Analysis

Tax law rewrite: *Scambler* on looking back to ICTA 1988

Speed read

In *Scambler v HMRC*, the Upper Tribunal sets out when it is permissible to look to the previous legislation to help interpret Tax Law Rewrite (TLR) statutes. There are only two 'gateways': real and substantial difficulty in interpreting the TLR provisions; and ambiguity which cannot be resolved by normal methods. These are narrower than the gateways to consider *Hansard*. 'Ambiguity' here has a precise meaning: where words are reasonably capable of bearing two or more distinct interpretations, rather than a single interpretation which might or might not apply because it has vague edges. It is also possible to go back to the original use of legislation in order to understand its context: *Scambler* does not affect that.

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A key objective of consolidating legislation, like the TLR project, is 'to gather disparate provisions into a single, easily accessible code' (*Eclipse Film Partners (No. 35) LLP v HMRC* [2013] UKUT 639 (TC), para 97). That objective would be seriously undermined were one to be faced with the uncertainty and expense of going back to ICTA 1988 (or trudging back further through decades of earlier legislation) to decipher today's meaning. But even where the TLR project was not in itself intended to change tax law, the TLR statutes use different words to aim to deliver the same meaning. When can taxpayers or HMRC look to the past? There is undoubtedly experience of HMRC seeking to rely on earlier legislation, e.g. the TMA 1970 predecessors to bulk powers in FA 2011 Sch 23. The Upper Tribunal in *Scambler* [2017] UKUT 1 (TCC) considered just this issue and resolved an ambiguity in ITA 2007 by reference to the predecessor provision in ICTA 1988.

The ambiguity in *Scambler*

Scambler is not a business tax case. For many readers, it will be relevant only for its statutory interpretation principles: another tool in the toolbox for when interpretation is difficult.

The Scamblers were dairy farmers who claimed sideways loss relief in their 2010/11 self-assessment tax returns. HMRC denied their claims on the basis of the restrictions on sideways loss relief in ITA 2007 ss 67 and 68. The Scamblers appealed unsuccessfully to the FTT, and again to the Upper Tribunal. Uncertainty arose as to the meaning of 'the activities' in ITA 2007 s 68(3)(b).

Under s 67(2), the Scamblers were not eligible for sideways loss relief because their farming trade had made losses in each of the five previous tax years. However, s 67(3)(b) provided an exception to this exclusion if their farming activities met the 'reasonable expectation of profits test'. That test is in s 68(3)(a) and (b), and is met when:

a. a competent person carrying on the activities in the current tax year (year 2010/11 in the Scamblers' case) would reasonably expect future profits; but
b. a competent person carrying on *the activities* at the beginning of the prior period of loss (year 2005 in the Scamblers' case) could not reasonably have expected those activities to become profitable until after the end of the current tax year (year 2010/11).

Significantly, the Scamblers had made material changes to their dairying activities between 2005 and 2010. The issue thus arose as to the meaning of 'the activities' in s 68(3)(b). Which activities did a competent person have to have expected to remain unprofitable until 2011? Did it mean the activities performed in 2005 or (if they had been carried on in 2005) the activities now performed in the current tax year 2010/11? The FTT had held that it meant the activities in 2005. The Upper Tribunal concluded that both meanings were tenable interpretations of s 68(3)(b), and thus ambiguity arose.

Prior case law on the issue confirms that different views were possible. An *obiter* statement in *French v HMRC* [2014] UKFTT 940 (TC) indicated 'the activities' in s 68(3)(b) to mean the earlier activities. Importantly, the FTT noted that its decision would have been different had the words 'the activities' been 'those activities', which would have clearly tied the reference to activities back to the activities in s 68(3)(a), namely the current ones. *Erridge v HMRC* [2015] UKFTT 89 (TC) interpreted 'the activities' to mean the activities in the current tax year, but in the context of the beginning of the prior period of loss. *Silvester v HMRC* [2015] UKFTT 532 (TC) followed the approach in *French*, distinguishing *Erridge* on its facts.

Both the Scamblers and HMRC accepted there was real difficulty in interpreting the literal words of s 68(3)(b). The Scamblers argued the ambiguity could be resolved by reference to ministerial statements under the rule in *Pepper v Hart* [1992] STC 898. HMRC submitted that the ambiguity could be resolved by reference to the antecedent statutory provision in ICTA 1988 s 397(3).

The 'gateways' to the previous law

The Upper Tribunal approved the approach to interpretation of TLR consolidation statutes taken by the FTT in *Shirley v HMRC* [2014] UKFTT 1023 (TC). Therefore, this is the first full and authoritative decision on the point. The discussion in *Eclipse* was thin.

The Upper Tribunal starts with a normal approach to the statute. You should examine the actual language used in the consolidation statute itself without reference to any of the statutes it has replaced. You should take a normal approach to statutory interpretation, giving consideration to the 'clear words' of the statute. Ascertaining the 'clear words' is not confined to literal interpretation and must consider the context and scheme of the Act as a whole, and its purpose.

And you can then only adopt an interpretation that the statutory language is reasonably capable of bearing.

It then considers whether to look back. It held that this can only then be done when either:

- there is 'real and substantial difficulty in interpreting the provisions'; or
- 'there is ambiguity which classical methods of construction cannot resolve'.

These are the 'gateways'. Having determined that the meaning of 'the activities' in s 68(3)(b) was 'ambiguous', the Upper Tribunal did turn to ICTA 1988. The Upper Tribunal explained this by citing *Shirley*, itself citing *Eclipse*, which relied on non-tax case *Farrell v Alexander* [1977] AC 59, for the proposition that, where a consolidated provision to be interpreted is ambiguous, there is 'a subordinate presumption … that it is presumed that there was no intention to change the meaning of the provision which has been repeated in the same language in the consolidated code'.

The provision antecedent to ITA 2007 s 68(3)(b), namely ICTA 1988 s 397(3)(b), did refer to 'those activities', the very clue that the FTT in *French* had wished for. This resolved the ambiguity by clearly tying the reference to 'the activities' to those in the current tax year in s 68(3)(a). However, notwithstanding the Upper Tribunal taking a different view to the FTT on this point, the Scamblers' appeal again failed because, on the FTT's finding of fact, Mr Scambler's evidence could not satisfy the reasonable expectation of profits test.

Because the Upper Tribunal was able to resolve the ambiguity by reference to the antecedent legislation, it was not necessary to consider the Scamblers' submission to examine ministerial statements under the rule in *Pepper v Hart*. However, the Upper Tribunal went on to say that, in any event, in its view the three *Pepper v Hart* conditions were not satisfied in this case. While the legislation was ambiguous and the material to be relied on consisted of statements by a minister, those statements were not sufficient to clearly favour one interpretation.

Finally, the Upper Tribunal considered a further and related issue of interpretation. The cross heading to ITA 2007 ss 67 to 70 referred to 'Restriction on relief for "hobby" farming or market gardening'. This cross heading appeared for the first time in the ITA 2007. The Upper Tribunal gave short shrift to the Scamblers' argument that the restrictions on sideways loss relief did therefore not apply to them as commercial farmers: headings, even if clear and unambiguous, are generally of very limited use in interpretation because they are necessarily brief and inaccurate in nature.

Applying the gateways

There are three important points about the gateways.

For the second gateway, the Upper Tribunal appears to have given 'ambiguity' its precise meaning; namely, where words are reasonably capable of bearing two or more distinct interpretations, rather than a single interpretation of uncertain scope because it has vague edges. *John Hudson v Kirkness* (1955) 36 TC 28 is House of Lords authority that a provision is ambiguous not because it merely contains a word which in different contexts is capable of different meanings, but because it contains a word or phrase which in a particular context is open to two perfectly clear and plain interpretations.

For the first gateway, the meaning of 'real and substantial difficulty' is unclear. It appears to be narrower than the *Pepper v Hart* test for considering *Hansard*. That is because in *Shirley* (at paras 57 to 58), the FTT rejected HMRC's attempt to rely on earlier legislation to avoid an interpretation which would result in 'injustice, absurdity, anomaly or contradiction, or [which] stultifies or runs counter to the statutory objective', being the phrase used by Lord Simon in *Farrell v Alexander*. However, in *Shirley* the FTT noted that where an interpretation leads to injustice etc., a literal interpretation may be inappropriate even without having regard to antecedent provisions. The FTT then gave a clue to the interrelationship between the gateways, that an anomaly might lead to a conclusion that the legislation *is* in fact ambiguous in the particular context.

The gateways to previous legislation are narrow, but they do exist

It also seems to have been important to the Upper Tribunal that there was specific evidence that the TLR had not meant to change the law here. It referred specifically to the explanatory notes, which in relation to ITA 2007 s 68 stated: 'It is based on section 397(3) and (5) of ICTA'; other explanatory notes referred specifically to provisions being new or making a change to existing legislation. In practice, this means that if ICTA 1988 (or other earlier legislation) does look helpful to your preferred interpretation, it will be critical to check the explanatory notes to the consolidating provision, and the destination tables (e.g. in *Tolley's Yellow Tax Handbook* Part 3), to support your argument that the consolidation provision has not changed the law. Provisions such as Capital Allowances Act 2001 Sch 3 Part 1 do not help – that makes clear that the 'continuity' of the law on rewriting applies only if the law has not been changed.

Other reasons to look back

The clarification in *Scambler* is not exhaustive. Most importantly, it does not affect the need to consider the context in which the earliest 'antecedent' provision was passed when the purpose of the consolidated rule (here, TLR) is not clear. As in the non-tax case *Ex parte Spath Holme Ltd* [2001] 2 AC 349, where legislation does not indicate its purpose or the circumstances in which it should apply, the court is unable to put itself in the 'draftsman's chair' without considering the earlier provision in its social and factual context. This may be a wider test.

Need to know

As we said above, the substantive provisions in *Scambler* are of narrow interest. The importance of the case is in clarifying the tools available to resolve difficulties, in any part of the seven TLR statutes (or other rewritten legislation). The gateways to previous legislation are narrow, but do exist. But absent one of those, or a *Spath Holme* situation, for taxpayer and HMRC it remains a case of 'don't look back in anger' – at least, not today. ■

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