

Loan relationships

(Lecture B1102 – 8.40 minutes)

In the recent case of *CJ Wildbird Foods Ltd v HMRC* (2018), the First-Tier Tribunal has found for the taxpayer and, in doing so, held that loans to a company, which were not being serviced or repaid, still constituted loan relationships. Accordingly, debits for impairment losses were available for corporation tax purposes.

The appeal concerned a series of inter-company loans advanced by CJ Wildbird Foods Ltd (WF) to Birdforum Ltd (BFL), in which WF held a 50% interest, over the years ended 31 March 2013, 2014 and 2015. These loans, which totalled approximately £150,000 each year, followed similar loans which had been advanced in earlier years. The issue in dispute was whether, as a result of these loans and in the light of the surrounding circumstances, the amounts advanced represented loan relationships for the purposes of Part 5 of CTA 2009 such that a deduction should be allowed to WF in respect of the write-down of these loans. BFL had no income and consequently lacked the wherewithal to pay interest and to make repayments of the sums lent. HMRC denied the debits for impairment in WF's corporation tax returns.

HMRC contended that there was no loan relationship because there was no money debt. They argued that the amounts owing did not bear the hallmarks of a loan in order to fall within the definition of a money debt. HMRC also referred to *Smart v Lincolnshire Sugar Company Ltd* (1937) in relation to the question of whether there was a transaction for the lending of money, given that the borrower might never be able to repay the amounts advanced. In their arguments, HMRC maintained that WF's advances of money were not arm's length transactions bearing any resemblance to the commercial reality of a loan relationship and that their preferred analysis was that the payments were akin to capital contributions and therefore disallowable for corporation tax purposes.

However, the First-Tier Tribunal decided that the advances made were, in law, repayable with interest and so the loans clearly constituted a money debt. The advances were shown in the accounts as due and owing and, while they had been provided for in full (and WF had not yet demanded repayment), they had not been legally written off, ie. formally released. The judge went on to find that there was a clear contractual agreement between the parties that interest was payable at an agreed rate on the moneys advanced. There had been no specific waiver of that arrangement – merely an agreement that there was no point in the interest actually being charged unless and until funds were available to pay it.

In relation to whether there was a transaction for the lending of money, the First-Tier Tribunal distinguished the present case from *Smart v Lincolnshire Sugar Company Ltd* (1937) as involving significantly different facts. Even though, at the time when the advances were made, the borrower could not repay the amounts, the judge considered that this situation had now become relatively commonplace in a number of commercial scenarios – as was the lack of a fixed repayment date – and that neither factor should prevent the loans from being treated as loan relationships.

In his summing up, he said:

'The modern business world has many famous examples of companies, especially in the technology sector, with no cash and no immediate prospect of generating a profit which go on to be very successful. Clearly, the appellant considers BFL potentially to be such a company and is therefore prepared to subsidise its running costs by way of loan for the time being in the hope of obtaining repayment of some or all of its loans in due course, possibly with a gain on its share investment as well.'

Contributed by Robert Jamieson