[2019] UKFTT 0537 (TC)

TC07331

INCOME TAX – loss relief – loss in a trade – whether yacht chartering trade carried on on a commercial basis and with a view to the realisation of profits for the purposes of Section 66 of the Income Tax Act 2007 – held that the Appellant intended to realise profits (so that the condition in Section 66(2)(b) was met) but that the prospects of profits were so remote that the trade could not be said to have been carried on on a commercial basis for the purposes of Section 66(2)(a) – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2018/01900

BETWEEN

ROULETTE V2 CHARTERS LLP **Appellant**

-and-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **Respondents**

TRIBUNAL: JUDGE TONY BEARE
MS ELIZABETH BRIDGE

Sitting in public at Taylor House, 88 Rosebery Avenue, London EC1R 4QU on 17, 18 and 19 July 2019

Mr Oliver Marre for the Appellant

Mr Max Simpson, litigator of HM Revenue and Customs' Solicitor's Office, for the Respondents

DECISION

INTRODUCTION

1. This decision relates to an appeal against closure notices which were issued by the Respondents to the Appellant under Section 28B of the Taxes Management Act 1970 (the "TMA") for the tax years of assessment (each, a "tax year") ending 5 April 2012, 5 April 2013, 5 April 2014, 5 April 2015 and 5 April 2016. Each of the closure notices, which were issued on 17 October 2017, set out the conclusion that, by virtue of the application of Section 66 of the Income Tax Act 2007 (the "ITA"), the losses shown in the accounts of the Appellant for the periods of account of the Appellant which constituted the basis periods for the tax years to which this appeal relates were not available to be set off against the general income in those tax years of the member of the Appellant to whom 100% of the losses were allocable for income tax purposes, a Mr Trevor Silver.

2. On 15 November 2017, the Appellant appealed against the closure notices and requested a review. On 21 November 2017, the Respondents confirmed their view of the matter. On 13 February 2018, the Respondents notified the Appellant of the result of their review, which was to uphold their original conclusion in each closure notice in full. On 14 March 2018, the Appellant notified the First-tier Tribunal of its appeal against the conclusion reached in each of the closure notices.

3. There is one procedural point which we should make at the outset. When the Respondents send a closure notice under Section 28B of the TMA, they are obliged to make the amendments to the limited liability partnership's self-assessment return which reflect the conclusion set out in the closure notice and then to make the amendments to the self-assessment returns of each relevant member of the limited liability partnership which reflect the amendments to the limited liability partnership's return (see Sections 28B(3) and 28B(4) of the TMA). It is not clear to us that either of those things has been done in this case. Nevertheless, it is clear from the language used in Section 31(1)(b) of the TMA that the right of appeal set out in that section extends not only to any amendment made by a closure notice under Section 28B of the TMA but also to "any conclusion stated … by [that] closure notice". It follows that we can see no procedural impediment to the making of this appeal by the Appellant as such.

4. However, given that the conclusion in each closure notice against which the appeal has been made relates not to the question of whether the trading losses have arisen in the first place, but rather to the question of whether Mr Silver is entitled to set off those trading losses against his general income, we would have expected the present proceedings to have arisen from the amendments made to Mr Silver's self-assessment returns pursuant to Section 28B(4) of the TMA which reflected the conclusion set out in each closure notice. The fact that this is not how the proceedings have commenced leads us to wonder whether any such amendments to Mr Silver's personal self-assessment returns have in fact been made. A somewhat similar issue arose in the case of *Mr Anthony and Mrs Julia Rowbottom substituted for TJ Charters LLP v The Commissioners for Her Majesty's Revenue and Customs* [2016] UKFTT 9 (TC) ("*Rowbottom*"). In that case, there were two points in issue – the question of whether the relevant losses arose to the limited liability partnership at all and the question of whether, if they did, sideways relief was available to the members of the limited liability partnership to whom the losses were allocated. This led the First-tier Tribunal in that case to say the following at paragraph [7] of its decision:

"We say at this stage that it appears to us that neither issue is properly raised by this appeal as it stands. The closure notice disallows the losses to the partnership, TJC. It says nothing about the availability of losses for sideways relief to the partners in TJC. The issues between the parties, as it seems to us, need to be raised in an appeal brought by Mr and Mrs Rowbottom, and not by TJC. We have power under

rule 9 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ("the Rules") to substitute a party if the wrong person has been named as a party. We consider that TJC is the wrong person to have been named as appellant in the appeal and Mr and Mrs Rowbottom should have been named as appellants instead (or in addition to TJC). We consider, however, that we have before us the necessary evidence and submissions to decide the real issues between the parties – viz: whether or not the trade losses of TJC are available for relief against the general income of Mr and Mrs Rowbottom. We also consider that it would be in accordance with the overriding objective of the Rules (to deal with cases fairly and justly) to direct a substitution pursuant to rule 9 of the Rules. Accordingly, in order that the real issues between the parties can be decided, we direct the substitution of Mr and Mrs Rowbottom for TJC as appellants in the appeal and proceed accordingly."

5. The above has caused us to consider whether we should proceed in a similar manner and exercise the power referred to in the extract from *Rowbottom* set out above to substitute Mr Silver as the appellant in the appeal in place of the Appellant. We have concluded that this is not necessary on the facts in this case. It would seem from the above extract that, in *Rowbottom*, the relevant closure notice simply contained the conclusion that the relevant losses should be disallowed. It did not deal with the question of sideways relief at all. In contrast, each closure notice in this case did contain the conclusion that sideways relief was not available to Mr Silver and, as Section 31(1)(b) of the TMA provides for a right of appeal against that conclusion, we see no reason why we need to substitute Mr Silver as the appellant in place of the Appellant.

BACKGROUND AND AGREED FACTS

6. The Appellant is a limited liability partnership formed under the Limited Liability Partnerships Act 2000 (the "LLPA") on 17 April 2008 to carry on the trade of yacht-chartering. The members of the Appellant are Mr Silver and Mr Robert Newsholme. It is common ground that:

(1) pursuant to Section 2 of the LLPA, in order for a limited liability partnership to be formed:

(a) two or more persons associated for carrying on a lawful business with a view to profit must have subscribed their names to an incorporation document;

(b) that document (or a copy of it) must have been delivered to the registrar of companies; and

(c) there must also have been delivered to the registrar of companies a statement made by either a solicitor engaged in the formation of the limited liability partnership or anyone who subscribed his name to the incorporation document to the effect that the requirement described in paragraph 6(1)(a) above has been complied with;

(2) as a limited liability partnership incorporated under the LLPA, the Appellant is a body corporate, and therefore a separate legal person from each of its members as a matter of general English law;

(3) however, for income tax and corporation tax purposes, as long as it carries on its trade with a view to profit:

(a) all of the activities of the Appellant fall to be treated as carried on in partnership by its members;

(b) anything done by, to or in relation to the Appellant for the purposes of, or in connection with, any of its activities fall to be treated as done by, to or in relation to, its members as partners;

(c) the property of the Appellant is treated as held by the members as partnership property,

(see Section 863(1) of the Income Tax (Trading and Other Income) Act 2005 (the "ITTOIA") and Section 1273(1) of the Corporation Tax Act 2009 (the "CTA 2009"));

(4) in addition, for all purposes, except as otherwise provided, in the Income Tax Acts and the Corporation Tax Acts:

(a) references to a firm or partnership include a limited liability partnership to which Section 863(1) of the ITTOIA and Section 1273(1) of the CTA 2009 apply;

(b) references to members or partners of a firm or partnership include members of such a limited liability partnership;

(c) references to a company do not include such a limited liability partnership; and

(d) references to members of a company do not include members of such a limited liability partnership,

(see Section 863(2) of the ITTOIA and Section 1273(2) of the CTA 2009);

(5) it follows from the above that, as long as the Appellant was carrying on its trade in each period of account of the Appellant which is relevant to this appeal "with a view to profit", then the Appellant fell to be treated for both income tax and corporation tax purposes in respect of the tax year in relation to which that period of account is the basis period in the same way as a partnership, with the result that:

(a) it would not fall to be treated for such purposes as an entity separate and distinct from its members;

(b) its losses or profits for such purposes would fall to be calculated in the same way as if it were an individual;

(c) those losses or profits would be allocated to its individual members in accordance with their respective shares in the losses or profits of the Appellant during that period of account; and

(d) in each period of account which is relevant to this appeal, Mr Silver was entitled to 100% of the losses and profits of the Appellant, with the result that the whole of the losses or profits of the Appellant in the tax year in relation to which that period of account is the basis period will have been treated as accruing to Mr Silver,

(see Part 9 of the ITTOIA);

(6) the Appellant made a loss in respect of each period of account which is relevant to this appeal (and, indeed, each period of account which preceded each such period of account);

(7) subject to the terms of certain other provisions in Chapter 2 of Part 4 of the ITA, which include the provision described in paragraph 8 below, as long as the loss in respect of each tax year which is relevant to this appeal fell to be treated as having been made by Mr Silver himself pursuant to the provisions described above, that loss could be set off against the general income of Mr Silver in respect of the relevant tax year (see Section 64 of the ITA);

(8) Section 64 of the ITA is subject to the terms of (inter alia) Section 66 of the ITA, which restricts the availability of losses for "uncommercial trades". Section 66 of the ITA is set out in full in paragraph 8 below;

(9) throughout the period in which the Appellant carried on its trade of yacht chartering, it conducted its trade using only one yacht, a 65 foot Oyster named Roulette V2 (the "Yacht"). The Yacht was purchased by Mr Silver from the manufacturer in September 2007 with the aid of a loan. Mr Silver subsequently discharged the loan and contributed the Yacht to the Appellant as a capital contribution in July 2008, shortly after the Appellant was formed;

(10) prior to acquiring the Yacht, Mr Silver had owned other yachts – Meaalofa, a 53 foot Amel acquired in April 1998 and held until 2003, and Roulette, a 56 foot Oyster acquired in 2003 – which he sailed for pleasure;

(11) as the Appellant operated at a loss throughout the period following its formation, Mr Silver has made periodic capital contributions to the Appellant in order to fund the losses; and

(12) the Respondents have not sought to challenge the ability of Mr Silver to set off, against his general income, the losses arising in the periods of account of the Appellant which constitute the basis periods for the tax years ending 5 April 2009, 5 April 2010 or 5 April 2011.

7. It is also common ground in this appeal that, although the dispute centres on the conduct of the Appellant's trade over only a small part of the overall period comprising the periods of account which are relevant to this appeal, the "presumption of continuity" which is a general feature of the UK tax system means that the conclusions which we reach in relation to that small part of the overall period should be regarded as applying to each of the periods of account in question.

THE RELEVANT LAW

8. As we have intimated in paragraph 6(8) above, the statutory provision which is at the heart of this case is Section 66 of the ITA. This provides as follows:

"*Restriction on relief for uncommercial trades*

Restriction on relief unless trade is commercial

(1) Trade loss relief against general income for a loss made in a trade in a tax year is not available unless the trade is commercial.

(2) The trade is commercial if it is carried on throughout the basis period for the tax year—

(a) on a commercial basis, and

(b) with a view to the realisation of profits of the trade.

(3) If at any time a trade is carried on so as to afford a reasonable expectation of profit, it is treated as carried on at that time with a view to the realisation of profits.

(4) If the trade forms part of a larger undertaking, references to profits of the trade are to be read as references to profits of the undertaking as a whole.

(5) If there is a change in the basis period in the way in which the trade is carried on, the trade is treated as carried on throughout the basis period in the way in which it is carried on by the end of the basis period.

(6) The restriction imposed by this section does not apply to a loss made in the exercise of functions conferred by or under an Act.

(7) This section applies to professions and vocations as it applies to trades."

9. It can be seen that the section precludes trading losses from being relieved against general income unless the trade in question is "commercial" (see both the heading to the section and the terms of Section 66(1) of the ITA). It then goes on to explain, in Section 66(2) of the ITA, that a trade is "commercial" if it is carried on throughout the basis period for the tax year (or, pursuant to Section 66(5) of the ITA, at least at the end of the basis period for the tax year):

(1) "on a commercial basis"; and

(2) "with a view to the realisation of profits of the trade".

10. There are two additional points which we should make at this juncture in relation to the law which is relevant to this appeal.

11. The first is that one of the issues which is in dispute between the parties is whether, in order to succeed in this appeal, it is necessary for the Appellant to establish, in relation to each period of account which is relevant to this appeal, that it was both carrying on its trade "on a commercial basis" and carrying on its trade "with a view to the realisation of profits of the trade" or whether, because of the way in which the Respondents have drafted their Statement of Case, it is merely necessary for the Appellant to establish that the former was the case. We address that question in detail in the discussion set out in paragraphs 80 to 83 below.

12. In connection with that procedural question, we should mention the Tribunals, Courts and Enforcement Act 2007 and The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (SI 2009/273) (the "Tribunal Rules") which have been made pursuant to that Act and which govern the conduct of proceedings before the First-tier Tribunal.

13. Rule 25(2) of the Tribunal Rules provides that "[a] statement of case must—

(a) in an appeal, state the legislative provision under which the decision under appeal was made; and

(b) set out the respondent's position in relation to the case."

14. However, this requirement is subject to Rule 7(2) of the Tribunal Rules, which provides that, "[if] a party has failed to comply with a requirement in these Rules, a practice direction or a direction, the Tribunal may take such action as it considers just, which may include…waiving the requirement" and to Rule 2 of the Tribunal Rules, which requires the First-tier Tribunal to give effect to the overriding objective – of dealing with cases fairly and justly – whenever it exercises any power under the Tribunal Rules or interprets any rule.

15. The second is that it can be seen from paragraphs 6(1) to 6(5) above that:

(1) the very status of the Appellant as a limited liability partnership under the LLPA depends on its members' "being associated for carrying on a lawful business with a view to profit" (see Section 2(1)(a) and (c) of the LLPA); and

(2) a limited liability partnership is not treated as being the equivalent of a partnership for income tax and corporation tax purposes – and is therefore not transparent for those purposes but is instead opaque for those purposes, like any other body corporate – unless it is carrying on its trade "with a view to profit" (see Sections 863(1) and (2) of the ITTOIA and Sections 1273(1) and (2) of the CTA 2009).

16. It can therefore be seen that, in the case of a limited liability partnership such as the Appellant, a conclusion that the Appellant was not carrying on its trade "with a view to profit" would have consequences under both general English law and UK tax law which would extend beyond an inability for Mr Silver to set off the losses of the Appellant against his general income. However, as neither party made any submissions in relation to these issues in the conduct of this appeal and, as may be seen from the conclusions reached in the discussion set

out in paragraphs 84 to 96 below, a consideration of the issues is unnecessary in terms of determining this appeal, we do not propose to address the issues in this decision.

THE EVIDENCE

The documentary evidence

17. The documents bundle for the hearing (the "Documents Bundle") included minutes of numerous meetings at which the affairs of the Appellant were discussed. Those minutes reveal that:

(1) there was considerable focus throughout on managing the costs of the Appellant and on obtaining additional charters - for example, by improving the website and the Appellant's notepaper, printing brochures, using the contacts within the industry of Mr John Boyce – who had been engaged by the Appellant to manage the Yacht - and taking advantage of promotional articles in magazines;

(2) reference was made in the minutes of the meeting held on 3 November 2008 to the potential sale of the Yacht and the possible purchase by the Appellant of other yachts which might be more attractive as charter options;

(3) reference was made in the minutes of various meetings to the fact that the Appellant should not be relying on its broker, Oyster Brokerage Limited ("OBL"), for customers and should have its own form of charter agreement;

(4) in paragraph 13 of the minutes of the meeting of 19 March 2009, reference was made to advice from Mr Michael Ashdown, tax advisor to Mr Silver and the Appellant, to the effect that:

(a) charter income "needs to be as high as possible. The income box on the VAT return should be higher than the cost box as often as possible"; and

(b) "he saw no reason why TS could not have preferential payment terms, but the charter rates need to be as commercial as possible"; and

(5) the meetings which were held to discuss the Appellant's affairs were not confined to those affairs. Within the minutes, there are occasional references to the affairs of Mr Silver himself, interchangeably with the affairs of the Appellant. For example:

(a) in paragraph 14 of the minutes of the meeting on 19 March 2009, reference was made to the rental income which Mr Silver might obtain from his berth in Antibes given that the Yacht was not there;

(b) in paragraphs 10 and 17 of the minutes of the meeting of 30 April 2009, reference was made to Mr Boyce's going to Monaco and Antibes at the end of May and bringing Mr Silver's BMW back to the UK for an MOT and to Mr Boyce's finding out more about the possible withholding taxes which might be levied on payments of rent to Mr Silver for the use of his berth in Antibes; and

(c) in paragraph 4 of the minutes of the meeting of 6 August 2009, Mr Boyce was asked to investigate a potential sale of Mr Silver's berth in Antibes.

18. The Documents Bundle also included invoices for the period between July 2010 and August 2011 which were included at pages 6 et seq. in tab 24. We were also provided with an additional invoice to Mr Silver in relation to a charter to Mr Silver's son for two weeks in August 2010. Four of the charters which were reflected in those invoices were to Mr Silver, Mr Silver's son and a company related to Mr Silver – Landid Property Holdings Limited. The balance of the charters over that period – eight in all – were to persons unrelated to Mr Silver. In addition, we observed that one of the invoices over that period to a person unrelated to Mr

Silver – the invoice to a Mr France for one week in August 2010 – was for £6,000, which was the same weekly rate as that paid by Mr Silver for the two week charter to his son in the same month.

19. The Documents Bundle also included certain insurance documentation which revealed that:

(1) prior to 2011, the Appellant had not been insured at all for periods when the Yacht was out on charter;

(2) thereafter, cover for those periods was acquired but only for a maximum of 12 charters over any annual insurance period; and

(3) the insurance documents were in the name of Mr Silver himself and not in the name of the Appellant.

20. The Documents Bundle included price lists from OBL covering various periods which showed that the Yacht was being advertised for charter:

(1) over the period from May 2009 to April 2010, at rates of between £12,000 and £14,000 per week (in the Mediterranean) and between £10,500 and 11,500 per week (in the Caribbean);

(2) over the summer of 2010, at the rate of £15,500 per week in the Mediterranean; and

(3) over the period from May 2011 to April 2012, at the rate of £16,000 per week in the Mediterranean.

21. Finally, the Documents Bundle included copies of the accounts of the Appellant for each period of account. These revealed the following by way of income, expenses (before depreciation), depreciation and losses:

Period of account ending	Income (including bank interest received)	Expenses before depreciation	Depreciation	Loss
30 April 2009	£41,012	(£195,923)	(£113,037)	(£267,948)
30 April 2010	£91,600	(£190,645)	(£113,050)	(£212,095)
30 April 2011	£122,816	(£146,694)	(£113,050)	(£136,928)
30 April 2012	£62,175	(£148,276)	(£113,050)	(£199,151)
30 April 2013	£42,002	(£61,076)	(£113,050)	(£132,124)
30 April 2014	£45,625	(£90,074)	(£113,050)	(£157,499)
30 April 2015	£55,750	(£111,927)	(£113,050)	(£169,227)
30 April 2016	£152,000	(£219,342)	(£113,050)	(£180,392)

The witness evidence

22. In the course of the hearing, we heard evidence from Mr Silver and Mr Newsholme – the two members of the Appellant – as well as from Mr Boyce - who was engaged by the Appellant to carry out certain duties in relation to the Appellant's yacht-chartering trade and by Mr Silver to carry out certain duties for Mr Silver in his personal capacity - and Mr Griffyth Thomas, the

Officer of the Respondents with responsibility for Mr Silver's personal tax affairs since September 2015.

23. The key features of Mr Silver's evidence were as follows:

(1) although the Appellant had experienced financial difficulties, he and Mr Newsholme had at all times throughout the Appellant's existence sought to run the Appellant on a commercial basis and with a view to profit;

(2) although he had purchased the Yacht in his own name, his intention had always been that the Yacht would be used in the course of a yacht-chartering trade and not for his personal pleasure. The Yacht was the first yacht of his which required a crew and its pumping system and rigging were highly specified. It was a fast cruising yacht which could be handled by the crew alone and did not need any input from the guests on board. He would not have opted for the high specifications which he had if he hadn't intended the Yacht to be used for chartering from inception;

(3) the decision that the Yacht would be transferred to the Appellant was taken only after he had taken professional advice as to the best vehicle for holding the Yacht. Following delivery of the Yacht, he had transferred the Yacht to the Appellant as soon as he had been able to discharge the bank debt which he had taken out to make the acquisition;

(4) he had purchased the Yacht from Oyster Marine Limited ("OML") and, prior to making the purchase, he had spoken to the people at a subsidiary of OML, OBL, which dealt in yacht and chartering brokerage, to understand whether using the Yacht in the course of a yacht-chartering business was viable. They had assured him that it was;

(5) the business model suggested by OBL was that the owner of the Yacht would be able to obtain charters of the Yacht in each year for a minimum of 6 weeks in the Mediterranean and 8 to 10 weeks in the Caribbean, in each case at around £10,000 to £12,000 per week. Moreover, Mr Silver thought that the owner would be able to obtain additional charters of the Yacht for a further 8 weeks or so each year. That suggested that charter income of between £180,000 and £250,000 per annum was a realistic expectation at the time when the Yacht was ordered;

(6) having said that, he recognised that the pricing of charters was always subject to negotiation and that the list price for any period (as described in paragraph 20 above) might not be able to be obtained;

(7) as regards the Appellant's costs, he had expected the running costs in the initial periods of account to be lower than they actually were because the Yacht was still under warranty but, in the event, these had proved to be higher than expected. He had tried to cut costs by finding a cheaper berth for the Yacht and reducing crewing costs;

(8) he said initially in his oral testimony that he had not planned for the Appellant to keep the Yacht for more than 3 to 4 years and he had not anticipated significant depreciation in the value of the Yacht over that time period. His previous yachts had depreciated very slowly over the initial years of his ownership. However, he accepted that:

(a) at the time of buying the Yacht, the expected depreciation of the Yacht over the first three years was £133,100 per annum– as set out as an attachment to his undated letter to Ms Anne Griffiths, an Officer of the Respondents, which appeared at page 74 of tab 18 to the Documents Bundle;

(b) the Appellant was depreciating the Yacht in its accounts over twenty years on a straight-line basis – ie at 5% per annum. This meant that it was shown in the accounts as depreciating at approximately the same amount;

(c) depreciation would accelerate over time and the periods of account of the Appellant which were relevant to this appeal largely fell after the initial three or four year post-delivery period;

(9) unfortunately, he had taken delivery of the Yacht just as the financial recession occurred and so the Appellant had been unable to obtain the level of charters that he had expected at the time of placing the order. In particular, OBL had not lived up to its promise in terms of delivering customers and, in September 2011, OBL's appointment as charter manager was terminated. Moreover, the recession also meant that the Appellant had been unable to sell the Yacht within the three to four year timeframe which he had anticipated when placing the order;

(10) the Appellant had appointed Mr Boyce to be manager of the Yacht because of Mr Boyce's experience in the industry and substantial contacts. It would not have engaged Mr Boyce – and thereby incurred the additional costs of doing so - unless it had intended to carry on its trade on a commercial basis;

(11) there were regular meetings of the two members of the Appellant, often including Mr Boyce, to discuss the operations of the Appellant. These meetings were initially formally minuted (and copies of the minutes were included in the Documents Bundle). However, after Mr Newsholme's wife became ill and Mr Newsholme was less able to devote time to the Appellant's trade, although the meetings continued to be held, the practice of formally minuting the meetings ceased;

(12) the Appellant had set up a website and prepared a brochure in order to attract customers. The website had been actively managed and kept up to date over each period of account which was relevant to this appeal;

(13) he had tended to charter the Yacht himself during off-peak periods, when demand was lower – at Easter or in June - and not in August. If a person who was unrelated to him had wanted to charter the Yacht at any time when he would otherwise have taken it, then he would have stepped aside and given that person priority. In addition, he had paid a commercial rate to the Appellant for his own charters. However, he conceded that:

(a) the minutes of the meeting held on 6 August 2009 referred to the fact that OBL had confirmed that they "could have sold August charters at least twice over. Future consideration has to be to ensure that [non] commercial charters are kept to a minimum during periods when commercial charters are at a premium" and that this suggested that non-commercial charters were being implemented, at least on or before 6 August 2009; and

(b) Mr Silver's son had chartered the Yacht for two weeks in August 2009 for £15,000 and for two weeks in August 2010 for £12,000 (although Mr Silver said that no-one was prepared to charter the Yacht at those times for a greater amount);

(14) the fact that the Appellant was intended to be run on a commercial basis could be seen by the fact that the Isle of Man had accepted the Appellant's application to register for VAT on the basis of the Appellant's business plan. However, he could not now locate the business plan;

(15) the trade had eventually been discontinued (and the Yacht had been mothballed) in October 2017 when it became apparent that the charter income was never going to cover the costs of maintaining the Yacht;

(16) he conceded that Mr Boyce, in addition to providing his services to the Appellant, also provided services to him in his personal capacity. For instance, the berth in Antibes was owned by Mr Silver and rented to the Appellant and therefore, when it was agreed at the meeting on 6 August 2009 that Mr Boyce would actively pursue a sale of the berth, as noted in paragraph 17(5)(c) above, Mr Boyce was doing that for Mr Silver and not the Appellant;

(17) he also conceded that the Appellant had made losses at all times since its trade commenced, as revealed in the accounts of the Appellant for each period of account (see paragraph 21 above). In any event, in paragraph 37 of his witness statement, Mr Silver acknowledged that, by the time of the meeting on 30 April 2009, "we knew [the Appellant's trade] was unlikely to be profitable". The losses set out above had necessitated regular capital contributions from him to the Appellant;

(18) he accepted that, even if the charter income in any year had been sufficient to cover the costs of running the Yacht, there was no prospect that the charter income would be capable of covering both the running costs and the depreciation. However, he thought that, if the business carried on by the Appellant were to be successful, then that would generate substantial goodwill in the business and that the value of that goodwill would be sufficient to counteract the loss arising out of the depreciation in the Yacht in due course. He had therefore not been concerned about the impact of the depreciation on the overall profitability of the Appellant's trade; and

(19) he accepted that:

(a) prior to 2011, the Appellant had not been insured at all for periods when the Yacht was out on charter; and

(b) thereafter, cover for those periods was acquired but only for a maximum of twelve charters over any annual insurance period.

However, he attributed the first of these to an oversight on his part and said that, as regards the second of these, there was no point in paying a premium to obtain cover for any more charters than were actually going to occur. Therefore, his strategy was to pick twelve as the aggregate number of charters which it was realistic to expect the Appellant to be able to obtain over any annual insurance period and then to pay a top up premium if, in the event, the Appellant was able to obtain more charters than those twelve. In the event, that had not been necessary because the number of charters obtained had been beneath that limit.

24. The key features of Mr Boyce's evidence were as follows:

(1) he had been approached by Mr Silver to manage the Yacht for the Appellant. In that capacity, his role was to use his experience and expertise within the industry to manage the crew and the running of the trade and his contacts within the industry to generate business;

(2) the intention at all times was that the Appellant was intended to be run on a commercial basis in an industry-standard manner and to make profits. However, due to market conditions, the Appellant's business had not been as successful as everyone had hoped at the start. Nevertheless, the Appellant did try to maximise its profits by seeking to obtain charter customers itself, as opposed to relying exclusively on OBL;

(3) as his expertise was in yachting and not financial matters, and he had not previously carried on a chartering business, he did not have a detailed knowledge of the financial issues associated with carrying on a chartering trade. To the extent that he did have some knowledge in the financial area, that was largely to do with the going rate for charters. He knew somewhat less about the costs associated with chartering a yacht and the amount by which yachts depreciated. Accordingly, he did not know how many charters would be needed each year in order for the Appellant to make a profit;

(4) he would occasionally act as an intermediary in the negotiation of rates for a particular charter – as was revealed in an email at pages 2 and 3 of tab 20 of the Documents Bundle – and he would also sometimes make decisions in relation to costs although, generally, he referred those decisions to Mr Silver;

(5) he accepted that some of the items which were discussed at the meetings in relation to the Appellant's affairs related instead to Mr Silver's affairs. However, he believed that Mr Newsholme made an adjustment for this when preparing the accounts of the Appellant;

(6) he said that August was the peak month for charters and that repeat customers were an important part of building the Appellant's business. In that context, he said that the August charters to Mr Silver's son would have been acceptable if Mr Silver's son was the only potential customer for those periods but not if Mr Silver's son was displacing a potential customer who was unrelated to Mr Silver. He said that, in the latter case, although Mr Silver would have had the right to compel the charter to Mr Silver's son to proceed, he would have expressed his disagreement with the decision. In that context, Mr Boyce was taken to a letter from Mr Newsholme to Ms Griffiths of 28 September 2017 in which Mr Newsholme referred to certain non-commercial charters in the following terms:

"Having read your comments I think there is a possibility that you may have mis-construed some of the comments contained in the documentation. You are quite correct that there were references to this point in the minutes etc. In fact, there was one occasion when Trevor's son chartered the yacht in the month of August. For this Trevor did pay market rate, but the point is that in the summer months it would have been much more preferable to charter to third parties on the principle of building up a sustainable client base for repeat and future charters. John Boyce made his feelings clear at the time and it was documented accordingly".

Mr Boyce was asked to explain the final sentence in the above extract and he said that the "feelings" to which Mr Newsholme was referring must have been the point made above about preferring charterers who were unrelated to Mr Silver over Mr Silver and persons related to him; and

(7) he confirmed that the Mediterranean season ran roughly from April to September and that the Caribbean season ran roughly from December to March. The seasons were reflected in the marina fees, so that, for example, in the Mediterranean, the marina fees between April and September were double what they were in the off-season. In the case of the Yacht, it had been to the Caribbean only once – over the winter of 2009/2010 - and, during that period, the only customer who had chartered the Yacht was Mr Silver. However, this was largely attributable to the fact that OBL had not fulfilled its end of the bargain as regards finding potential customers.

25. The key features of Mr Newsholme's evidence were as follows:

(1) he had been Mr Silver's tax advisor and had also provided day-to-day assistance in helping to administer Mr Silver's various business interests. However, he had ceased to fulfil these roles as a result of his wife's illness and the latest tax return which he had

filed for Mr Silver was Mr Silver's tax return in respect of the tax year ending 5 April 2013. The limited liability partnership structure had been set up on the advice of Mr Ashdown and he believed that the structure was primarily VAT-driven;

(2) Mr Silver had been very clear from the outset that his purpose in acquiring the Yacht was to charter out the Yacht with a view to making profits. In that regard, he recalled that, as part of registering the Appellant for VAT purposes in the Isle of Man, a twenty year business plan had needed to be filed with the Isle of Man VAT authorities but he had been unable to locate that business plan in connection with preparing for the hearing of this appeal;

(3) his role in the Appellant's trade had been to ensure the smooth day-to-day running of the administration part of the business. He did not himself arrange charters but he ensured that charter agreements were signed and that payments for charters were duly made. He also took the minutes of the meetings with Mr Silver and Mr Boyce although his wife's illness meant that he had been less and less able to maintain his involvement in the Appellant's business. Nevertheless, he was well aware that Mr Silver and Mr Boyce had continued to meet (and to discuss matters on the telephone) despite the absence of formal minutes over the period of his reduced involvement. He knew this because they continued to let him know of the results of those discussions;

(4) as he had no entitlement to the profits of the Appellant in his capacity as a member, he had taken the remuneration for his work for the Appellant in the form of a fee. His involvement with the Appellant had ceased on 6 April 2017, when he formally resigned as a member of the Appellant;

(5) as regards the work done by Mr Boyce for Mr Silver in his personal capacity, Mr Newsholme confirmed that he had taken this into account in the books of the Appellant by apportioning Mr Boyce's charges between the Appellant and Mr Silver. Mr Silver's portion of the charges were treated as drawings by Mr Silver from the Appellant, with the result that Mr Silver suffered the economic burden of that portion of the charges by having to make increased capital contributions to the Appellant;

(6) he conceded that, contrary to the extract from his letter to Ms Griffiths set out in paragraph 24(6) above, Mr Silver's son had in fact chartered the Yacht in two successive Augusts (2009 and 2010) and not just one. However, he did recall the exchange of views between Mr Silver and Mr Boyce which was recorded in that extract – he and Mr Boyce had both been in agreement that customers other than Mr Silver and persons related to Mr Silver should be preferred in the case of August charters, for the reasons given in the extract;

(7) like Mr Silver, he had thought that, on the basis of the advice as to the potential charters which Mr Silver had received from OBL at the time of ordering the Yacht, it would be feasible to make a profit from chartering the Yacht. However, unlike Mr Silver, this was not because he had expected that the Appellant would accrue some valuable goodwill to counteract the impact of the depreciation of the Yacht. Instead, he had believed that the income derived by the Appellant from its chartering activities would be sufficient to cover both its running costs and the depreciation; and

(8) finally, he explained the reference in the minutes of the meeting of 19 March 2009 to the advice from Mr Ashdown on the need to maximise income in the Appellant as being a reference to safeguarding the Appellant's Isle of Man VAT position.

26. The key features of Mr Thomas's evidence were as follows:

(1) in the period covered by the invoices which were in the Documents Bundle, approximately 50% of the charter income derived by the Appellant had emanated from Mr Silver or persons related to Mr Silver and approximately 65% of the time that the Yacht was out on charter it was being chartered Mr Silver or persons related to Mr Silver;

(2) contrary to the suggestion made by Mr Marre, the Respondents had not accepted that the Appellant had satisfied the conditions in Section 66(2) in each of the periods of account of the Appellant that had preceded the periods of account which were relevant to this appeal. Instead, it was just that no-one within the Respondents had ever got around to examining the position in relation to those periods of account before the enquiries into the later tax years were opened; and

(3) contrary to the statement made by Mr Silver, the Appellant's website had not been kept up to date after 2011.

THE RELEVANT ISSUES

27. This appeal raises two issues as follows:

(1) the Procedural Issue – in the light of the terms of their Statement of Case, is it open to the Respondents to require the Appellant to establish that, throughout each period of account which is relevant to this appeal, in addition to carrying on its trade "on a commercial basis", it carried on its trade "with a view to the realisation of profits of the trade"? and

(2) the Substantive Issue - has the Appellant established that, throughout each period of account which is relevant to this appeal, it carried on its trade "on a commercial basis" and, if the answer to the Procedural Issue is in the affirmative, has the Appellant established that, throughout each such period of account, it carried on its trade "with a view to the realisation of profits of the trade"?

28. It is common ground that the burden of proof in relation to the Procedural Issue is on the Respondents but that the burden of proof in relation to the Substantive Issue is on the Appellant. However, Mr Marre urged us to bear in mind that, should we determine the Procedural Issue in favour of the Respondents, we should apply the burden of proof more leniently in the case of the "realisation of profits" limb of the Substantive Issue and resolve any ambiguities in relation to that limb in favour of the Appellant.

INTRODUCTION TO, AND THE ARGUMENTS IN RELATION TO, THE RELEVANT ISSUES

The Procedural Issue

Introduction

29. The background to the Procedural Issue is as follows:

(1) each closure notice of 17 October 2017 stated that "[the] losses produced by the accounts do not satisfy the criteria of Section 62 ITA 2007 and are not allowable against general income under Section 66 ITA 2007. Please refer to my earlier correspondence dated 17 March 2017, 5 May 2017 and 13 October 2017 which gives the background to my conclusion";

(2) the "Conclusion" section of the Respondents' letter of 17 March 2017 said as follows:

"I have considered the facts and figures in detail. I propose to disallow sideways loss relief claimed under Section 64 ITA 2007. Primarily because the accounts and records clearly indicate that there never has or will be an expectation of profit. The yacht charter fails the second test of

Section 66(2)(b) ITA 2007. I consider that there is no possibility of profit regardless of however long the charter continues…

Secondly, I do not believe that for the periods in question the trade has been run in a commercial manner and so also fails the test at Section 66(2)(a) ITA 2007, for the reasons given above";

(3) the Documents Bundle did not contain a letter from the Respondents of 5 May 2017. It seems likely that the reference in each closure notice to a letter of that date was intended to say 19 May 2017 instead. Having said that, there is nothing in the letter of 19 May 2017 which sheds any further light on the reasons which the Respondents were giving to the Appellant for denying the availability of the relief;

(4) following further exchanges between the parties, the Respondents' letter of 13 October 2017 responded to certain points which the Appellant had made in the course of those exchanges and concluded:

"I am sorry that this may be a disappointing reply but my position remains unchanged";

(5) in their letter of 21 November 2017 confirming their view of the matter, the Respondents stated that that view "remains as set out in my decision letters of 17 October 2017 and also in previous correspondence";

(6) in the review conclusion letter of 13 February 2018, the Respondents noted that there were two points at issue, as follows:

" Whether the trade was commercial within the meaning of the Income Tax Act 2007

Whether the trade was carried on during the relevant periods with a view to the realisation of profits in the trade".

It then went on to set out both limbs of the test in Section 66(2) and the Respondents' analysis of the facts before concluding that "the decision to issue the …closure notices on the basis that losses are not available under S66 ITA 1970 should be upheld";

(7) in the "Grounds for appeal" section of its Notice of Appeal to the First-tier Tribunal of 14 March 2018, the Appellant stated as follows:

"We believe [the Appellant] was in business with a view to profit and the business was commercial consequently sideways losses are available to set against other income"; and

(8) the parts of the Respondents' Statement of Case which are pertinent to this issue said as follows:

"…

Points at Issue

3.1Was the partnership Roulette V2 LLP trading commercially to satisfy S66 Income Tax Act 2007 thus enabling the losses produced by the accounts to be set against the partner's general income as claimed.

Legislation And Case Law

…

4.2 S64 Income Tax Act 2007 – Deduction of losses from general income.

4.3 S66 Income Tax Act 2007 – Restriction on relief unless trade is commercial.

Case history

….

5.8 Agreement could not be reached during the enquiry so closure notices for all 5 years were issued on 17 October 2017. The basis for the amendment to the partnership returns were that losses claimed are not allowable under S66 ITA 2007.

…

Matters in Dispute

8.1 Has the yacht charter partnership been carried out on a commercial basis.

Appellants Contentions

9.1 The appellant believes the LLP was in business with a view to profit and the business was commercial.

9.2 As the business was commercially operated sideways losses are available to set against other income.

HMRC's case

10.1 This partnership has not been run on a commercial basis therefore the condition of S66 (2)(b) Income Tax Act 2007 is not satisfied and losses are not available for be set off as claimed.

10.2 In arriving at this decision HMRC have considered the accounts submitted for the partnership for the periods 2009/10 to 2015/16. These accounts show a loss situation in every year.

10.3 HMRC considered the evidence submitted and have found that from the beginning charter booking fees were not sufficient to cover running costs. They have not seen any evidence to show any reasonable expectation of profits.

10.4 HMRC have not been provided with any evidence to show the expectation of a profit from the outset of the partnership.

10.5 HMRC have also considered the substantial capital introduced to the partnership by Mr Silver as clear evidence that the partnership was not commercial.

10.6 HMRC consider that the lack of evidence to show a business plan or realistic plan to increase the number and value of charters or a clear plan to reduce the overheads on a charter means the business was not run on a commercial basis or with a view to a profit.

10.7 The appellant has stated that it was always his intention to sell the yacht after 3 years HMRC believe this to show there was never a commitment to a trade and the reason for purchase was a personal one in line with the appellant's hobby.

10.8 HMRC have considered the insurance policy and in particular the restriction on charters without the written approval of the company. Even when amended in later policies there was a restriction to a maximum of 12 passengers and charters. HMRC believe this also supports their position that the partnership was not operating commercially.

10.9 HMRC believe the yacht was chartered in an attempt to generate revenue to offset costs rather than with a view to a profit. As such the conditions of S66 Income Tax Act 2007 are not satisfied and the losses are not available for sideways set off against the director's general income.

…

Outcome

11.1 HMRC request the Tribunal to find that the partnership was not operated on a commercial basis.

11.2 HMRC request the Tribunal to find that the closure notices issued on 17 October 2017 for the years 2011/12 to 2015/16 inclusive are correct.

11.3 HMRC request the tribunal to dismiss the appeals."

The arguments of the parties

30. Mr Marre submitted on behalf of the Appellant that the Respondents should be precluded from arguing at the hearing that the Appellant had failed the second condition in Section 66(2) of the ITA – the fact that, in carrying on its trade in the periods of account in question, the Appellant did not have "a view to the realisation of profits" – because both the exchanges of correspondence leading up to the Notice of Appeal to the First-tier Tribunal and the grounds of appeal set out in that Notice of Appeal had made it clear that both conditions in Section 66(2) of the ITA were in play and yet the Statement of Case had not referred to the second condition as being in issue.

31. In that regard, Mr Marre pointed in particular to paragraphs 8.1, 10.1 and 11.1 of the Statement of Case as suggesting that only the first condition remained in issue between the parties. He explained the references in the Statement of Case to the absence of a view to the realisation of profits by the Appellant as being no more than the recognition by the Respondents that, as is discussed in paragraphs 36 to 57 below in relation to the Substantive Issue, an expectation of profits is an integral part of satisfying the first condition.

32. In response, Mr Simpson submitted on behalf of the Respondents that, although the Statement of Case was not a model of clarity, there were sufficient references in the Statement of Case to both conditions and to the language used in the second condition to put the Appellant on notice that it had a case to answer in relation to the second condition as well as the first.

33. In particular, Mr Simpson pointed out that, because of the way in which Section 66 of the ITA was worded – with its initial reference to the need for the trade to be "commercial" and then with the subsequent reference to the need for the trade to be carried on "on a commercial basis" as one of the two conditions which needed to be satisfied in order for the trade to be "commercial" – not every reference to the word "commercial" in the Statement of Case could fairly be construed as a reference to the first condition in Section 66(2) of the ITA. In that regard, Mr Simpson directed us to the use of the word "commercial" and "commercially" in paragraphs 10.5 and 10.8 respectively of the Statement of Case. He also directed us to the references in paragraphs 10.3, 10.4, 10.6 and 10.9 of the Statement of Case to the lack of expectation of profits.

The Substantive Issue

Introduction

Actual losses

34. It is common ground that the requirements of Section 66 of the ITA can still be met despite the fact that the taxpayer in question has actually suffered losses. That much is obvious from the fact that, by definition, the section is confined to dealing with circumstances where losses have arisen.

35. At first instance in *Acornwood LLP v The Commissioners for Her Majesty's Revenue and Customs* [2014] UKFTT 416 ("*Acornwood*"), the First-tier Tribunal noted the following at paragraph [369]:

"[369] The legislation requires that the trading activity be carried on with a view to profit, but says nothing about the scale of the profit (nor, realistically, could it do so) and it requires only an aim to profit, and not the realisation of profits. One may set out with a clear business plan, with adequate capital and other resources, and with a commitment to devote the necessary time to the trade, yet still fail because of unexpected market conditions, because the choice of commodity was ill-judged or because of misfortune. As we see it, the legislation (which, after all, is aimed at relieving losses) is not intended to penalise those who, despite their best efforts, are unsuccessful, but rather to exclude those

who, despite their desire for profits, do not conduct their trading activities in a manner which, all things being equal, are conducive to the generation of profits.

The two conditions

36. It may be seen from the extract from *Acornwood* cited above that, in each case, it is necessary to consider whether the trade in respect of which the losses have arisen satisfies the two conditions in Section 66(2) of the ITA.

37. There is a considerable degree of overlap between those two conditions. As Henderson LJ (with whom David Richards and Arden LJJ agreed) said in *Samarkand Film Partnership No 3 and Others v The Commissioners for Her Majesty's Revenue and Customs* [2017] STC 926:

"The conditions therefore embody two tests: a test of commerciality, and a profits test…broadly speaking [the profits test] requires the trade to have been carried on with a view to making profits."

38. He went on to say that:

"… considerations of profitability cannot be divorced from an assessment of the commerciality of the business. In my judgment it is wrong to regard the profitability and commerciality tests in the legislation as mutually exclusive, and they necessarily overlap to an extent which will vary from case to case."

39. For that reason, in many cases, either both conditions will be satisfied or both conditions will not.

40. However, upon closer examination, it is clear that the conditions are slightly different and that there are cases where one condition has either been accepted by the Respondents as having been satisfied at the same time as the Respondents have mounted a challenge in relation to the other condition or the relevant court has held that one condition has been satisfied but not the other.

41. An obvious difference between the two conditions is that, whereas the condition in Section 66(2)(a) of the ITA is objective in nature, the condition in Section 66(2)(b) of the ITA is subjective in nature, albeit subject to an objectively-measured safe harbour in Section 66(3) of the ITA.

42. The leading authority in relation to the condition in Section 66(2)(a) of the ITA is the decision of Robert Walker J in *Wannell v Rothwell* [1996] STC 450 ("*Wannell*"). At page 461b of that decision, Robert Walker J said as follows:

"I was not shown any authority in which the court has considered the expression "on a commercial basis", but it was suggested that the best guide is to view "commercial" as the antithesis of "uncommercial", and I do find that a useful approach. A trade may be conducted in an uncommercial way either because the terms of trade are uncommercial (for instance, the hobby market-gardening enterprise where the prices of fruit and vegetables do not realistically reflect the overheads and variable costs of the enterprise) or because the way in which the trade is conducted is uncommercial in other respects (for instance, the hobby art gallery or antique shop where the opening hours are unpredictable and depend simply on the owner's convenience). The distinction is between the serious trader who, whatever his shortcomings in skill, experience or capital, is seriously interested in profit, and the amateur or dilettante. There will no doubt be many difficult borderline cases well for the commissioners to decide; and such borderline cases could as well occur in Bond Street as at a car boot sale."

43. Thus, in the view of Robert Walker J, a trade should not be treated as having been carried on "on a commercial basis" if the terms of the trade were uncommercial or if the way in which the trade has been conducted was uncommercial. On the facts in that case, Robert Walker J expressed some doubts about the finding of the Special Commissioner – to the effect that the lack of commercial organisation which had characterised the relevant activity meant that the trade had not been carried on "on a commercial basis" – but he ultimately dismissed the appeal

on the basis that he could not say that the Special Commissioner's decision was perverse or unsupported by the evidence (see *Wannell* at page 461f et seq.).

44. At the same time, Robert Walker J referred to the finding of the Special Commissioner to the effect that "the taxpayer was aiming at profits – quick profits" and noted that it was implicit in what the Special Commissioner had said about the taxpayer's experience and method of operating that the taxpayer "had a reasonable prospect of achieving profits". It is therefore clear that, had he been required to decide the point on the facts in that case, Robert Walker J would have held that the condition in Section 66(2)(b) of the ITA was satisfied even though he did not feel able to disturb the Special Commissioner's conclusion that the condition in Section 66(2)(a) of the ITA was not satisfied.

45. *Wannell* is an example of facts which failed the objective condition in Section 66(2)(a) of the ITA but satisfied the condition in Section 66(2)(b) of the ITA because the taxpayer in that case met both the subjective standard in the latter condition itself and the objectively-measured safe harbour in relation to the latter condition in Section 66(3) of the ITA.

46. A somewhat similar separation between the two conditions was mentioned in the case of *Walls v Livesey (Inspector of Taxes)* [1995] STC (SCD) 12 ("*Walls*"). In that case, a taxpayer had made losses in a commercial property letting trade as a result of a combination of an incompetent agent, an incompetent builder and unexpected adverse economic circumstances. However, prior to starting his trade, the taxpayer had made perfectly sensible financial projections. The Special Commissioner noted in his decision that the Respondents had accepted on the basis of those facts that the trade had been carried on "on a commercial basis" (see paragraph 8 of the decision). It followed that the only issue which needed to be addressed was whether the taxpayer had entered into the trade with "a view to the realisation of profits". The Special Commissioner held that the taxpayer "had neither purpose nor interest in adopting any other course than the realisation of profits". Thus, both conditions were satisfied on the facts in *Walls* but is clear from the decision that the Respondents had accepted that the first condition was satisfied in any event, thereby revealing their acceptance that the two conditions were slightly different in nature.

47. The subjective nature of the condition in Section 66(2)(b) of the ITA is demonstrated by the existence of the objectively-measured safe harbour in Section 66(3) of the ITA. As noted in paragraph 8 above, this stipulates that:

"If at any time a trade is carried on so as to afford a reasonable expectation of profit, it is treated as carried on at that time with a view to the realisation of profits."

48. An inevitable conclusion to be drawn from the existence of that deeming provision is that the condition in Section 66(2)(b) of the ITA can be satisfied in a particular case even if there is no reasonable expectation of profit. As Nugee J observed in *Seven Individuals v The Commissioners for Her Majesty's Revenue and Customs* [2017] STC 874 ("*Seven Individuals*") at paragraph [35]:

"It is true that these provide that if a trade is carried on so as to afford a reasonable expectation of profit, then the profit limb is deemed to be satisfied (s. 384(9) ICTA and s. 66(3) ITA). But it does not follow that if there is no reasonable expectation of profit, the profits limb cannot be satisfied. What is required by s. 384(9) ICTA/s. 66(2)(b) ITA is that the trade is carried on "with a view to the realisation of profits in [or of] the trade". That requirement is looking at the aim or purpose of the relevant person, which is (primarily at least) a subjective question, rather than whether profits could reasonably be expected, which is an objective question. The two are not therefore synonymous - indeed if they were the deeming provisions in s. 384(9) ICTA/s. 66(3) ITA would be of no effect."

49. In *Seven Individuals*, Nugee J referred to the question of whether Section 66(2)(b) of the ITA was satisfied as being "primarily at least…a subjective question" (our emphasis). He did not

say that the question was wholly subjective. In saying this, we believe that he may have been thinking of the decision of the First-tier Tribunal in *Ingenious Games LLP v The Commissioners for Her Majesty's Revenue and Customs* [2016] UKFTT 521 ("*Ingenious FTT*") , to which he referred later in his decision and which had concluded, inter alia, as follows:

"(g) Dextra indicates that there may be some objective element in "with a view to" although in a different statutory context. In the present context "profit" has a meaning independent of what the taxpayer considers it to be: that indicates an objective element in the test: an assessment of whether the intended conduct of the business has a realistic possibility of delivering a profit.

In Vodafone Millett LJ said (742J) that the determination of purpose in section 74 TA 88: "… does not involve an enquiry of the taxpayer whether he consciously intended to obtain a trade or personal advantage by the payment. The primary enquiry is to ascertain what was the primary object of the taxpayer in making the payment. Once ascertained, its characterisation as a trade or private purpose is a matter for the commissioners, not the taxpayer". The same principle applies in relation to the question of whether something is done with a view to profit. The enquiry as to the object of the activity is not into the way in which that object is described at the time or later by the taxpayer.

(h) As a result, if the conduct or intended conduct of the business is such that there is no realistic possibility of profit, the business cannot be said to be carried on with a view to profit, no matter what the subjective intentions of the taxpayer as to profit are.

(i) That objective test is, however, about whether the conduct is such as to give a realistic possibility of profit, not about whether it is businesslike or commercial.

(j) If the conduct of the business is such that it is inevitable or almost certain that a profit will be made that will be the carrying on of the business with a view of profit. We accept Mr Milne's submission that Lord Millett's dictum that purpose is not limited to conscious purpose and that some consequences are so inevitable that they must be taken as a purpose applies here. If it is true for "purpose" it seems to us that it must also apply to "view". If Miss Mallalieu had bought her black clothes with a view to satisfying the court dress rules, it seems inevitable that she must also have bought them with a view to decency and warmth. If a person intends to travel in an aeroplane from London to New York it is inevitable that they will travel with a "view" to crossing the Atlantic Ocean whether or not they consciously considered it when buying a ticket.

(k) Between the two extremes, no realistic possibility of profit and almost inevitable profit, there is a hinterland in which the hopes and expectations of the taxpayer will be a significant factor and where the flexibility of the phrase "with a view to" permits the weighing of the subjective intentions of the taxpayer as to the financial results (not the "profit") of the business and the likelihood of the intended conduct and so those results yielding a profit."

– see paragraphs [492](g) to (k) in *Ingenious FTT*, cited by Nugee J at paragraph [51] of *Seven Individuals*.

50. However, the decision in *Ingenious FTT* has now been superseded by the decision in *Ingenious Games LLP v The Commissioners for Her Majesty's Revenue and Customs* [2019] UKUT 226 (TCC) ("*Ingenious UT*") and it is clear from that decision that the question of whether a person has "a view to the realisation of profits" is wholly subjective in nature. In its decision, the Upper Tribunal said as follows:

"[332] …Nugee J was considering a different test in [Seven Individuals], and was not deciding whether an objective override formed part of the "with a view to profit" test in s 863 ITTOIA, or indeed what was meant by "realistic possibility". He assumed for the purposes of his decision that the FTT in Ingenious was correct in its formulation of the test, without deciding the point. In addition, where he says "it could be said that there was a realistic possibility of profit", the "could" is possibly a qualification rather than an endorsement, and "remote" could relate to the point Nugee J made about the possibility of a profit in year 10, that is a temporal point rather than being a descriptor of the chance of profit. We therefore place no reliance on what was said in Seven Individuals.

[333] We consider the better view to be that the test is a purely subjective one. There is no need for profit to be the predominant aim. As is noted in Lindley & Banks, difficult questions can arise when any profit-making aim is subsidiary to other purposes. In those circumstances, it is necessary to consider at what point the line is crossed and there is in fact no view to profit. Some sort of "reality check" is needed. It is necessary to identify whether there is a "real" intention rather than something that was not, in fact or reality, aimed for. The question as to whether a trade was carried on "with a view to profit" also cannot be answered in isolation, divorced from the context of the business in question. The context of "carries on a trade…" directs attention at least to some extent to the way in which the trade is conducted. Furthermore, an indifference to whether a profit is realised is not sufficient to meet the test. In this case, therefore, the FTT would have had to have been satisfied that the LLPs had genuinely intended to seek a profit from their activities.

[348] …in our view the FTT fell into error in sub-paragraphs [[492]](g) to (k). That follows from our finding that there is no objective element in the test, either as an override which applies even if there is the requisite subjective intention (as suggested by the FTT at sub-paragraph (h)) or as a stand- alone test which has the effect that inevitable or almost certain profit will result in the test being satisfied irrespective of subjective intention (as suggested by the FTT at sub-paragraph (j)). Neither does the test require there to be weighing up of subjective intentions and the likelihood of profit as referred to by the FTT at sub-paragraph (k)."

51. We are therefore bound by *Ingenious UT* to proceed in this appeal on the basis that the test in Section 66(2)(b) of the ITA, before taking into account the objectively-measured safe harbour in Section 66(3) of the ITA, is wholly subjective in nature. Accordingly, there is no basis for concluding that, before taking into account the objectively-measured safe harbour in Section 66(3) of the ITA, whether or not the relevant taxpayer was intending to realise profits from the trade has any objective component whatsoever.

52. That is not to say that the likelihood of profits can never have any relevance to the question of whether the relevant taxpayer has been carrying on the trade with a view to the realisation of profits. As the Upper Tribunal noted in *Ingenious UT* at paragraph [340], "the question is whether there is a real and serious intention to make a profit. As noted at [344] and [345] below, the likelihood of profit may be an element of relevant evidence, but no more."

The Upper Tribunal went on:

"[344] In determining whether there is the requisite subjective intention, all the evidence must be considered. As mentioned in *Gestmin v Credit Suisse* at [22] which we have cited at [342] above, contemporaneous documentary evidence will always be highly relevant. Objective evidence is also relevant and, depending on the context, it may be significant. This may include evidence about whether there was, in fact, a real potential for, or likelihood of, profit. This is not because there is an objective test or override. Rather, the potential for profit is one part of the evidence that may be relevant to determine whether the requisite subjective intention exists.

[345] Where the intention being tested is that of experienced businessmen, the lack of any realistic potential for or likelihood of profit on an objective basis may call into question whether there is a (subjective) view to profit. Experienced businessmen of course take risks, and different individuals will be willing to take differing levels of risk, but businessmen will generally seek to satisfy themselves that the risks are worth taking for the potential return on capital employed, at least if they are risking their own funds. The dynamics may differ where it is someone else's money that is at risk of being lost. HMRC repeatedly submitted that this was a case where the investment was being made with other people's money, namely that of the Exchequer in the form of the monies that the investors expected to receive from HMRC by way of tax repayments. And the extent of the risk taken may depend not only on the risk appetite of the investors but on the degree to which the individuals making the decisions are answerable for any failure, or incentivised by success."

53. We did not find that any of the other cases which were cited to us by the parties provided meaningful guidance on the meaning of the language used in Section 66 of the ITA. The cases

simply involved an application of the principles described above to the facts in the relevant case.

54. For example, the First-tier Tribunal decision in *Mr AW Kerr/Grantham House v The Commissioners for Her Majesty's Revenue and Customs* [2011] UKFTT 40 (TC) is an example of a case like *Walls* where it has been held that, as long as the relevant taxpayer has done all that he can and taken prudent steps to ensure that his or her trade realises profits, he or she will not be precluded from setting off losses which arise in the trade against his general income if those losses arise as a result of unexpected events.

55. Similarly, in the recent decision of the First-tier Tribunal in *Jonathan Beacon v The Commissioners for Her Majesty's Revenue and Customs* [2018] UKFTT 104 (TC) ("*Beacon*"), the First-tier Tribunal effectively dismissed, for lack of evidence, most of the factual contentions which the Respondents had made in that case, including that there was no business plan or business records, that the taxpayer had carried on the trade as an exit strategy from his medical practice instead of for the purposes of realising profits and that customers were charged non-commercial rates for contracting with the taxpayer. The case is therefore of no real assistance in the present circumstances.

56. The decision in *Charles Atkinson v The Commissioners for Her Majesty's Revenue and Customs* [2013] UKFTT 191 (TC) ("*Atkinson*") is of interest only insofar as it also concerned a yacht-chartering business. However, the facts in that case were very different from the ones involved in this appeal. In particular, in *Atkinson*, two separate businesses were being carried on - one by the taxpayer as an individual and the other by a company controlled by the taxpayer - and a significant issue in the decision was the way in which income and expenses were allocated between the two businesses.

Conclusions

57. We have therefore drawn the following conclusions in relation to the two conditions in Section 66(2) of the ITA, taking into account the decisions in the cases set out above:

(1) the condition in Section 66(2)(b) of the ITA can be satisfied in one of two ways – either by reference to the wholly subjective intention of the relevant taxpayer to realise profits from the trade or because, objectively, the trade has been carried on in such a manner as to afford a reasonable expectation of profits;

(2) simply because a trade has not been carried on in such a manner as to afford a reasonable expectation of profits, that will not preclude the condition in Section 66(2)(b) of the ITA from being satisfied if the taxpayer in question had the subjective intention of realising profits, no matter how unreasonable (or detached from reality) the prospects of realising that intention may have been. In other words, as long as the relevant taxpayer intended to make profits from the relevant activity, the fact that there was no realistic prospect that he or she would realise profits from the relevant activity is irrelevant;

(3) the likelihood of profits is relevant in relation to the language in Section 66(2)(b) of the ITA only to the extent that, as an evidential matter, it might call into question the assertion that the relevant taxpayer had a subjective intention to make profits;

(4) the likelihood of profits is much more significant in relation to the objectively-measured safe harbour which applies in the context of the condition in Section 66(2)(b) of the ITA (which is set out in Section 66(3) of the ITA) and in relation to the objective condition in Section 66(2)(a) of the ITA. There is inevitably a greater degree of overlap between those two objectively-worded provisions than there is between the subjective language in Section 66(2)(b) of the ITA and the objective language in Section 66(2)(a) of the ITA;

(5) thus, as the Upper Tribunal said in *Ingenious UT* at paragraph [315]:

"…the "commercial basis" requirement prevents inappropriate use of losses by someone who has little prospect of profit on an objective basis",

and, as the First-tier Tribunal said at first instance in *Acornwood* at paragraph [370]:

"[370] Thus we take the draftsman to have used the phrase "on a commercial basis" to mean in accordance with ordinary prudent business principles, and not in the manner of the amateur or dilettante to which Robert Walker J referred. No business is certain to succeed, and the making of a loss, or of only modest profits, is not necessarily an indication that its proprietor has not pursued the trade on commercial lines. But if, as Mr Blair demonstrated, it can be shown that at the moment the business was started the prospect of recovering the capital invested, even without a surplus, was dependent on the realisation of an unrealistically high profit with the consequence that loss was, if not certain, then much more probable than not, it does not seem to us that it can fairly be said that those embarking on the trade can have entertained a serious profit motive, and their claim to have intended to conduct the trade on commercial lines must, at the least, be doubtful. The amateur may be content to make a loss since the pleasure of the activity is reward in itself; the ordinarily prudent commercial person would not enter into a partnership whose business was more likely than not to result in a loss";

(6) in summary, as Robert Walker J said in *Wannell*, the test in Section 66(2)(a) seeks to distinguish between the "serious trader who… is seriously interested in profit, and the amateur or dilettante";

(7) it follows that it is possible for a taxpayer to embark on a trade intending in good faith to realise profits from the trade but to put his or her intentions into effect so poorly that there is no reasonable prospect of realising those profits. Such a taxpayer might well satisfy the condition in Section 66(2)(b) of the ITA on subjective grounds but fail both to meet the objectively-measured safe harbour in relation to the condition in Section 66(2)(b) of the ITA (which is set out in Section 66(3) of the ITA) and to satisfy the objective condition in Section 66(2)(a) of the ITA; and

(8) the discussion set out at paragraphs [45] to [47] in *Seven Individuals* demonstrates this point clearly – Nugee J rejected the contention made on behalf of the taxpayers in that case that, as long as the relevant taxpayer had a serious interest in making profits and was well-organised, he or she should be able to satisfy the condition in Section 66(2)(a) of the ITA even if the prospect of making profits was remote. Such a taxpayer would clearly meet the condition in Section 66(2)(b) of the ITA but Nugee J said as follows in relation to the relevant taxpayer's ability to satisfy the condition in Section 66(2)(a) of the ITA:

"I do not think it follows that as long as the trade is sufficiently organised and the trader hopes to make a profit…that is always enough. Let us assume that the trade is well organised. The question of whether such a trade is being carried on on commercial lines is not to my mind answered simply by pointing to a hope by the trader to make profits. A trade run on commercial lines seems to me to be a trade run in the way that commercially-minded people run trades. Commercially-minded people are those with a serious interest in profits, or to put it another way, those with a serious interest in making a commercial success of the trade. If therefore a trade is run in a way in which no one seriously interested in profits (or seriously interested in making a commercial success of the trade) would run it, that trade is not being run on commercial lines."

<u>The arguments of the parties</u>

Commercial basis

58. Mr Simpson submitted on behalf of the Respondents that the fact that the Appellant derived a large part of its income from Mr Silver and persons related to him and that the

Appellant was dependent on regular capital contributions from Mr Silver showed that the Appellant was not carrying on its trade "on a commercial basis".

59. In response, Mr Marre submitted on behalf of the Appellant that the Respondents' case was based on a fundamental error – namely, a failure to recognise the inevitable implications of the distinction between, on the one hand, Mr Silver, the individual, and, on the other hand, the Appellant, as a body corporate with a legal personality which was separate and distinct from Mr Silver's.

60. That distinction meant that the fact that the Appellant derived a large part of its trading income from Mr Silver and persons related to him was irrelevant. Mr Silver was simply the Appellant's most significant customer. He paid the Appellant for his charters in the same way as did any other customer of the Appellant. Similarly, there was nothing inappropriate or uncommercial about the fact that the Appellant accepted capital contributions from Mr Silver from time to time. Accepting those capital contributions made sound commercial sense from the Appellant's perspective. It enabled the Appellant to continue to trade despite the losses which it was making.

61. Mr Simpson went on to submit that the manner in which the Appellant had conducted its trade fell within both examples of trades carried on on a non-commercial basis as outlined in *Wannell*. That is to say, the terms of the trade were uncommercial and the way in which the trade was conducted was uncommercial.

62. The terms of the trade were uncommercial, even before depreciation was taken into account, because there was no way in which the expected income from chartering the Yacht would have been able to cover the running costs of the Yacht, leaving aside the additional cost of the depreciation.

63. In addition, the manner in which the Appellant had conducted the trade was amateurish. For example, the Appellant was not insured for charters at all for a long period and then was insured for no more than twelve charters. The Appellant had sought to characterise the failure to insure the Yacht for charters at all as a mistake and, if so, it was a sizeable and amateurish mistake. Leaving uninsured a yacht which was worth over £2m and comprised the only significant asset of the business was behaviour indicative of "the amateur or dilettante" expressly mentioned by Robert Walker J in *Wannell* as being an example of an uncommercial basis and not of the "serious trader" with which those terms were contrasted.

64. Similarly, allowing Mr Silver's son to charter the Yacht for two weeks during two consecutive Augusts was uncommercial. August was the peak season for chartering and that was the time when the Appellant should have been looking to charter the Yacht to persons unrelated to Mr Silver who might become repeat customers. This was akin to the hobby art gallery or antique shop which was closed at peak times to suit the owner's convenience. In effect, that was like having a sandwich shop that closed at lunchtime. It was no wonder that Mr Boyce had strenuously objected to those charters. As for the rate at which the Yacht had been chartered to Mr Silver's son, although Mr Newsholme had described it as commercial in his letter to Ms Griffiths of 28 September 2017, each of the Appellant's three witnesses had conceded in his testimony that it was uncommercial.

65. Finally, the fact that Mr Boyce had been working for both Mr Silver and the Appellant simultaneously, and that his work for Mr Silver was discussed at the meetings which related to the Appellant, showed that the conduct of the Appellant's trade was amateurish. It was irrelevant that financial adjustments were made within the books of the Appellant which had the effect of ensuring that Mr Silver bore the cost of Mr Boyce's work for him. The work which Mr Boyce did for Mr Silver personally should have been kept separate from the work which Mr Boyce was doing for the Appellant.

66. In response, Mr Marre submitted that the great preponderance of evidence suggested that the Appellant had conducted its trade "on a commercial basis".

67. Although the application to the Isle of Man VAT authorities could no longer be located, Mr Silver and Mr Newsholme had testified to the fact that it had contained a comprehensive description of the Appellant's business plan and the Isle of Man VAT authorities had been prepared to approve the Appellant's application for VAT registration on the back of the application.

68. In addition, the Appellant had done all that it could in terms of engaging OBL to find customers, printing its own brochures, maintaining a website and conducting promotional activities (such as taking advantage of promotional articles in magazines) to stimulate business. It had also engaged Mr Boyce in part because of his contacts in the yachting world in order to stimulate custom. There had also been a rigorous attention to the costs incurred by the Appellant, as Mr Boyce had testified. For example, the Appellant had considered finding a new berth for the Yacht which was cheaper than its existing berth.

69. The Appellant had also held regular meetings during the periods of account in question to discuss matters which were relevant to its business. All three of the Appellant's witnesses had testified to the fact that the meetings continued on a regular basis even after Mr Newsholme ceased to minute them as a result of his wife's illness. And, in any event, it was clear from the comments of First-tier Tribunal in *Beacon* at paragraph [45] - referring to comments made by the Administrative Chamber of the Upper Tribunal in *JF v The Commissioners for Her Majesty's Revenue and Customs* [2017] UKUT 334 (AAC) - that, in the case of a small business, expectations as to the quality of records and other documentation needed to be suitably adjusted.

70. In relation to each charter to Mr Silver's son, there was no evidence to the effect that any person other than Mr Silver's son would have been prepared to charter the Yacht for the same or a greater amount than that which had been paid by Mr Silver in relation to the charter. The reason for the inconsistency in the evidence on this point was that the witnesses had been confusing the list rate for chartering the Yacht at any time with the rate which a person who was unrelated to Mr Silver would have been prepared to pay for chartering the Yacht at that time. The latter might well be lower than the former.

71. Moreover, even if the charters to Mr Silver's son were on uncommercial terms, the two charters amounted to only four weeks over two years and therefore only a small part of the period over which the Yacht was available for charter over that period.

72. In addition, there was nothing uncommercial about chartering the Yacht to Mr Silver or persons related to him. Mr Silver was a separate person from the Appellant and was the ultimate repeat customer. As long as he was prepared to pay a commercial rate for each of his charters, then chartering to him made sound commercial sense. And, in any event, Mr Silver had testified to the fact that he tended to charter the Yacht only when no one else wanted to do so.

73. As for the fact that the services supplied by Mr Boyce to Mr Silver had been discussed at meetings of the Appellant, there was nothing uncommercial in that in and of itself. On the contrary, the fact that a proper apportionment of Mr Boyce's fees was made as between the Appellant and Mr Silver showed that, unlike the situation between the two related traders in *Atkinson*, dealings between the Appellant and Mr Silver had been at arm's length.

View to the realisation of profits

74. Mr Simpson submitted that, based on the decision in *Seven Individuals*, the question of whether the Appellant had had a view to the realisation of profits was only primarily, and not

wholly, subjective in nature. There was still an objective element to the test in that it was necessary to determine whether the meaning of the word "profits" was something other than what the Appellant considered it to be – see paragraph [51] in *Seven Individuals*, referring to paragraph [492](g) in *Ingenious FT*. In this case, the fact that the members of the Appellant had failed properly to take into account the impact of depreciation on the profitability of the Appellant showed that the Appellant had failed properly to understand the meaning of the word "profits" and had therefore not had "a view to the realisation of profits" for the purposes of Section 66(2)(b) of the ITA.

75. In response, Mr Marre submitted that the evidence of all three of the Appellant's witnesses demonstrated that the sole intention of the Appellant was to realise profits from chartering out the Yacht. Thus, putting the Appellant's case in relation to the second condition at its worst, the Appellant's expectation of realising profits was merely a bit optimistic. If the number of charters which OBL had predicted had proved accurate and the Appellant had also been able to negotiate its own additional charters, both of which did not happen, largely as a result of the recession, then the Appellant might have been able to make profits. Moreover, as the Yacht had been modified to such a high specification, it was less susceptible to depreciation than might otherwise have been the case. This meant that the likelihood of the Appellant's realising profits was somewhat greater than the accounts depreciation might have suggested.

76. Mr Marre added that the Respondents had accepted that, in the periods of account of the Appellant preceding the periods of account which were relevant to this appeal, the Appellant's trade was "commercial" for the purposes of Section 66 of the ITA. And, as the test in Section 66 of the ITA had to be applied on a year by year basis and nothing about the trade had changed after those preceding periods of account, logic suggested that the trade must have been "commercial" for those purposes in the later periods of account too.

77. In response, Mr Simpson pointed out that, as Mr Thomas had testified in his evidence, the Respondents had not accepted that the Appellant had satisfied the test in Section 66 of the ITA in each of the periods of account that preceded the periods of account which were relevant to this appeal. Instead, it was just that no-one within the Respondents had ever got around to examining the position in relation to those earlier periods of account before the enquiries into the later tax years were opened.

FINDINGS OF FACT

78. We found each of the witnesses to be honest and helpful and saw no reason to doubt the credibility of any of them.

79. In the light of their testimony and the other evidence with which we have been provided, we make the following findings of fact:

(1) contrary to the submissions made by Mr Simpson on behalf of the Respondents, we find as a fact that the Yacht was acquired by Mr Silver for the sole purpose of using the Yacht to carry on the trade of chartering. It was not Mr Silver's intention at any time that he would use the Yacht for his own private purposes. We say that because we believed Mr Silver when he said that the Yacht was acquired for that purpose and that he wouldn't have acquired a yacht with such high specifications if he had intended to use it for his own private purposes;

(2) similarly, we accept the evidence of all three of the Appellant's witnesses to the effect that, and find as a fact that, far from being acquired by the Appellant for the purpose of obtaining income to defray the costs which were going to be incurred in using the Yacht, the Yacht was acquired by the Appellant for the purpose of generating profits for the Appellant from chartering out the Yacht;

(3) we also accept the evidence of those witnesses to the effect that the Appellant did a number of things which were consistent with carrying on a business in a commercial manner. For example, we find as a fact that:

(a) the Appellant produced a business plan for submission to the Isle of Man VAT authorities as part of its application for VAT registration in the Isle of Man;

(b) Mr Silver consulted with OBL prior to placing his order for the Yacht in order to form a view on the prospects for chartering out the Yacht once acquired;

(c) the Appellant did not rely solely on the efforts of OBL to charter out the Yacht but instead made efforts to secure such charters on its own – for example, by appointing Mr Boyce, printing brochures and taking advantage of promotional articles in magazines. In this context, there was a dispute between the parties' respective witnesses as to whether the Appellant's website was kept up to date after 2011. Whilst very little turns on the point, given the other promotional efforts which were made by the Appellant, we should record that we saw no documentary evidence to support either the proposition that the website was kept up to date after 2011 or the converse proposition and therefore we cannot and do not make a finding of fact on that point either way;

(d) there were regular meetings to discuss the affairs of the Appellant (albeit that the affairs of Mr Silver were also discussed at some of those meetings and that the documentation of those meetings following Mr Newsholme's wife's becoming ill was not all that it could have been); and

(e) strenuous efforts were made to control the Appellant's costs at all times, including the costs of berthing the Yacht;

(4) however, we also find as a fact that there were some serious deficiencies in the manner in which the Appellant conducted its trade;

(5) first and foremost, the Appellant failed properly to take into account the impact on the profitability of the trade which would inevitably arise from the depreciation in the value of the Yacht. Mr Newsholme said that he thought that, despite the depreciation, the Appellant would still be able to generate sufficient charter income to cover both the running costs and the depreciation, whilst Mr Silver said that he expected that any shortfall between the Appellant's income and expenses as a result of the depreciation would be covered by goodwill arising as a result of the conduct of the trade;

(6) however, even on the most optimistic projection for charter income, the possibility that the trade would generate a profit for the Appellant, once depreciation was taken into account, was remote. Based on the evidence of Mr Silver, when he placed the order for the Yacht, assuming that the Yacht could be chartered out in both the Mediterranean and the Caribbean each year, charter income of between £180,000 and £250,000 per annum might be expected to arise. However, when one looks at the accounts of the Appellant, it becomes apparent that even that amount of charter income was highly unlikely to exceed the expenses of the business once depreciation was taken into account;

(7) for example, the accounts of the Appellant reveal that, in its first four periods of account, the expenses of the business, including depreciation, were £308,960, £303,695, £259,744 and £261,326. Of course, accounts depreciation is not necessarily the same as actual depreciation but Mr Silver conceded in his undated letter to Ms Griffiths mentioned in paragraph 23(8) above that the expected depreciation over the first three years of the business did match the accounts depreciation in this case;

(8) in any event, this appeal does not turn on the expectations of Mr Silver and Mr Newsholme at the time when the Yacht was ordered. The test in Section 66 of the ITA has to be applied on a period of account by period of account basis and the tax years to which this appeal relates are the tax year ending 5 April 2012 and the following four tax years. It is therefore necessary to consider the position as it stood in each of the period of account ending 30 April 2011 and the following four periods of account;

(9) when one does that, it becomes plain that, by the time of the relevant period of account, regardless of the reasons why it was the case, the initial expectations of Mr Silver and Mr Newsholme as to the likely amount of charter income had been shown to be wildly wrong. This is because the charter income in each of the periods of account preceding the relevant period of account were nowhere near the figures mentioned in paragraph 79(6) above. Even Mr Silver acknowledged (in paragraph 37 of his witness statement) that, by the time of the meeting of the Appellant on 30 April 2009, "we knew [the Appellant's trade] was unlikely to be profitable";

(10) in addition, the Yacht had been taken to the Caribbean only once, in the winter of 2009/2010. It was never taken to the Caribbean again after that. It should therefore have been apparent to Mr Silver and Mr Newsholme throughout each period of account which is relevant to this appeal that the initial expectation that the Yacht would be capable of being chartered out in the Caribbean for a number of weeks each year was never going to be realised. That inevitably meant that the Yacht would be available for chartering out only over the summer season in the Mediterranean, which in turn meant that the Appellant would be even less capable of meeting its expenditure than had been the expectation at the inception of its trade. Indeed, the fact that, once it was noticed that the Appellant was not insured in respect of the Yacht during charter periods at all, the insurance arrangements were modified to allow for no more than twelve charters each year, strongly suggests that no more than twelve charters per annum were expected. And, even if one assumes that some of those charters could have been for more than a week, the expected level of charter income which would be generated by twelve charters per annum would inevitably fall well short of the expenditure, including depreciation, which must have been expected to arise;

(11) for that reason, we find as a fact that, in the periods of account which are relevant to this appeal, the prospects of the Appellant's realising any profits from the trade were remote and that a sensible businessman, acting rationally, should have realised that. The fact that profits were so unlikely to arise means that Mr Marre's submission at the hearing to the effect that the Appellant's expectation of profits was merely "a bit optimistic" was, in our view, something of an understatement and wide of the mark;

(12) in addition, in the circumstances, with such a significant gap between anticipated income and anticipated expenditure, we can see no justifiable basis for Mr Silver's expectation that the Appellant would generate any goodwill at all, let alone sufficient goodwill to remedy the losses which the trade had been generating and would clearly continue to generate;

(13) in addition to the discrepancy between expected income and expected expenditure noted above, the Appellant made a serious error in failing to insure the Yacht for charters into which it entered prior to 2011. By the time of the periods of account which are relevant to this appeal, that error had been cured by changing the terms of insurance in order to allow for cover for up to twelve charters each year and, in that respect, we accept Mr Silver's evidence that the intention was that additional cover could be purchased in the event that the Appellant was able to obtain more than twelve charters in any year. Nevertheless, we noted at the hearing that the insurance documentation which we saw

was in the name of Mr Silver and not the Appellant and we believe that this was a further error in the way in which the Appellant's trade was conducted as regards the insurance. At the hearing, Mr Marre suggested that the policies should be regarded as having been taken out by Mr Silver as agent for, or on trust for, the Appellant but we have been provided with no evidence to suggest that that was the case. We have therefore concluded that, if it had been necessary for the Appellant to make a claim under the policies at any point during the periods of account in question, there was a meaningful risk that the relevant insurer would have been able successfully to refuse to reimburse the Appellant for the loss in question, on the basis that the Appellant itself was not the insured person;

(14) there was a dispute between the parties as to whether the charter rates which were paid by Mr Silver for the charters by his son were commercial rates. Mr Silver paid £15,000 for the two week charter in August 2009 and £12,000 for the two week charter in August 2010. Although these amounts were considerably lower than the list price for the relevant periods – which were between £12,000 and £14,000 per week in August 2009 and £15,500 per week in August 2010, in each case according to the OBL charter rates in tab 21 of the Documents Bundle - we agree with Mr Marre that there is a big difference between list price and market price. A much more pertinent question is whether a higher price could have been obtained at each relevant time from a person unrelated to Mr Silver;

(15) in that respect, we have noted that:

(a) the Yacht was chartered for nine days between 29 July 2010 and 7 August 2010 to a Mr and Mrs Blythe for £9,000 and for a week between 8 August 2010 and 15 August 2010 to a Mr France for £6,000. It was again chartered to Mr France for a week between 21 August 2011 and 28 August 2011 for £6,000. Mr and Mrs Blythe and Mr France were not related in any way to Mr Silver;

(b) the Yacht was also chartered to two other persons unrelated to Mr Silver over periods which might shed some light on this question – it was chartered to Land Investment Jaroslaw Fijalkowski for two weeks between 13 July 2010 and 27 July 2010 for £16,800 and to an individual or entity called Raber for six days between 13 August 2011 and 19 August 2011 for EU 13,500;

(c) Mr Silver said in his testimony that, for the periods that his son was chartering the Yacht, no one else had offered to charter the Yacht at the same or a higher price; and

(d) the dispute between Mr Boyce and Mr Silver in relation to the charters to Mr Silver's son appears - from the evidence of Mr Boyce and Mr Newsholme and the letter from Mr Newsholme to Ms Griffith of 28 September 2017 - not to have related to the rates paid by Mr Silver for the charters but rather to the fact that, in the view of Mr Boyce, a customer other than Mr Silver's son should have been preferred;

(16) on the other hand:

(a) the minutes of the meeting held on 6 August 2009 referred to the fact that OBL had confirmed that they "could have sold August charters at least twice over. Future consideration has to be to ensure that [non] commercial charters are kept to a minimum during periods when commercial charters are at a premium". This suggested that non-commercial charters were being implemented, at least on and before August 2009; and

(b) each of the charters referred to in paragraph 79(15) above related to 2010 or 2011. We have been provided with no comparators for August 2009;

(17) after taking all of this evidence into account, we have concluded, on balance, that:

(a) the charters to Mr Silver's son in August 2009 and August 2010 were very likely to have been at rates which were reasonably comparable to the commercial rates at the relevant times – that is to say, the rates which could have been obtained at the relevant time from persons unrelated to Mr Silver;

(b) however, there were potentially customers who were unrelated to Mr Silver who may been prepared to charter the Yacht for approximately the same rates at the relevant times; and

(c) therefore, the dispute between Mr Boyce and Mr Silver mentioned in paragraph 79(15)(d) above did not relate to the rates paid by Mr Silver for the charters but rather to the fact that, in the view of Mr Boyce, a customer other than Mr Silver's son should have been preferred; and

(18) there was also a dispute between the parties in relation to the fact that Mr Boyce provided services to both the Appellant and Mr Silver over the periods of account in question. On the basis of the evidence of the witnesses, we find as facts that:

(a) Mr Boyce did perform services for both the Appellant and Mr Silver over those periods;

(b) the discussions between the parties at the meetings in relation to the Appellant included discussions in relation to the services which Mr Boyce was providing to Mr Silver as well as discussions in relation to the services which Mr Boyce was providing to the Appellant; and

(c) Mr Silver bore the costs associated with the services which Mr Boyce provided to him by virtue of the fact that Mr Newsholme recorded those costs in the books and records of the Appellant as drawings by Mr Silver.

DISCUSSION

The Procedural Issue

80. The two questions which we need to address in relation to the Procedural Issue are as follows:

(1) first, did the argument in question form part of "the [Respondents'] position in relation to the case" as set out in the Statement of Case, as is required by Rule 25(2) of the Tribunal Rules; and

(2) secondly, if it did not, would it nevertheless be fair and just to allow the Respondents to adduce the argument at this stage?

81. We consider that it is clear from the terms of the communications from the Respondents described in paragraphs 29(1) to 29(6) above that the Respondents were seeking to challenge the availability of the losses in question for offset against Mr Silver's general income in respect of the tax years in question under both limbs of Section 66(2) of the ITA. Moreover, the language used in the "Grounds for appeal" section of the Appellant's Notice of Appeal to the First-tier Tribunal of 14 March 2018 demonstrated that the Appellant clearly understood this to be the case because that language referred to the fact that "[the Appellant] was in business with a view to profit and the business was commercial". Thus, again, both limbs of the section were mentioned.

82. It is against that background that the Respondents' Statement of Case needs to be considered.

83. In that regard, we would make the following points:

(1) it is unfortunate that the legislation in question is not drafted particularly clearly. There are in fact two headings to the section – one in italics, which refers to a "[restriction] on relief for uncommercial trades", and the other in bold, which refers to a "[restriction] on relief unless trade is commercial". They are followed by Section 66(1) of the ITA, which explains that relief against general income will be precluded "unless the trade is commercial". It is therefore clear at that stage of reading the provision that the section is imposing a single test and only a single test – namely, is the trade "commercial"? At that point, Section 66(2) of the ITA makes it clear that, in order for that single test to be satisfied, and for a trade to be "commercial", two conditions need to be satisfied. The first condition is worded in language which is very similar to the single test itself – because it requires one to consider whether the trade has been carried on "on a commercial basis" – whilst the second condition is worded in language which echoes the phrase used in the very definition of a limited liability partnership in Section 2 of the LLPA – because it requires one to consider whether the trade has been carried on "with a view to the realisation of profits";

(2) it can be seen that there is very little difference between, on the one hand, the language used to describe the first condition in the test and, on the other hand, the language used to describe the test itself. And this similarity clearly confused the person who drafted the Statement of Case because it is apparent that he or she failed to appreciate the distinction between the first condition in the test and the test itself. This can be seen at various points in the Statement of Case – for example, in the contrast between, on the one hand, paragraph 3.1, which says that the point is issue is "[was] the partnership Roulette V2 LLP trading commercially to satisfy S66 Income Tax Act 2007…" and, on the other hand:

(a) paragraph 8.1, which says that the matter in dispute is "[has] the yacht charter partnership been carried out on a commercial basis"; and

(b) paragraph 11.1, which says that "HMRC request the Tribunal to find that the partnership was not operated on a commercial basis";

(3) it is quite clear to us from:

(a) that contrast; and

(b) the references to the absence of an expectation of profits which are scattered throughout the Statement of Case – see, for example, paragraphs 10.3, 10.4, 10.6 and 10.8; and

(c) the rather odd reference to Section 66(2)(b) of the ITA in paragraph 10.1, in the context of a reference to whether or not the trade was run "on a commercial basis",

that the person drafting the Statement of Case had only the vaguest idea as to how Section 66 of the ITA operates;

(4) the difficult question for us is whether that means that the Respondents should be confined to fighting this appeal on the single ground that the Appellant did not satisfy the first condition in Section 66(2)(a) of the ITA or whether there is enough in the Statement of Case as it stands, despite the incompetent way in which it has been drafted, to lead to the conclusion that the Appellant should have deduced that the Respondents were still

intending to fight this appeal on the grounds of both conditions in Section 66(2) of the ITA;

(5) although we are somewhat reluctant to allow the Respondents to prosper despite the clear inadequacies in their Statement of Case, we have ultimately reached the view that the latter conclusion is the better one;

(6) we start from the fact that the Statement of Case needs to be read in the light of the correspondence which preceded the Notice of Appeal and the language used in the Notice of Appeal itself. All of that prior documentation made it clear that both conditions, and not simply the first condition, in Section 66(2) of the ITA were in dispute;

(7) we then note that that there are, in our view, sufficient references in the Statement of Case to the absence of a view to a profit and to the fact that there are two limbs to the test in Section 66(1) of the ITA – see, in addition to the references mentioned in paragraph 83(3) above, the references in paragraph 10.9 of the Statement of Case to "the conditions of S66" (our emphasis) – to suggest that, after reading the Statement of Case in the light of all that had preceded it, the Appellant should have been aware that the second condition in Section 66(2) of the ITA was still in play. There is certainly nothing in the Statement of Case which ever approaches a direct expression on the part of the Respondents that they were conceding that the second condition was satisfied;

(8) in our view, this means that the Appellant's argument that it approached the hearing in the belief that the Respondents had conceded that the second condition in Section 66(2) of the ITA had been satisfied by the Appellant in this case is unsustainable. This is certainly not a case like *Allpay Limited v The Commissioners for Her Majesty's Customs and Excise* [2018] UKFTT 273 (TC), where the "payment services issue" (as it was described by the First-tier Tribunal in that case) was not mentioned at all in the relevant Statement of Case and therefore the appellant was entitled to assume that the issue had been conceded. Here, there were, in our view, sufficient references to the absence of a view to the realisation of profits in the Statement of Case to lead to the conclusion that the second condition in Section 66(2) of the ITA, if not expressly pleaded, was at the very least impliedly pleaded, in the Statement of Case. It is far from "litigation by ambush", as the term was used in *BPP v The Commissioners for Her Majesty's Customs and Excise* [2014] UKFTT 644;

(9) for these reasons, we have concluded that the Statement of Case should be construed in such a way that it can properly be said to have set out, expressly or at the very least impliedly, the Respondents' view that neither condition, and not solely the first condition, in Section 66(2) of the ITA was satisfied in this case; and

(10) however, even if we might be said to be wrong in law in construing the Statement of Case in that way, we think that these are circumstances where fairness and justness dictate that the Respondents should be allowed to argue in this appeal that the second condition, as well as the first condition, in Section 66(2) of the ITA has not been satisfied. To decide otherwise would be to fly in the face of the language used in the Statement of Case and all the documentation which preceded the Statement of Case. It does not seem fair or just to us for the Appellant to be able to avoid any consideration by us of the second condition on the ground that it thought that the Respondents had conceded the point. Thus, to the extent that it is necessary for us to exercise our discretion under Rule 7(2) of the Tribunal Rules to allow the Respondents to challenge the availability of the losses in question for offset against the general income of Mr Silver on the basis that Section 66(2)(b) of the ITA has not been satisfied in this case, we hereby do so.

The Substantive Issue

84. Given the conclusion set out in paragraph 83 above, there are two questions which we need to address in relation to the Substantive Issue. These are as follows:

(1) in each of the relevant periods of account of the Appellant, was the Appellant carrying on its trade "on a commercial basis" for the purposes of Section 66(2)(a) of the ITA? and

(2) in each of the relevant periods of account of the Appellant, was the Appellant carrying on its trade "with a view to the realisation of profits" for the purposes of Section 66(2)(b) of the ITA?

Realisation of profits

85. We will start our discussion of the Substantive Issue with the second of the two questions, as it is the easier of the two to address on the present facts.

86. In our view, given that it has now been determined by the Upper Tribunal in *Ingenious UT* that the second question is wholly subjective in nature, the answer to that question on the present facts is a resounding "yes".

87. We say that because, based on the evidence summarised in paragraphs 17 to 26 above, and the findings of fact which we have made in paragraph 79 above, it is quite clear that it was the subjective intention of the Appellant, as determined by reference to the intentions of both members of the Appellant – and, for that matter, Mr Boyce – that the chartering trade carried on by the Appellant during each of the periods of account in question should give rise to profits. That subjective intention was not that the income derived by the Appellant from its activities might defray some of the costs which would inevitably be incurred in maintaining and running the Yacht.

88. It follows inexorably from that conclusion that, in each of the relevant periods of account of the Appellant, the Appellant was carrying on its trade "with a view to the realisation of profits" for the purposes of Section 66(2)(b) of the ITA. This is because, in answering this question, subject to the evidential point to which we refer below, we are obliged to look solely at the state of mind and intentions of the members of the Appellant and to conclude that the realisation of profits condition is satisfied as long as they intended to realise profits in the trade. We are not required to consider whether that intention was reasonable or realistic. Those are considerations which would be relevant if reliance were sought to be placed on the safe harbour in Section 66(3) of the ITA but they have no place in applying the language in Section 66(2)(b) of the ITA. As Nugee J said in *Seven Individuals* at paragraph [35], "it does not follow that if there is no reasonable expectation of profit, the profits limb cannot be satisfied".

89. That is not to say that the likelihood (or otherwise) of profits is wholly irrelevant in considering this question. In reaching the conclusion set out above, we have applied the injunction in paragraphs [340], [344] and [345] of *Ingenious UT* – which are set out in paragraph 52 above - to take into account the likelihood (or otherwise) of profits as an element of the evidence in determining whether the relevant subjective intention existed. However, in this case, we are satisfied that, regardless of the lack of likelihood of profits, the subjective intention of the Appellant in carrying on its trade was to realise profits.

Commercial basis

90. The likelihood (or otherwise) of profits is much more relevant in answering the question set out in paragraph 84(1) above. This is because the cases summarised in paragraphs 36 to 57 above demonstrate that, if a taxpayer "has little prospect of profit on an objective basis" (see *Ingenious UT* at paragraph [315]), then he cannot be said to be carrying on the trade "on a

commercial basis" for the purposes of Section 66(2)(a) of the ITA. Indeed, we think that Mr Marre implicitly recognised that an expectation of profits is crucial to the conclusion that the trade is being carried on "on a commercial basis" when he submitted, in relation to the Procedural Issue, that the references in the Statement of Case to the absence of an expectation of profits were no more than the recognition by the Respondents that an expectation of profits was an integral part of satisfying the first condition.

91. It may be seen from the extract from *Wannell* cited at paragraph 42 above that, in each case, the relevant court or tribunal needs to determine whether the taxpayer in question falls to be regarded as "the serious trader who, whatever his shortcomings in skill, experience or capital, is seriously interested in profit" or, in contrast, as "the amateur or dilettante". As the decision in *Wannell* demonstrated, the mere fact that the relevant taxpayer is aiming at profits is not sufficient, in and of itself, to justify the conclusion that the taxpayer is carrying on the trade "on a commercial basis". For example, in *Wannell*, the fact that the relevant trade was being carried on in a manner which lacked commercial organisation meant that it was not being carried on "on a commercial basis" despite the intention to derive profits from the trade.

92. The facts in this appeal are more nuanced than those in *Wannell* in that, as we have outlined in paragraph 79(3) above, there were many respects in which the Appellant conducted its trade in a manner which one would expect from a commercial trader. We have concluded that the Appellant took a number of steps to increase its profits, whether by generating additional charter income or by trying to cut its expenses. In addition, regular meetings were held to discuss the ongoing conduct of the trade.

93. We also accept the proposition that Mr Silver was a customer of the Appellant in the same way as any other customer and that he was, in fact, the ultimate repeat customer. Moreover, we have not been presented with any evidence which establishes on the balance of probabilities that Mr Silver paid less than a commercial rate for the charters to him and persons related to him. We therefore see nothing uncommercial in the fact that the Yacht was chartered to Mr Silver and persons related to him, even in the case of the charters to Mr Silver's son in August 2009 and August 2010.

94. However, the Appellant also displayed a considerable degree of ineptitude in the manner in which it conducted its trade. We agree with Mr Simpson that failing to insure the Yacht for charters – which was the case prior to 2011 - is an example of amateurish conduct. So too, in our view, is the fact that the insurance was at all times taken out by Mr Silver himself and not by the Appellant. In our view, those errors are not dissimilar to the four month delay by the limited liability partnership in *Rowbottom* in getting the relevant vessel appropriately licensed for chartering – see *Rowbottom* at paragraph [54].

95. More importantly, we have concluded that, in the periods of account of the Appellant which are relevant to this appeal, the prospects of the Appellant's realising any profits from the trade were remote. By the time of each of those periods of account, it should have been absolutely clear to the members of the Appellant that the charter income was highly unlikely ever to cover the running expenses of the Appellant, even before depreciation was taken into account. And, once depreciation was taken into account, the prospects of the trade's giving rise to profits were remote. (This perhaps might explain the somewhat curious advice which Mr Ashdown is recorded as having delivered to the Appellant at the meeting to which reference is made in paragraph 17(4) above. One might have thought that a trader which was carrying on its trade on a commercial basis would not need to be advised that "charter income needs to be as high as possible" or that "[the] income box on the VAT return should be higher than the cost box as often as possible".)

96. Taking that into account, we have concluded that, although we do not accept the Respondents' submission to the effect that the sole purpose of the Appellant in carrying on its activities was to generate income in order to defray some of the costs which were going to be incurred in relation to the Yacht, we do not think that the Appellant has satisfied us that it was carrying on its trade "on a commercial basis", for the purposes of Section 66(2)(a) of the ITA. Instead, we think that a sensible trader in the position of the Appellant within each of the periods of accounts which are relevant to this appeal would immediately have brought the trade to an end and mothballed the Yacht. This was a conclusion which the Appellant eventually reached in October 2017 but we think that a prudent trader – that is to say, a trader carrying on its trade on a commercial basis - would have reached the conclusion considerably sooner than the Appellant in fact did.

97. In short, in this case:

(1) to paraphrase the words of Robert Walker J in *Wannell*, the terms of the trade were uncommercial – because there was no way in which the charter income would be able to cover the expenses of the Appellant – and the manner in which the trade was conducted was, at least in certain respects, amateurish. In our view, these deficiencies went beyond a mere shortcoming in skill, experience or capital; and

(2) to paraphrase the First-tier Tribunal in *Acornwood* at paragraph [370], losses in this case were assured and therefore the claim to have conducted the trade on commercial lines must be doubtful. The ordinarily prudent commercial person would not have continued to carry on the trade in circumstances where the prospects of profits were so remote.

CONCLUSION

98. For the reasons set out above, we have concluded that, in relation to each of the periods of account which are relevant to this appeal, the Appellant did not carry on its trade "on a commercial basis" for the purposes of Section 66(2)(a) of the ITA, with the consequence that, even though it was carrying on the trade "with a view to the realisation of profits" for the purposes of Section 66(2)(b) of the ITA, its trade was not "commercial" for the purposes of Section 66(1) of the ITA. As a result:

(1) the trading losses which arose in the Appellant and were allocable to Mr Silver in respect of the tax years in relation to which the periods of account were the basis periods were not available to be set off against Mr Silver's general income in respect of those tax years; and

(2) the Appellant's appeal is dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

99. 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 Rules. 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.

TONY BEARE
TRIBUNAL JUDGE

RELEASE DATE: 15 AUGUST 2019