or B and C together, or A and C together. Control is held by any two together, so the addition of another person to the controlling combination is superfluous - A, B and C together do not form a control group for this purpose."*

CTM 60250

35 *"More than one person or one group of persons may 'control' a company. For example, one person may have the greater part of the voting power, while two people hold the greater part of the issued share capital and a group of three people are entitled to the greater part of the assets in a winding up. All three combinations of*

people can be taken to have control of the company at the same time.

If say three persons, A, B and C, each hold one third of the shares in a company, and they are not connected in any way which would allow the rights and powers of one to be attributed to another, then control is held by A and B, or B and C, or A and C but not A, B and C together.

This is because in determining whether companies are 'associated companies', you should only consider 'minimum' controlling combinations. You should disregard combinations containing superfluous members. For example, a company controlled by the unconnected persons A, B and C, but not by any one or two of them alone should not be regarded as associated with any company controlled by one of them alone (as in the first subparagraph above) or by any two of them (as in the second subparagraph above).

However deciding on the 'minimum' controlling combination for any of the tests set out at CTA2010/S453 (3) (a) to (d) (formerly ICTA88/416 (2)(a) to (c)) does **not** mean you have to establish the smallest controlling combination of each company when determining whether companies are associated companies.

So in the first sub-paragraph above, you may be able to determine that two companies are associated because the three people who together have an entitlement to the greater part of the assets in a winding up also together hold the greater part of the voting power in another company. In that case you would take this group as controlling the company and not the single or two person combinations. As this example shows, the identical controlling combination does not need to be established by the same test in each company.”

14. It is submitted that B and C were the only minimum controlling combination in EEE and that HMRC has incorrectly interpreted its own manuals in this case. Mr Wells noted that in practice it is relatively uncommon to find private companies in which the various rights are divided in different proportions to the share capital, but when that situation exists it is right to look at all of the combinations envisaged by section 416 (2). The guidance correctly suggests that in such a case, different combinations of shareholders may have different control under various tests. The test is that of control and it is submitted that it is not possible for multiple combinations to all have control at the same time.

15. In respect of the Appellant, it is accepted that the combination of A, B and D hold the majority of the shares for both companies. It is equally true that A, C and D hold a majority for both companies. However HMRC cannot explain why A, B and D possess the greater part of the share capital yet A, C and D do not, or if both combinations possess the greater part of the share capital, HMRC cannot explain how that gives one combination control. The correct analysis is that neither has control.

16. The only logical approach is to identify the smallest combination that gives unambiguous control, otherwise any two companies would be associated in which the identity of the shareholders is identical but the percentage of shareholdings is not.

17. The correct approach is to identify the “minimum controlling shareholding” for each company and then see if they are identical. B and C together (as being the least number of shareholders who could control EEE) own the greater part of the share capital of EEE and therefore that is the minimum controlling shareholding. B and C do not possess the greater part of the share capital in the Appellant and consequently the companies cannot be said to be associated.

18. Mr Wells submitted that the legislation did not envisage different people having control of a company at the same time and the reality of the situation must be looked at; in EEE it is B and C where control exists. The test of control is not who *could* have control, but rather who *actually* does have control.

HMRC’s Case

19. On behalf of HMRC Mrs Drayson contended that the correct interpretation of the legislation is to establish all of the combinations of persons who could control one company under s416(3) and then separately consider the second company and apply the same process. The result will then determine whether the two companies are associated.

20. Only a minimum controlling combination should be considered, which is defined in HMRC’s guidance CTM 60250 as “*a group of persons which has control of the company but would not have control of it if any of the persons were excluded from the group.*” HMRC submit that this definition is implicit in the legislation at s 416 (3) which refers to “*two or more persons together*” who satisfy the conditions for control set out in s 416 (2). The minimum controlling combination envisages identifying persons who have control without any superfluous participants.

21. In respect of the Appellant the possible minimum controlling combinations are:

- A, B and C (75%)
- A, B and D (75%)
- A, C and D (75%)
- B, C and D (75%)

22. For EEE the possible minimum controlling combinations are:

- B and C (66%)
- A, B and D (67%)
- A, C and D (67%)

23. Mrs Drayson submitted that the legislation does not preclude HMRC from looking at a number of minimum controlling combinations, even where those combinations have a greater number of participants. The only stipulation of the

legislation is that the combination together should satisfy one of the conditions in s 416 (2). The alternative combinations set out at paragraph 22 above are therefore equally valid and should not be confined to B and C.

5 24. HMRC submitted that it should be recognised that whilst B and C are one possible minimum controlling combination, if the two participants fails to act together others would have control. The alternative combinations of A, B and D and A, C and D do not contain any superfluous participants as all 3 are required to possess a greater shareholding.

10 25. As a result, there are two combinations that can control both companies: A, B and D and A, C and D and the companies are therefore associated.

Decision

26. We considered the submissions of both parties carefully. We should note that we were sympathetic to the Appellant's position and we accepted that there were no issues or inferences of deliberate tax avoidance in this case.

15 27. Our approach was to consider the legislation and whilst we had regard to HMRC's guidance, we bore in mind that it is not based in statute.

28. We noted that the wording of the legislation set out at section 416 (2) provides as follows:

20 *"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..."

25 29. The legislation clearly envisages a person (or persons) as having control "*if he exercises or is able to exercise...direct or indirect control...*" (emphasis added). The section goes on to refer to the 3 particular tests set out in subsection (2) (a) – (c) "*...but without prejudice to the generality of the preceding words...*" In those circumstances we were satisfied that the test for control includes any persons, or combinations of persons who could, in varying circumstances, exercise control, in this case by possessing the greater shareholding. In applying this interpretation to the facts of this case, we concluded that HMRC was correct to consider all of the possible situations in which control was, or could be exercised. For that reason rejected the Appellant's submission that once it was established that B and C had a greater shareholding of EEE, all other alternative combinations for control must be ignored.

30 30. The legislation goes on to provide, at s 416 (3), that where two or more persons together satisfy the conditions of subsection (2) they shall be taken to have control of the company. We agreed with HMRC's interpretation of the legislation as meaning that a minimum controlling combination must disregard any superfluous members and we were satisfied that the legislation had been correctly applied by HMRC.

31. Mr Wells submitted that HMRC had failed to follow its own guidance in respect of the minimum controlling combination of EEE by including superfluous participants. We rejected this submission; the alternatives proposed as minimum controlling combinations (other than B and C) are A, B and D and A, C and D. A and D each own 17% of the shareholding in EEE. We accepted that without either the remaining groups would not possess a greater shareholding and therefore neither A nor D could be described as superfluous.

32. We also accepted that HMRC had followed the guidance set out in CTM 60250, which clarified that *“the “minimum” controlling combination...does not mean you have to establish the smallest controlling combination...”* However we should note that we found HMRC’s guidance only served to confuse matters in this case.

33. We were satisfied that the test to be applied in determining the issue of “control” is set out in the legislation and for the reasons set out above we concluded that the Appellant and EEE are associated and the appeal must therefore be dismissed.

34. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to “Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)” which accompanies and forms part of this decision notice.

J. BLEWITT
TRIBUNAL JUDGE

RELEASE DATE: 22 January 2014