



Neutral Citation: [2022] UKFTT 00158 (TC)

Case Number: TC08485

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

By remote video hearing

Appeal reference: TC/2020/01434

*Capital gains tax- entrepreneurs' relief – whether commenced trading – whether discharged
burden of proof – no - appeal dismissed*

Heard on: 11 February 2022
Judgment date: 08 May 2022

Before

TRIBUNAL JUDGE IAN HYDE

Between

JOHN DOUGLAS WARDLE

Appellant

and

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: the appellant appeared in person

For the Respondents: Mr M Simpson litigator of HM Revenue and Customs' Solicitor's
Office

DECISION

INTRODUCTION

1. The form of the hearing was by video on the Tribunal video system. The documents to which I was referred are an authorities bundle, trial bundle and supplemental bundle being in total 667 pages.
2. Prior notice of the hearing had been published on the gov.uk website, with information about how representatives of the media or members of the public could apply to join the hearing remotely in order to observe the proceedings. As such, the hearing was held in public.
3. This appeal concerns the availability of entrepreneurs' relief to reduce the rate of capital gains tax payable by the appellant in respect of his disposal of interests in Biomass UK No.1 LLP ("the LLP"), a limited liability partnership established for the purpose of building and operating a waste-to-energy plant.
4. References to sections are to sections in the Taxation of Chargeable Gains Act 1992 ("TCGA") unless stated otherwise.

THE FACTS

5. In addition to the bundles, the appellant provided a witness statement and gave oral evidence. I found the appellant to be an honest and credible witness.
6. There was also produced a witness statement from a Mr Richard Frearson, the managing director of Power Consulting (Midlands) Limited, the project manager for the LLP. Mr Pearson did not give evidence at the hearing, but the statement concerned only the service of the notice to proceed under the feedstock agreement and was not challenged by HMRC.
7. The appellant has deliberately disclosed only limited documents potentially relevant to this appeal and has not disclosed, for three reasons. First, he did not want to advertise the profits made. Second, the documents associated with the project were commercially sensitive and subject to confidentiality obligations. Third, there were some 56 documents executed at financial close on the project and it would, in the appellant's view, have been unnecessary to produce all of them as the issues could be illustrated by a single, sample contract. The appellant has therefore only produced one contract, the feedstock agreement and even then, the name of the counterparty and other aspects have been redacted.
8. The central issue in this appeal is the nature of the activities carried out by the LLP and the burden of proof in this appeal is on the appellant to show on the balance of probabilities those activities amounted to trading. The appellant clearly has detailed knowledge of the arrangements but, nevertheless, as I set out further below, with the exception of one contract limited himself to general assertions and so did not substantiate his oral evidence with documents which in my view he could have done. I have found the appellant an honest witness, but the burden of proof in an appeal is a different matter. In complex matters such as the present an appellant cannot assume oral evidence is sufficient.
9. From the documents produced and the appellant's oral evidence I find the facts as set out below.

The facts in outline

10. The appellant is a retired commercial solicitor who, whilst in practice, specialised in advising on energy projects. After leaving private practice the appellant remained involved in investments and developments, including in the renewable energy sector and specifically a project to construct and operate a waste-to-energy plant in Hull.

11. On 12 June 2015 the LLP was established to acquire, construct, and operate a power plant in Hull using wood waste biomass as its fuel or feedstock.
12. On 18 August 2015, the project in Hull was transferred to the LLP and the appellant became the owner of 14.65% of the partnership equity (denoted by 1,465 membership units) in the LLP.
13. On 21 August 2015 (“Financial Close”) the LLP entered into a number of contracts relating to the construction, operation, and financing of the Hull plant, including a contract to purchase feedstock from a supplier (the “Feedstock Agreement”).
14. On 24 August 2015, the LLP issued a “notice to proceed” under the Feedstock Agreement to the relevant supplier.
15. On 14 September 2016, the LLP applied to the Environment Agency for a permit to operate the power plant.
16. On 08 November 2016, the Appellant disposed of 666 of his 1,465 units in the LLP (“the Disposal”).
17. On 10 May 2017, the Environment Agency issued the permit.

The appellant’s tax return

18. The Appellant in his tax return for the year 2016-17 made a claim for entrepreneurs’ relief on the Disposal.
19. On 25 May 2018, HMRC opened an enquiry under section 9A Taxes Management Act 1970 (“TMA”) into the Appellant’s return.
20. On 26 March 2020, HMRC closed their enquiry by way of a notice under section 28A(1B) and (2) TMA rejecting the entrepreneurs’ relief claim.
21. On 27 March 2020, the Appellant appealed the closure notice.
22. Following HMRC’s view of the matter by letter of 31 March 2020, the Appellant appealed to the Tribunal on 07 April 2020.

The LLP’s activities

23. The appellant gave evidence as to the overall purpose of the LLP’s activities.
24. The purpose of LLP’s activities was to generate profits from constructing and operating a power plant burning wood waste. Revenues would be derived from the production and sale of electricity and the sale of Renewable Obligation Certificates (“ROCs”) awarded by Ofgem.
25. ROCs are certificates issued by Ofgem under the Electricity Act 1989 to accredited renewable power generators in respect of net renewable electricity produced. The ROCs are transferable and can be sold to third parties who can use them to satisfy their renewables obligations.
26. The LLP’s financial model was to generate two thirds of its revenue from the sale of ROCs and one third from selling electricity. Obtaining wood waste was necessarily important to both activities. Specifically, the ROCs would not be available were the plant to burn diesel as it had to do from time to time.

Financial close, construction and commissioning of the plant

27. The appellant gave evidence as to the commercial and legal arrangements for the development and operation of the waste to energy plant.
28. On Financial Close on 21 August 2015, some 56 contracts were entered into by the LLP with various parties relating to the construction, operation and financing of the Hull plant. It

was the appellant's evidence that after Financial Close the LLP was committed to the construction and operation of the waste to energy plant. For example, some 25% of the construction price was advanced to the building contractors on Financial Close.

29. On Financial Close the LLP entered into an electricity supply contract with one of the major energy companies. The appellant did not suggest or produced any evidence of commitments or arrangements relating to the sale of ROCs on or prior to 08 November 2016, and I therefore find that there were none.

30. The site of the plant in the docks in Hull was as at Financial Close, a disused industrial site. It would take some two years to build the plant after which the project would enter into a commissioning phase of some 6 months to a year where the contractor would test the plant. During that period feedstock would be burnt and electricity generated but only to test the plant. Once the commissioning process was completed the operator would take over and power generation proper would start.

31. It was the appellant's evidence, that in November 2016 the site was being cleared but no construction had started. The appellant explained that at this point, whilst there was planning permission, the detailed design of the plant was still being worked on.

The Feedstock Agreement

32. The Feedstock Agreement was produced by the appellant and in broad terms provided for the counterparty (the "Supplier") to be required to deliver waste wood and the LLP was obliged to accept it.

33. The wood was supplied for free if the LLP collected it and for £20 a tonne payable by the LLP to the Supplier if delivered by the Supplier, the £20 being intended to cover transport costs.

34. The Feedstock Agreement had benefits for both parties. The LLP obtained the fuel it needed both to generate electricity, and because it was a qualifying biofuel, entitle it to be awarded ROCs which it could sell. If the LLP did not have sufficient waste wood it would have to use diesel, which based on the amount needed to produce the same energy as a tonne of waste wood equated to £270 a tonne. Further, burning diesel prevented the LLP from being issued ROCs.

35. The Supplier benefitted from the Feedstock Agreement because it generated waste wood from its activities and needed to dispose of it. If it did not supply the waste wood to the LLP it would need to pay £140 a tonne to dispose to landfill.

36. I was taken during the hearing to specific provisions in the Feedstock Agreement being in summary as follows:

(1) Clause 2: the obligations in the agreement (save as to confidentiality, dispute resolution and jurisdiction) only became enforceable upon service by the LLP of a notice to proceed

(2) Clause 3.1.1: subject to conditions relating to force majeure, maintenance of the plant and unplanned shutdowns, the LLP was required to take and the Supplier was required to deliver specified minimum levels of feedstock each year.

(3) Clause 3.3.1: the Supplier had priority rights during the term of the contract to supply feedstock to the LLP

(4) Clause 3.6.2: the LLP agreed to indemnify the Supplier in the event it did not take the required amount of feedstock

(5) Clause 7.1: LLP indemnified the Supplier against loss or damage caused by the LLP in connection with carrying out the agreement

(6) Clause 15.1: the contract would last for 20 years after the commencement date. The commencement date was defined as the start of the commissioning period, being as explained by the appellant, the period lasting between 6 months and a year during which the plant was tested before becoming operational.

(7) clause 16.2.11: the contract is terminated in the event that the construction contract and/or boiler supply contract would be terminated and such termination results in the plant not being constructed.

37. The appellant argued that the LLP provided services to the Supplier under the Feedstock Agreement in that it took material that the Supplier would otherwise have to pay some £140 a tonne to dispose of at landfill. I do not accept that interpretation and I find that the LLP does not provide a service to the Supplier. No doubt the Supplier found it useful that the LLP took the waste wood away and committed to do so over 20 years at minimum volumes, but I find that that it is matter of mutual benefit rather than a service. I am reinforced in this conclusion by the drafting of the Feedstock Agreement. Aside from a commitment from the Supplier to take away ash produced by the plant, the contract is couched in terms of the purchase of material by the LLP (described in the agreement as “the Purchaser”) not the provision of a service by the LLP.

Other relevant contracts

38. The appellant did not produce any other contracts in evidence. Thus, I was not shown the following to which the appellant referred either in his skeleton argument or during the hearing:

- (1) The construction contract
- (2) The boiler supply contract
- (3) The electricity contract
- (4) The financing arrangements
- (5) The leasing arrangements

39. There may have been more material contracts and arrangements relevant to understanding the project, but the appellant did not either refer to or produce them.

40. It is central to the appellant’s argument in this appeal that all contracts relevant to the construction and operation of the plant were executed on Financial Close so that the LLP was committed and, provided all contracts were performed, the plant would be built, commissioned, and then operated as a waste-to-energy plant. Further, the commitments by the various parties meant that it was in everyone’s interest that the project would be completed. For example, some 25% of the cost of the construction was advanced on Financial Close.

41. The Feedstock Agreement, for example as set out above it is conditional on the construction and boiler contracts not being terminated, and the appellant argued I can accept that other contracts, such as the electricity contract were subject to identical conditions. The appellant asserted that that was the case but did not produce the contracts. There is no documentary evidence before me, for example, as to the conditions for termination of the construction contract, which would have caused the Feedstock Agreement to be terminated. By way of further example, there was no evidence before the Tribunal as to the nature of the electricity contract save the appellant’s assurance that it was only conditional on terms that were described as “similar” to the Feedstock Agreement. I do not take as read that a contract

with a supplier of surplus wood and a contract with a major energy company are on “similar” terms.

42. As Mr Simpson pointed out during the hearing he has been unable to scrutinise these contracts. I have found the appellant to be honest but the appellant has denied HMRC and the Tribunal the opportunity to consider these contracts, rather than relying on the appellant’s own conclusions. I can therefore make no finding of fact as to the nature of the financial commitments of the LLP and the nature of the above contracts and arrangements.

ENTREPRENEURS’ RELIEF

43. Entrepreneurs’ relief provides for the reduction of the rate of capital gains tax (“CGT”) to 10% on disposals of capital assets provided a number of conditions are satisfied. The relevant legislation is set out in Chapter 3 of Part V Taxation of Chargeable Gains Act 1992 (“TCGA”):

44. Section 169H:

“169H(1) This Chapter provides for a lower rate of capital gains tax in respect of qualifying business disposals (to be known as “entrepreneurs’ relief”).

169H(2) The following are qualifying business disposals–

(a) a material disposal of business assets: see section 169I,

(b) a disposal of trust business assets: see section 169J, and

(c) a disposal associated with a relevant material disposal: see section 169K.

169H(3) But in the case of certain qualifying business disposals, entrepreneurs’ relief is given only in respect of disposals of relevant business assets comprised in the qualifying business disposal: see sections 169L and 169LA.

169H(4) Section 169M makes provision requiring the making of a claim for entrepreneurs’ relief.

169H(5) Sections 169N to 169P make provision as to the amount of entrepreneurs’ relief.

169H(6) Section 169Q and 169R make provision about reorganisations.

169H(7) Sections 169S and 169SA contain interpretative provisions for the purposes of this Chapter.”

45. Section 169I provides insofar as relevant:

“169I(1) There is a material disposal of business assets where–

(a) an individual makes a disposal of business assets (see subsection (2)), and

(b) the disposal of business assets is a material disposal (see subsections (3) to (7)).

(2) For the purposes of this Chapter a disposal of business assets is–

(a) a disposal of the whole or part of a business,

(b) a disposal of (or of interests in) one or more assets in use, at the time at which a business ceases to be carried on, for the purposes of the business, or

(c) a disposal of one or more assets consisting of (or of interests in) shares in or securities of a company.

(3) A disposal within paragraph (a) of subsection (2) is a material disposal if the business is owned by the individual throughout the period of 1 year ending with the date of the disposal.

...

169I(8) For the purposes of this section–

(a) an individual who disposes of (or of interests in) assets used for the purposes of a business carried on by the individual on entering into a partnership which is to carry on the business is to be treated as disposing of a part of the business,

(b) the disposal by an individual of the whole or part of the individual's interest in the assets of a partnership is to be treated as a disposal by the individual of the whole or part of the business carried on by the partnership, and

(c) at any time when a business is carried on by a partnership, the business is to be treated as owned by each individual who is at that time a member of the partnership.”

18. Section 169S provides:

“169S(1) For the purposes of this Chapter “a business” means anything which

–

(a) is a trade, profession or vocation, and

(b) is conducted on a commercial basis and with a view to the realisation of profits.

169S(5) In this Chapter –

‘trade’ has the same meaning as in the Income Tax Acts (see section 989 of ITA 2007)”

46. Section 989 Income Taxes Act 2007 (“ITA”) provides that:

“‘trade’ includes any venture in the nature of trade,”

THE PARTIES ARGUMENTS

the issue

47. The issue in this appeal is whether the disposal by the appellant of the units in the LLP constituted a material disposal of business assets under section 169I(1).

48. For this purpose, a member an LLP is deemed to own part of the business of the LLP (s169I(8)(c)).

49. It is agreed that as at the date of the Disposal the appellant had owned the units sold throughout the period of one year ending with the date of the Disposal (s169I(3)).

50. “Business” is defined by section 169S(1) and in this context may be summarised as follows:

“a trade...conducted on a commercial basis and with a view to the realisation of profits.”

51. Section 989 ITA extends the meaning of “trade”:

“‘trade’ includes any venture in the nature of trade,”

52. For entrepreneurs’ relief to be available it is necessary for the LLP to be trading for the period of 1 year ending with the date of disposal (the period 9 November 2015 - 8 November 2016).

53. It was agreed between the parties that the nature of LLP’s activities did not change during the period from Financial Close on 24 August 2015 until the Disposal on 8 November 2016. The issue could therefore be rephrased - and the parties argued before me on this basis – as to whether the net result of Financial Close was from that point carrying on venture on the nature of a trade.

the appellant's arguments

54. Following his earlier appeal to the Tribunal in respect of a different disposal (*Wardle v HMRC* TC/2019/06727), the appellant accepted that for there to be “a business” within s169S(1), the LLP must have commenced trading.

55. The appellant argued in this appeal that since 24 August 2015 and up to the date of the Disposal the LLP was a trading on a commercial basis with a view to a profit, so satisfying the definition of a business in section 169S(1).

56. The appellant characterised the LLP's business not simply as a generator of electricity but as the construction and operation of the plant as a waste-to-energy business, procuring waste wood and then converting it into electricity with the LLP's principal revenue streams being the sale of electricity as a by-product of processing waste wood and obtaining and selling ROCs.

57. It was a necessary part of that business that the LLP procured long-term supplies of waste wood and to do so long in advance of the first electricity being generated. This was achieved through the Feedstock Agreement with both parties accepting contractual obligations for the sourcing and supply of the waste wood and liabilities for failure to supply and to accept such waste wood. Such obligations became effective from Financial Close on 24 August 2015 and the issue of the notice to proceed following which the parties commenced the implementation of the contract.

58. The appellant's trade therefore started on 24 August 2015 that this was being done commercially and with a view to realising profits.

59. The appellant relied on *Wardle* but accepted it had only limited applicability to the current appeal. Specifically, the appellant relied upon the interpretation of section 169S(1) by Judge Zaman in her decision at paragraphs 98 and 100:

98. I consider that the “natural and ordinary” meaning of the definition of “a business” in s169S(1) is that it requires that an individual or partnership making the disposal is disposing of **something (or anything) that is, at that time, a trade and is conducted, at that time, on a commercial basis. The trade must exist at that time – it does not extend to activities which are capable of being conducted as a trade at a point in the future.** I have tested this by reference to the various submissions before me, and borne in mind the relevant principles of statutory interpretation...

100. Having regard to all of the submissions, I have concluded that the words chosen by Parliament in s169S(1) require that a disposal by a partnership only constitutes a disposal of the whole or part of a business **if the partnership has commenced trading.** Therefore, the disposals by the Partnership were not a material disposal of business assets and do not qualify for entrepreneurs' relief.” (*appellant's emphasis added*)

60. The appellant relied more extensively on the decision of Special Commissioner Hellier sitting as a Special Commissioner in *Mansell v R&C Commrs* [2006] Sp C551:

“88. Section 218 speaks of a trade ‘set up and commenced’ before, or on or after, 6 April 1994. The words ‘set up’ suggest that a trade can be set up without being commenced. This echoes the distinction drawn in *Slater* (see paragraph 72 above), the distinction between getting ready and commencing in *Birmingham Cattle*, Lord Millett's observation that ‘the work of finding, acquiring and fitting out a shop or restaurant begins long before the premises are open for business and the first customer walks through the door’, and the assembly of a ‘sufficient organisational structure’ to undertake the essential

preliminaries noted in *Gartry*. I conclude that a trade cannot commence until it has been set up (to the extent it needs to be set up), and that acts of setting up are not commencing or carrying on the trade. Setting up trade will include setting up a business structure to undertake the essential preliminaries, getting ready to face your customers, purchasing plant, and organising the decision-making structures, the management, and the financing. Depending on the trade more or less than this may be required before it is set up.

89. Although none of the cases cited to me dealt directly with the question of when a trade commences, those cases suggest to me the following principles. First before the trade can be said to commence, there must be a fairly specific concept of the type of activity to be carried on.

90. Second: an activity which consists merely of a review of the possibilities in the expectation or hope that information will be obtained to justify going into a business of some kind is not the carrying on of a trade.

91. **Third: is not always necessary that a sale is made or a service supplied before a trade can be said to be commenced.** It is tempting to say that a trade commences only when the first sale is made. In normal everyday usage one would say that a person starts trading when he becomes entitled to money from his first customer. **But, for the following reasons, it does not seem to me that making the first sale is necessarily the earliest time when a ‘trade is ... commenced’ for the purposes of section 218:**

(a) there is a small but fine distinction between ‘trading starting’ and a trade being commenced, which may make everyday usage a pilot slightly out of its home waters;

(b) **the comments made by Lord Millett in *Khan v Miah* tend to suggest that selling the first meal is not the earliest time when trading starts;** and

(c) for these purposes the extended definition of trade affects the question. The question becomes: when did the trade, manufacture, adventure or concern in the nature of trade start? In normal usage an adventure in trade might start before the ‘trading’ started. An adventure normally starts when the adventurer leaves home, or the merchant first charts his ship rather than when the first monster is killed or the cargo is brought back home and sold.

92. I note that it is possible that for the linguistic reasons noted in paragraph (c) above, there may be somewhat different considerations relevant to when a trade such as buying and selling flowers commences from those relevant to when an adventure or concern in the nature of a trade may commence.

93. **It seems to me that a trade commences when the taxpayer, having a specific idea in mind of his intended profit making activities, and having set up his business, begins operational activities – and by operational activities I mean dealings with third parties immediately and directly related to the supplies to be made which it is hoped will give rise to the expected profits, and which involve the trader putting money at risk: the acquisition of the goods to sell or to turn into items to be sold, the provision of services, or the entering into a contract to provide goods or services: the kind of activities which contribute to the gross (rather than the net) profit of the enterprise. The restaurant which has bought food which is in its kitchen and opens its doors, the speculator who contracts to sell what he has not bought, the service provider who has started to provide services under an agreement so to do, have all engaged in operational activities in which they have incurred a financial risk, and I would say that all have started to trade.**

94. It does not seem to me that carrying on negotiations to enter into the contracts which, when formed, will constitute operational activity is sufficient. At that stage no operational risk has been undertaken: no obligation has been assumed which directly relates to the supplies to be made. **Not until those negotiations culminate in such obligations or assets, and give rise to a real possibility of loss or gain has an operational activity taken place.** Until then, those negotiations may be part of setting up the trade but they do not to my mind betoken its commencement.

Conclusions

95. It seems to me that Lord Millet's statement that 'it is necessary to identify the venture in order to decide whether the parties have actually embarked upon it, but it is not necessary to attach any particular name to it' is equally applicable to the question as to whether a person has commenced a trade. But it is necessary that there be a fairly specific concept of the type of activity in the mind of the putative trader which is to be carried on, although it does not have to be given, or be capable of being given a simple name." [appellant's emphasis added]

61. The appellant argued that the decision in *Mansell* contradicts HMRC's argument based on *Birmingham & District Cattle By-Products Co. Ltd v IR Commrs* (1919) 12 TC 921, that the LLP must have sold electricity before it can have commenced trade.

62. The appellant also had more general criticisms of the decision in *Birmingham & District Cattle*. The decision was over 100 years old and based on a different statutory regime.

63. *Mansell* had also been endorsed by Henderson J in the High Court in *Tower MCashback LLP v HMRC* [2008] STC 3366:

"94....In a valuable discussion in paragraphs 88 and following of his decision, Mr Hellier referred to the fitful guidance to be obtained from earlier authorities (none of which deals directly with the question when a trade commences), and concluded that in his view a trade commences "when the taxpayer, having a specific idea in mind of his intended profit making activities, and having set up his business, begins operational activities". He went on to say that by operational activities he meant dealings with third parties immediately and directly related to the supplies to be made which it is hoped will give rise to the expected profits, and which involve the trader putting money at risk.

95. It is unnecessary for me to say whether I would have reached the same conclusion on the facts as Mr Hellier did in *Mansell*, but in broad terms I find his test of the beginning of operational activities a useful one. Every case will turn on its own facts, but in general the test presupposes that the framework or structure for the trade will have to be set up or established before any operational activity can begin..."

64. The appellant argued *Mansell* was directly applicable and it is not necessary that a sale is made or a service supplied before a trade has commenced provided:

- (1) dealings with third parties immediately and directly related to the supplies to be made have been concluded;
- (2) such dealings result in the trader assuming a financial risk; and
- (3) such dealings can be hoped to give rise to planned profits.

65. The appellant argued that the setting up of the LLP's business was concluded following Financial Close on 21 August 2015. By that date:

- (1) the specific concept of the Plant as a waste-to-energy facility had been defined within a business structure, both corporate and contractual;
- (2) the Plant's customers (both those wishing to have their waste wood processed and those wishing to purchase electricity) had been identified and related contracts had been entered into;
- (3) the contracts for the purchase of the plant and machinery had been entered into;
- (4) the decision making structures and procedures had been established;
- (5) the management team had been appointed;
- (6) the financing had been arranged.

66. The LLP's trade commenced when notices to proceed were issued on 24 August 2015. Entering into the Feedstock Agreement and giving the notice to proceed amounted to dealing with a third party customer for the disposal of waste wood it had contracted to supply, the processing of which the LLP expected would give rise to revenues and profits. The same was also true of the contract with the energy company for the supply of electricity.

67. In addition to the significant outlay of cash on the plant by the LLP which started at Financial Close, the contractual arrangements involved the LLP accepting contractual obligations and liabilities, thereby putting money at risk. The Feedstock Agreement gave rise to the real possibility of loss or gain of an operational nature including the indemnities in clauses 7.1 and 24 becoming operative. Trading had, on the above principles, commenced.

68. To the extent the contracts were conditional, thus the Feedstock Agreement was conditional on the construction of the plant, this was not a bar to trading. In *Michael Hunt v HMRC* [2019] UKFTT 0515, Judge Brooks quoted *Mansell* with approval and adopted Special Commissioner Hellier's approach in paragraph 93 of that decision. The Tribunal found the relevant business was trading notwithstanding at the time it did not have a licence to do so and that licence was a condition precedent in the relevant contracts:

“80. Although, because it did not hold an Operating Licences from the Gambling Commission, the condition precedent in the contracts with the CICs was not met, Altala nevertheless not only entered into agreements with the CICs to provide services but, as described above, created the infrastructure for a lottery and entered into dealings with third parties as required by that agreement, eg by making arrangements for the sale of tickets, procuring the equipment required to make the draw and making agreements with “an appropriate broadcaster and production company”. In doing so Altala incurred substantial expenditure and clearly put its money at risk in the hope that it would give rise to profits.

81. Having regard to all the circumstances case, I consider that Altala did engage in operational activities in which it incurred a financial risk. As is clear from *Mansell*, this is sufficient for it to have commenced trading. It therefore follows that Mr Hunt is entitled to the relief claimed under s 253(4) TCGA.”

HMRC's arguments

69. Mr Simpson's starting point was that the activities in this appeal should be seen as fundamentally a manufacturing trade. Unless electricity is generated there will be no income from the sale of either electricity or ROCs. The LLP did not provide a service in taking the waste wood from the supplier.

70. Mr Simpson relied for the meaning of “trade” on the decision of the House of Lords in *Ransom v Higgs* [1974] 50TC1, an avoidance case in which HMRC sought to argue the taxpayer was trading. Lord Reid said at page 78I:

‘As an ordinary word in the English language “trade” has or has had a variety of meanings or shades of meaning. Leaving aside obsolete or rare usage, it is sometimes used to denote any mercantile operation, but it is commonly used to denote operations of a commercial character by which the trader provides to customers for reward some kind of goods or services. The contexts in which the word “trade” has been used in the Income Tax Acts appear to me to indicate that operations of that kind are what the legislature had primarily in mind.’

71. Lord Morris at page 84H said:

‘To be engaged in trade or in an adventure in the nature of trade surely a person must do something, and if trading he must trade with some one’.

72. Lord Wilberforce at page 88E said:

“Trade” cannot be precisely defined, but certain characteristics can be identified which trade normally has. Equally some indicia can be found which prevent a profit from being regarded as the profit of a trade. Sometimes the question whether an activity is to be found to be a trade becomes a matter of degree, of frequency, of organisation, even of intention, and in such cases it is for the fact-finding body to decide on the evidence whether a line is passed... Trade involves, normally, the exchange of goods or of services for reward-not of all services, since some qualify as a profession or employment or vocation, but there must be something which the trade offers to provide by way of business. Trade, moreover, presupposes a customer (to this too there may be exceptions, but such is the norm), or, as it may be expressed, trade must be bilateral-you must trade with someone. ... Then there are elements or characteristics which prevent a trade being found even though a profit has been made-the realisation of a capital asset, the isolated transaction (which may yet be a trade)’.

73. A trade is therefore carried on where the production and sale of goods or the performance of services is carried on habitually and with a view to profit. Further, it assumes trading with a third party.

74. Mr Simpson argued that *The Birmingham & District Cattle By-products Co Ltd v CIR* [1919] 12TC92. 31 set out the relevant test for the commencement of a manufacturing trade:

“It seems to me that it is really very clear. The question is when the company commenced its trade or business. It has been treated as commencing its trade or business in October, 1913, when, according to its Minutes, it said it did, but I do not in the least hold it bound by those Minutes for this purpose; I want to look at the substance of the matter. It is set forth that they really commenced in June, or, at any rate, some time before August, 1913, to carry on the trade or business. Now apparently the company was incorporated on the 20th June to carry on the business of making some use of the by-products of the butcher’s trade. It arose out of a combination of a number of butchers who entered into a contract with the trustee of the company to be formed that they would supply, and the company to be formed would take, these by-products. There was a combination among those butchers for that purpose. Now the company took over those agreements, and having taken over those agreements the directors, at the expense of the company, as was very proper, went about and looked at places of business of a similar character in various parts of the country. That was an admirable thing to do preparatory to commencing

business, but it certainly was not commencing business. If you go and look at other businesses to see how you will conduct your business when you set it up, you are preparing to commence business, but you are not commencing business.

Then they entered into a contract for the erection of works, which works were duly erected in July, 1913. That again is preparatory. The company were occupying themselves with activities within their powers, of course; they were living their life; but they had not yet begun to conduct their trade or business. Then they purchased machinery and plant for carrying on the business. That was getting ready. Then they entered into agreements for the purchase of products. Those are the agreements which I have already referred to which formed the substratum of the company, but no materials came in nor were any sausage skins made from the 20th June. They waited, and I suppose in October, the date they refer to in their Minutes, having looked round, and having got their machinery and plant, and having also employed their foreman, and having got their works erected and generally got everything ready, then they began to take the raw materials and to turn out their product

I am bound to say that I think the case is extremely clear, and the Commissioners have taken the view that they had not commenced business till then, and I do not see the slightest sign of any error in law in the Commissioners having taken that view. It seems to me it is the only view, both in law and in fact, if I may say so, that they could take, and, therefore, I must dismiss this appeal with costs”

75. In short, the test in *Birmingham & District Cattle* amounts to whether, having carried out the preparatory works, the business has bought raw materials and is producing goods. This test is to be preferred to the test in *Mansell* because:

- (1) The decision in *Birmingham Cattle* is from a higher court than *Mansell* and is binding on this Tribunal whereas *Mansell*, being the equivalent of the Tribunal is not.
- (2) *Birmingham Cattle* provides a more certain test than *Mansell*. Trade simply commences when “they began to take the raw materials and to turn out their product”.
- (3) *Mansell* may be of use where the trade does not have as clear a start date as the manufacturing of product, for example if the trade is a supply of services.

76. Further, *Birmingham & District Cattle* and *Mansell* are not in conflict. In *Birmingham & District Cattle* the following activities were not trading but rather were preparing to trade:

- (a) viewing other places of business of a similar character in other parts of the country.
- (b) entering into a contract for the building of a factory, and having that factory built.
- (c) purchasing machinery and plant for carrying on the business.
- (d) entering into agreements for the purchase of products to be used in the business and for the sale of finished products, and
- (e) engaging a foreman of works.

77. These activities were not the “operational activities” *Mansell* said indicated that trading had begun.

78. Further, even if the Tribunal prefers *Mansell*, on the tests set out in *Mansell* the LLP did not commence trading prior to the Disposal.

79. In *Mansell* Special Commissioner Hellier set out at paragraph 93 two conditions for an activity to be an operational activity and so trading:

“It seems to me that a trade commences when the taxpayer, having a specific idea in mind of his intended profit making activities, and having set up his business, begins operational activities – and by operational activities I mean dealings with third parties immediately and directly related to the supplies to be made which it is hoped will give rise to the expected profits, and which involve the trader putting money at risk....”

80. Firstly, it must be “dealings with third parties immediately and directly related to the supplies to be made which it is hoped will give rise to the expected profits” and secondly “which involve the trader putting money at risk”.

81. In respect of the “money at risk” condition, the obligation to purchase feedstock under the Feedstock Agreement did not begin until the “Commencement Date”, the Commencement Date being the date the construction contractor first needed the feedstock to begin testing the plant. There was no current obligation to purchase feedstock, only a future obligation.

82. Furthermore, the Feedstock Agreement at clause 16.2.11 provided for termination of the agreement in the event that the construction contract and/or boiler contract is terminated and the plan not constructed.

83. The future obligation to take feedstock was therefore conditional on the plant being built, failing which the LLP would have no obligation to purchase feedstock under this agreement. The money at risk condition in *Mansell* is not satisfied by the Feedstock Agreement.

84. The list of examples in paragraph 93 of *Mansell*, whilst not exhaustive, does not include the entering into of a contract to acquire goods to turn into items to be sold. This is because the entering into of such a contract is too removed from the supplies to be made to be “immediately and directly related to the supplies to be made”. Accordingly, even if the LLP did have a binding obligation for purchasing feedstock such that there was money at risk, the entering into an agreement creating that obligation would not be an operational activity because it is too far removed to be immediately and directly related to the supplies to be made.

DISCUSSION

85. The issue in this appeal is whether LLP has been trading for one year prior to the date of the Disposal, on 8 November 2016. In effect, as its activities did not change from Financial Close, then the question is whether the LLP commenced trading on 24 August 2015.

86. The short test of trading is supplying goods or services to a customer, for example set out, for example Lord Morris in *Ransom v Higgs* at page 84H:

‘To be engaged in trade or in an adventure in the nature of trade surely a person must do something, and if trading he must trade with some one’.

87. However, the appellant does not satisfy that test in the current circumstances. A substantial part of the energies of both parties in this appeal was therefore whether the appellant was entitled to take a broader definition of trade as set out in *Mansell*. HMRC preferred the test in *Birmingham & District Cattle*. The tests as set out in the two cases are difficult to reconcile, specifically applying the test in *Mansell* to the facts of *Birmingham & District Cattle* does not obviously come to the same conclusion as was found in *Birmingham & District Cattle*.

88. Whether or not a trade has commenced will depend on a consideration of all the individual facts and it is in my view inappropriate to apply the short reasoning in *Birmingham & District Cattle* to all circumstances. I do not accept HMRC’s argument that because it is a simpler the test *Birmingham & District Cattle* is necessarily to be preferred. In my view the

well-articulated and clear summary of the issues as set out in *Mansell* at [88] to [95] represents a better summary of the factors to take into account, at least in the current appeal. Henderson J in *Tower M Cashback* found the “operational activities” test in *Mansell* “useful” and in *Hunt* both HMRC and the appellant agreed that the relevant test was as set out in *Mansell*.

89. There is no doubt a danger in a rigid application but the facts in this appeal are unusual, specifically the embryonic nature of the business, subsisting as at Financial Close only in contractual rights and obligations. In these circumstances I find Special Commissioner Hellier's exposition of the principles to be applied to be the most useful guide as to whether the LLP was trading at Financial Close:

“93. It seems to me that a trade commences when the taxpayer, having a specific idea in mind of his intended profit making activities, and having set up his business, begins operational activities – and by operational activities I mean dealings with third parties immediately and directly related to the supplies to be made which it is hoped will give rise to the expected profits, and which involve the trader putting money at risk: the acquisition of the goods to sell or to turn into items to be sold, the provision of services, or the entering into a contract to provide goods or services: the kind of activities which contribute to the gross (rather than the net) profit of the enterprise. The restaurant which has bought food which is in its kitchen and opens its doors, the speculator who contracts to sell what he has not bought, the service provider who has started to provide services under an agreement so to do, have all engaged in operational activities in which they have incurred a financial risk, and I would say that all have started to trade.”

90. The first limb of Special Commissioner Hellier's principles is to look at whether the taxpayer has "a specific idea in mind of his intended profit making activities. I find that the LLP has done so here.

91. The second limb is that the taxpayer must as a preliminary step have "set up his business". Special Commissioner Hellier at [88] agrees with the analysis in *Birmingham & District Cattle* and frames the business in terms of both the capital costs of setting up a business and its organisation:

"88...I conclude that a trade cannot commence until it has been set up (to the extent it needs to be set up), and that acts of setting up are not commencing or carrying on the trade. Setting up trade will include setting up a business structure to undertake the essential preliminaries, getting ready to face your customers, purchasing plant, and organising the decision making structures, the management, and the financing. Depending on the trade more or less than this may be required before it is set up"

92. The issue here is that even on the appellant's case none of these things had been done, except perhaps the financing, beyond contractual commitments as at Financial Close.

93. Mr Hellier adopting the comments of Lord Millett in *Birmingham & District Cattle*, rather assumed that a business had to be set up first before commencing operational activities ("a trade cannot commence until it has been set up (to the extent it needs to be set up)" [88]). Henderson J in the High Court in *Tower M Cashback* at made the same assumption [95]:

“95. It is unnecessary for me to say whether I would have reached the same conclusion on the facts as Mr Hellier did in *Mansell*, but in broad terms I find his test of the beginning of operational activities a useful one. Every case will turn on its own facts, but in general the test **presupposes that the framework or structure for the trade will have to be set up or established before any operational activity can begin...**” (*emphasis added*)

94. The appellant in his evidence argued that the 56 contracts entered into on Financial Close and the associated financial commitments meant that the LLP and its contracting parties were committed to these things and so that amounted to setting up the business.

95. Leaving on one side the question of what evidence was before the Tribunal, this is a difficult point. Every case must be decided on its facts but in my view it is conceivable that a taxpayer could be said to have set up its business in these circumstances. However, this is more likely to be the case where there are clear indicators of buying, selling and related activities, in effect the third limb of Special Commissioner Hellier's principles.

96. Accordingly, I have found it useful to consider at the same time this third limb in *Mansell*, where a taxpayer need not always have made a sale but must have begun "operational activities":

"93...and by operational activities I mean dealings with third parties immediately and directly related to the supplies to be made which it is hoped will give rise to the expected profits, and which involve the trader putting money at risk: the acquisition of the goods to sell or to turn into items to be sold, the provision of services, or the entering into a contract to provide goods or services: the kind of activities which contribute to the gross (rather than the net) profit of the enterprise"

97. This test, as expanded by Special Commissioner Hellier at [94], looks at the revenue side of the business, raw materials and sales, including contracts for both. The arrangements that are potentially relevant are the Feedstock Agreement, the energy contract and the sale of ROCs.

98. As I have found, the Feedstock Agreement is a contract for the supply of materials to the LLP not a supply by the LLP. Nevertheless, I accept that the Feedstock Agreement is "immediately and directly related" to the supplies of energy and ROCs to be made by the LLP. Further, the LLP has put money at risk under the Feedstock Agreement but the contract and so future suppliers are conditional on the construction of the plant. I have been unable to make any findings as to the significance of that condition as the appellant did not produce the relevant construction contracts.

99. There are two potential sources of income to the LLP, the energy contract and the sale of ROCs. I have found that there are no contracts or other arrangements for the sale of ROCs in the relevant period and so they are in my view irrelevant in establishing whether the LLP had commenced operational activities. The appellant did not produce the energy contract and accordingly in my view the appellant has not demonstrated that the electricity contract amounted to the kind of commitment inferred in the third limb of Special Commissioner Hellier's test.

100. I am therefore not satisfied that the appellant has shown that the LLP has commenced operational activities beyond the commitments in the Feedstock Agreement which in any event are contingent on the construction of the plant.

DECISION

101. In the absence of sales to customers, the appellant sought to rely on the principles in *Mansell* provides an alternative route to establishing the commencement of a trade. Special Commissioner Hellier's principles do not apply readily to the current circumstances, in particular the assumption that a business must be set up before it can commence operational activities.

102. However, even applying the principles loosely on the basis that each case must be decided on its own facts, I am not satisfied that the appellant has demonstrated that the LLP has commenced trading in the period.

103. I therefore find that the LLP did not trade in the period 24 August 2015 to 8 November 2016. Accordingly, I find that the appellant is not entitled to entrepreneurs' relief and I dismiss the appeal.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

104. 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.

**IAN HYDE
TRIBUNAL JUDGE**

Release date: 09 MAY 2022