Capital allowances- HMRC's overly restrictive approach rejected

In this article I will explore two First-tier Tribunal decisions that found specialist buildings/structures operated as single units within the trade of farming and were found to be plant in their entirety.

The recently released First-tier Tribunal decision in the case of *JRO Griffiths Ltd* ([2021] UKFTT 257 (TC)) builds on the decision of *May & Anor* ([2019] UKFTT 0032 (TC)) in clarifying how the exclusions at List C of CAA01/s23 from the s21/22 exclusions (buildings and structures respectively) operate in practice. All legislative references in this article are to the Capital Allowances Act 2001 unless stated otherwise. It should be borne in mind that it is possible that the *Griffiths* decision will be appealed by HMRC.

Both cases, which demonstrated clear similarities in terms of the asset type and points at issue, were argued up to the litigation stage by the Croner Taxwise consultancy team and at litigation by Charles Bradley of Pump Court Tax Chambers.

As a brief summary, in *May* a grain store that performed the function of drying and maintaining the condition of the crop between harvest and sale was found to be plant as it fell within the List C exclusion at item 28 in respect of 'silos provided for temporary storage'. In the *Griffiths* case a rather more sophisticated (and consequently expensive) potato store that performed a broadly similar function was also found to fall within this silo exclusion. The potato store was additionally found to fall within the List C 'cold store' exclusion at item 18.

That both units were either buildings or structures and so subject the general restrictions at CAA01/s21 and s22 was common ground between the parties. Whilst it was not specifically found in *Griffiths* whether the potato store was a building or a structure, the judgement in *May* referred to the grain store as a building and both decisions noted that to a casual observer they would appear externally to be general barns or warehouses. I will refer to these units as buildings, which was the HMRC view for both cases and which I consider to be the correct classification.

Both buildings went beyond simply providing the setting or premises in which the trade took place due to their active and managed function of preserving their respective crops in peak condition for far longer than would be possible using traditional store designs, and this was evidenced to the satisfaction of the Tribunal. Whilst in both cases HMRC sought to argue that they were no more than the premises within which the trade took place, this was in my view never a strong argument and this is not the primary feature of this article. I would however mention that even if a building or structure does fall within the List C exclusions from the s21/22 exclusions, it must still perform the function of plant within the trade to create an entitlement to capital allowances.

The key issue in both cases was the interpretation of the relevant List C exclusions and these will now be examined in more detail.

The 'silo' argument

> *S23(4) List C*
>
> *28. The provision of-*
>
> *(a) silos provided for temporary storage*

It was common ground that that the term 'silos provided for temporary storage' List C entry was not defined by legislation and so took its ordinary everyday meaning. At both hearings we relied on the

Shorter Oxford English Dictionary (OED) definition as representing the 'gold standard' and this found favour with both tribunals.

In respect of a silo, the relevant OED definition is as follows:

> *'A pit or underground chamber used for storing grain, roots, etc; spec. one in which green crops are compressed and preserved for fodder as silage. Also, a cylindrical tower or other structure built above ground for the same purpose'*

In both cases HMRC argued that the buildings did not fall within this definition of a silo and in *Griffiths* they also made the point that no building had ever been found to perform the function of plant. As *Griffiths* was heard quite some time after the release of the decision in *May*, which HMRC decided not to appeal, this is incorrect but would align with the view expressed in the current published HMRC guidance at CA22050. This guidance currently remains unchanged and takes no account of, and makes no reference to, the *May* decision.

A key area of dispute common to both cases arose when HMRC sought to justify their position by further restricting the ordinary definition to align with the caselaw they considered, apparently incorrectly, to underpin it. When arguing this HMRC had *Schofield v Hall* ([1975] 49 TC 538), the only other tax case related to silos, in mind.

The *Schofield* case, which concerned a dockside grain silo used to temporarily store grain unloaded from ships and then distribute it to into lorries for onward transport, clearly also underpins the following extract from CA22050 setting out when HMRC consider a silo can qualify for allowances:

> *Treat a grain silo as plant where, together with its attendant machinery, it performs a function in distributing the grain so that [it] acts as a transit silo rather than a warehouse.*

HMRC argued, without evidence, that the List C entry existed to align a silo with the *Schofield* decision and should be interpreted in this light. It is worth mentioning that whilst HMRC guidance does not have the force of law HMRC officers are expected to follow it, which made eventual litigation of both these cases inevitable unless we could convince HMRC to change their position. Whether this should have been the case for *Griffiths* in light of the unappealed *May* decision is however debatable.

At the hearings for both cases Charles pointed out that *Schofield* was not helpful as it did not seek to define either 'silo' or 'temporary storage' as these terms were accepted by all involved parties as correct and so were not explored at the hearing, which focused solely on whether the silo performed the function of plant. In view of this and as there is no other caselaw covering this area, it followed that the ordinary meanings of the terms were the only relevant factor.

The HMRC attempts at definition restriction to their preferred basis were rejected by the Tribunal, who adopted the (to my mind self-evident) view that if a piece of legislation says something then that is what it means. The tribunal also rejected rather mangled HMRC arguments in *Griffiths* to exclude potatoes from the type of crop suitable to be stored in a silo.

In both cases the buildings were found to be structures constructed above ground for the purposes of storing appropriate crops and so met the ordinary definition of a silo.

On the 'temporary storage' issue, in the case of *May* the following Shorter OED definition of 'temporary' was found to be of assistance:

'Lasting or meant to last for a limited time only; not permanent; made or arranged to supply a passing need.'

Both decisions rejected HMRC attempts to align the List C meaning with the 7 day period in *Schofield* and in *Griffiths* it was pointed out that if Parliament had intended this result it could have done so with appropriate legislative wording without difficulty.

Again, in both cases it was found that the buildings were used for temporary storage and so, having met both criteria, fell within the relevant List C exclusion.

Before I move on to cover the cold store point, I would like to address the obvious question that arises from the narrative so far. Why, in view of the numerous and clear similarities between the two cases, did HMRC not appeal the *May* decision on a point of law but instead proceeded to litigate *Griffiths* with a re-hash of arguments it had run and failed with in *May*?

The simple answer is 'I don't know', but a possible reason is that it for the Upper Tribunal to overturn a finding of fact it would need to conclude not that it disagreed with the conclusion the lower tribunal reached but that that conclusion was not one that was open to it to arrive at based on the facts.

The reason HMRC decided to litigate *Griffiths* as if *May* did not exist is, however, beyond me to explain.

This was a point addressed in *Griffiths* by Charles who, not surprisingly, referenced the *May* decision at some length in his arguments. His position was that it was not open to HMRC to fail to appeal a point of law then simply seek to re-run the same arguments again on a case that effectively sits on all fours with the earlier decision. He argued that the judge should follow the *May* decision as a matter of judicial comity (which means 'courtesy', I looked it up at the time) and in support of this he referenced the case of *Patel & others v RCC ([2019] UKFTT 620 (TC)) para 27.*

HMRC simply argued that *May* was decided on its facts and a First-tier Tribunal decision did not set precedent.

The judge, whilst accepting Charles's argument and quoting the relevant *Patel* paragraph in his decision whilst referencing the assistance he took from the *May* case, went on to say that even without this assistance he would still have found that the potato store would have qualified for capital allowances.

It follows that even where a case doesn't set precedent there is a good argument that the principles established should be followed by later judges as a matter of courtesy unless they actually consider the original decision to be wrong. I realise that this could well be a double edged sword, but it is interesting all the same.

The 'cold store' argument

S23(4) List C

18. Cold stores

Again, there is no legislative definition of a cold store and it takes its ordinary meaning but no specific OED definition of this term could be located so we submitted the following alternatives for consideration:

"a building or room which is artificially cooled so that food can be preserved in it" (Collins)

"a refrigerated compartment or building for keeping foods, furs, etc., in cold storage" (Dictionary.com)

"a building for cold storage" (Merriam-Webster).

When in use, the potato store would maintain a constant internal temperature of between 6.5-11.5 degrees Celsius and the appropriate temperature was determined by the requirements of the particular potato variety stored. This was all accepted by HMRC.

HMRC to a degree conflated cold stores with refrigerated units in their arguments but it was understood by all parties that the artificial cooling in the potato store was achieved by air circulation monitored and controlled by a computerised system, rather than by mechanical refrigeration.

Our position was that there is no requirement for a cold store to be mechanically refrigerated (which to my mind was clear from the existence of a separate List C entry at 9 in respect of "refrigeration or cooling equipment") although the store walls did act as a radiator to extract and disperse heat from the stored crop.

We argued that what a 'cold store' was fell to be measured by reference to the condition the crop was maintained in comparison to its condition if not artificially cooled alongside the temperature it operated at. We argued that a temperature range of 6.5-11.5 degrees Celsius was suitably cold, thus the ordinary definition of a cold store was met.

HMRC argued that a cold store must be objectively cold and that this was not satisfied by the temperature ranges present here. In addition they argued that, whilst it didn't always have to maintain a temperature colder than the ambient external temperature, if it is not usually colder than the external temperature it is not operating as a cold store. They further argued that as there were doubts as to whether this design would operate as a cold store if sited elsewhere in, presumably warmer, parts of the world it was not a cold store.

The Tribunal found that the temperature ranges were sufficiently cold for the building to be considered a cold store, that mechanical refrigeration was not required and that it was irrelevant that the design wouldn't work in other parts of the world.

The potato store therefore operated as a cold store

Other helpful relevant factors

In both cases the Croner Consultancy team and, subsequently and as part of the litigation process, the Tribunal, undertook guided site visits to properly understand the building design and function. Our site visit allowed us to understand the process and function of the buildings and for arguments to be tested and explored in detail outside of the litigation process, preparing a solid base for our position.

Another factor present in both cases was strong witness evidence, from an experienced arable farming consultant in the case of *May* and a well-informed senior working director in *Griffiths,* which was supported by appropriate published third party material, both academic and practical. Both tribunals found this evidence helpful and referenced it at some length.

One general point that came up in *Griffiths* is worth a specific mention here. In their closing arguments HMRC sought to contradict elements of evidence given by the witness having failed to challenge him on these in cross examination. Charles pointed out that it is not permissible to do this, and I must admit this was not something either I or, presumably, the HMRC litigator knew. As I have

on occasion litigated cases without counsel assistance, this is something I will bear in mind for the future.

In both *May* and *Griffiths* it was clear that the level of expenditure incurred was far in excess of the costs of construction of a 'normal' building of a similar size and the impact of the expenditure on product quality, and by extension profitability, was explored. It does appear that, whilst this is not directly related to the points at issue, this was seen by the Tribunal as a relevant consideration.

The apparent contradiction here is clear- whilst HMRC are happy to tax the higher profits generated by the investment in the specialist buildings that help generate them, they remain unwilling to relieve the expenditure incurred in generating these additional profits.

In my opinion this stance is due to the commonly held (but as far as I know informal) HMRC view that the List C exclusions represent the definitive list of what can escape the s21/22 exclusions and any attempt to broaden the scope of these beyond the HMRC view of how they operate must be litigated (at face value, apparently more than once) if relief is to be obtained.

Will HMRC appeal *Griffiths*?

To my mind any HMRC request to appeal in respect of *Griffiths* on the 'silo' point would be difficult as the judgement, which is clear and comprehensive, correctly lists and reviews all the evidence and arguments presented, so making the finding of fact arrived at by the judge one that was reasonably open to him to reach. The earlier failure to appeal the *May* case will also present another hurdle to this, and it should be remembered that our arguments have now prevailed on first principles in front of two separate First-tier Tribunals.

On the 'cold store' aspect, there is no prior decided case that might impact any appeal but the above comments regarding the judgement apply equally to this point. A further consideration is that unless there are serious HMRC concerns around this particular element of the decision it would serve no operational purpose to appeal it in isolation as the claim also succeeded on the silo point.

That said, the decision as to whether to seek leave to appeal sits with HMRC and we will have to wait until mid-September to know for sure whether an application to appeal will be forthcoming.

Summary

In brief the following checklist may be helpful when preparing a capital allowance claim that may not align with the HMRC view of what is admissible under the relevant legislation:

- Undertake a site visit and discuss the issue with the person who may ultimately be a witness should litigation be required.
- Do your homework- background research is always helpful and may produce useable material.
- Are the costs incurred in excess of those for a general building/structure of a similar size? If so, can this be evidenced?
- Review 'year on year' profits- has the client's turnover and/or profit increased following incurring the expenditure?
- Make sure there is a good basis to argue the established plant tests are met.
- Be prepared to dig in- HMRC can't always be relied upon to be reasonable, especially if the case may involve broadening the scope of the List C exclusions.

- If the claim does not align with the HMRC view of the position a 'white space' entry on the relevant tax return to this effect, provided it is clear, should restrict HMRC from making a discovery at a later date if the claim enquiry window is missed for whatever reason.

Other considerations

There are undoubtably other areas where the HMRC position is contentious and untested, for example the circumstances in which relief is available in respect of polytunnels (or indeed what constitutes a 'fixed structure' for the purposes of s22(3)(a) more generally, which has potential application beyond farming). The above cases demonstrate that it is far from a foregone conclusion that the HMRC view will prevail.

In addition there are potential tax planning issues to consider- the current £1M Annual Investment Allowance ceiling and (for corporate entities) the possibility of claiming enhanced allowance under the temporary superdeduction regime shouldn't be overlooked and potentially offer far more attractive relief routes than that offered by, for example, the Structures and Buildings Allowance.

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