OUTER HOUSE, COURT OF SESSION

[2021] CSOH 38

P796/20

OPINION OF LORD TYRE

In the petition of

NIALL ADRIAN FINUCANE

Petitioner

for

Judicial Review of the lawfulness of the charges imposed by Her Majesty's Commissioners for Revenue and Customs under reference to schedule 11 and schedule 12 to the Finance (No 2) Act 2017

Petitioner: O'Neill QC, Welsh: Balfour & Manson LLP
Respondents (HM Revenue & Customs): Simpson QC, MacIver: Office of the Advocate General for Scotland

14 April 2021

Introduction

[1] The petitioner is an airline pilot. He is a citizen of Ireland and Switzerland. Between 2001 and 2014 he worked for Ryanair and was based at Prestwick. His contractual arrangements were operated on behalf of Ryanair by an English-registered company called Brookfield Aviation International Limited ("Brookfield").

[2] The petitioner states that in 2008 he was informed that he would henceforth be treated as providing his services to Ryanair not as an employee but as a self-employed individual. He believes that this was done to bring advantage to Ryanair by removing him

from the statutory protections afforded to employees. He was given no choice in the matter. He took legal advice and tax advice as to how best to deal with his new enforced self-employed status. In particular, he sought tax advice from AM Limited ("AML"), a company based in the Isle of Man. He was advised to enter into a "loan scheme", which he did. As explained more fully below, this arrangement provided for payments by Brookfield for the petitioner's work for Ryanair to be made initially to AML and later (following a change in tax law) to another Isle of Man entity (the AML Partners Collective Company). Those entities paid small amounts by way of salary (or, later, payment for services) to the petitioner and also advanced loans to him which amounted to the bulk of the payments received from Brookfield. Income tax was paid by the petitioner in the United Kingdom on the salary/services payments but not on the loans.

[3] The respondents ("HMRC") have for many years regarded loan schemes of this kind as a form of tax avoidance. The effectiveness of such schemes for avoiding tax on the amounts of the loans has been challenged in court proceedings and, since 2011, by a series of statutory enactments intended to nullify any tax advantage that might be obtained were the schemes to be held to be otherwise effective. As a consequence, the use of loan schemes has declined, but by 2016 significant amounts of loans remained outstanding and untaxed. In order to recover tax on those amounts, the Finance (No 2) Act 2017 introduced a charge, known as the loan charge, to be levied on the amounts of any loans outstanding as at 5 April 2019.

[4] In these proceedings, the petitioner seeks declarator that the loan charge imposed in 2017 is unlawful and in any event unable to be applied against him because (a) it constitutes an unjustified infringement of and interference in the fundamental EU law principle of free movement of capital: and (b) it is incompatible with the EU law

prohibitions against the retrospective imposition of penalties and, separately, the imposition of penalties which are disproportionately severe.

[5] The application came before me for a substantive hearing. At a previous permission hearing I had granted permission for the application to proceed out of time. Affidavits were lodged by the petitioner and by another former Ryanair pilot and, on behalf of HMRC, by Ms Jacqueline McGeehan, HMRC Deputy Director with responsibility for income tax policy, and Mr Steven McFarlane, an HMRC officer with responsibility for dealing with loan schemes operated by AML.

[6] The petitioner founds upon various rights under EU law. In relation to the United Kingdom's withdrawal from the EU, the following were not in dispute:

- Any EU law rights which were recognised and available before withdrawal continue to be recognised and available thereafter (European Union (Withdrawal) Act 2018, section 4):
- The principle of supremacy of EU law continues to apply to any enactment passed before the completion date (ibid, section 5(2)):
- The Charter of Fundamental Rights ("CFR") is no longer part of domestic law (ibid, section 5(4)), but can still be relied upon in these proceedings because they were commenced but not finally decided before the completion date (ibid, schedule 8, paragraph 39(3)):
- A general principle of EU law (such as, in the context of these proceedings, the principle of fiscal legality) is part of domestic law on or after the completion date only if it was recognised as a general principle of EU law by the European Court in a case decided before the completion date (whether or not as an essential part of the decision in the case) (ibid, schedule 1, paragraph 2):

- Any question as to the meaning or effect of any retained EU law is to be decided, so far as that law is unmodified on or after the completion date in accordance with retained case law and retained general principles of EU law (ibid, section 6(3)).

Loan schemes: a brief description

[7] In her affidavit, Ms McGeehan described loan schemes (or, as she termed them, "disguised remuneration schemes") as follows. Beneficiaries of loan schemes provide their labour and expect reward in return. A significant part of the expected reward is paid as a loan or advance to the individual, frequently from a third-party vehicle such as a trust. This loan is claimed not to be taxable as income in the way that the earnings of an employee or profits of a self-employed person would be. The individual is free to spend the money in the same way as any other income and will rarely make any provision for repayment of the loan. Such schemes were first used by large employers in the 1990s to deliver what was purported to be tax-free pay and bonuses to their employees. Later, smaller employers used them to reward directors and employees. The schemes typically diverted money through structures such as employee benefit trusts and employer funded retirement benefit schemes. There were also similar arrangements based on trading, where the contractor was a self-employed sole trader or in a partnership. These arrangements reduced the income of the trade by diverting monies or claiming a deduction from the business profits, with the amounts deducted being paid over to what was known as a "self-employed remuneration trust". The trust would then make a loan to the individual trader which was not expected to be repaid. Ms McGeehan's description of a loan scheme based on trading is consistent with

the petitioner's account of the arrangements into which he entered for the tax years 2011-12 to 2014-15:

> "In 2011, the petitioner became a member of the AML Partners Collective Company ('PCC'). As a partner of PCC, the petitioner became a beneficiary of the Partners Benefit Trust. As such, he was able to benefit from the trust fund. Knox House Trustees Limited is a company registered on the Isle of Man. Knox House Trustees Limited acted as trustee of the PCC Partners Benefit Trust. Knox House Trustees Limited was accordingly the lender for the purposes of loans made from the scheme to the petitioner."

[8] In HMRC's view, loan schemes were not effective to avoid income tax on the amounts advanced to the employee or trader. That view, however, was not initially shared by the courts. In *Dextra Accessories Ltd* v *HM Inspector of Taxes* [2002] STC (SCD) 413 and in *Sempra Metals Ltd* v *HMRC* [2008] STC (SCD) 1062, it was held by the Special Commissioners that loans from employee benefit trusts were not chargeable to income tax. It was not until 2017 that the Supreme Court held in *RFC 2012 plc* v *Advocate General* 2018 SC (UKSC) 1 that *Dextra* and *Sempra Metals* had been wrongly decided. In the meantime, the Government had proceeded to secure the enactment by Parliament of targeted anti-avoidance legislation.

Statutory provisions

[9] Needless to say, the legislation is complex. For present purposes it is sufficient to explain the overall effect of the charging provisions. In the first of these, the Finance Act 2011 inserted a new Part 7A into the Income Tax (Earnings and Pensions) Act 2003 ("ITEPA"). These provisions imposed a charge to income tax (and national insurance contributions) on the full value of a loan made to an employee, or to a related party, by a third party such as a trust. Anti-forestalling rules applied the charge to transactions after 9 December 2010, when a ministerial statement announcing the new charge had been made. Otherwise the charge was not retroactive. It was subject to various exceptions, including in

particular an exception for loans made on ordinary commercial terms with no connection to a tax avoidance arrangement. There were further exceptions for, eg, self-invested pension schemes and SAYE savings schemes. As regards loans made before 9 December 2010, HMRC continued to challenge these under other, pre-existing statutory provisions.

[10] The 2011 legislation was intentionally wide-ranging, and many employers stopped using the kinds of loan schemes targeted by it. Scheme promoters, however, continued to attempt to devise schemes that would fall outside the scope of the 2011 provisions. These included schemes in which the recipient of the loans was self-employed instead of employed. Legislation to combat the use of loan schemes in the context of self-employment was introduced by the Finance (No 2) Act 2017 by means of insertion of sections 23A to 23H into the Income Tax (Trading and Other Income) Act 2005 ("ITTOIA"), again without retroactive effect.

[11] After 2011, HMRC attempted by various means to encourage users of pre-2011 loan schemes to settle what were perceived to be their tax liabilities. Those attempts achieved only limited success and individual usage of loan schemes began to rise again. By 2015, HMRC were seeking to devise a new strategy for recovering the income tax and national insurance contributions that they perceived to be due in respect of outstanding loans received under both pre- and post-2011 schemes. The solution that HMRC chose to adopt was the loan charge. The stated purpose of the loan charge was, quite simply, to shut down the use of loan schemes by requiring affected taxpayers to do one of three things, namely to settle their perceived liabilities, to pay off the loans, or to pay the loan charge.

[12] Legislation imposing the loan charge is in schedules 11 and 12 to the Finance (No 2) Act 2017 (as subsequently amended). Schedule 11 applies to loans received by employees: schedule 12 to loans received by self-employed persons. The effect of each of these sets of

provisions is that the amount of any loan falling within the scope of the legislation which was outstanding as at 5 April 2019 became chargeable to tax at that time. As originally enacted, the legislation applied to loans made at any time since 1999. One effect of bringing all outstanding loans into charge in a single tax year was to bring some of those affected into a higher tax bracket than would have been applicable if the loans had been charged to tax in the years in which they were received. This was intended to encourage recipients to pay tax (and interest) on the basis that the loans had been chargeable when received (including paying tax for years in respect of which assessment would now be out of time). Both schedules contained provisions excluding loans not connected with a tax avoidance arrangement or the obtaining of a tax advantage.

[13] The introduction of the loan charge led to an outcry among those affected by it. Many of those were individuals who had participated in a loan scheme on the basis of assurances by scheme promoters that it "worked" and would not be challenged by HMRC. They had organised their financial affairs on the assumption that they would not be required either to pay tax on the loans or to make repayment of them to the lender, and did not now have the funds needed to pay the charge, especially as a lump sum in a single tax year. The retrospectivity of the charge, covering a period of 20 years, and its application to sums received during years which could not now otherwise be brought into charge to tax, were unusual features that were perceived to be particularly unfair. In many cases there had been little or no direct communication between HMRC and the affected individuals for a lengthy period of time, and intimation of a liability to pay a large amount of tax came as a severe shock.

[14] In response to these concerns, the Government commissioned an independent review by Sir Amyas Morse, the former Comptroller and Auditor General, of the policy and

implementation of the loan charge. In December 2019 the report of the Morse review was published. It contained a list of 20 recommendations, all except one of which the Government accepted and undertook to implement. Among the recommendations accepted were the following:

(i) the loan charge should not apply to loans entered into before 9 December 2010:

(ii) in respect of loans entered into after 9 December 2010, the charge should not apply to "unprotected years", ie years in respect of which no investigation had been opened by HMRC, provided that the taxpayer had made reasonable disclosure to HMRC of their use of a loan scheme (with other "unprotected years" remaining within its scope):

(iii) taxpayers should be allowed to spread their outstanding loan balances over a period of 3 years, in order to mitigate the impact of stacking the liabilities in a single tax year, thereby creating increased exposure to a higher rate of tax.

Implementation of those recommendations was effected by amendments made to schedules 11 and 12 to the Finance (No 2) Act 2017 by the Finance Act 2020. That, in broad outline, is how the law stood at the time of commencement of the present petition.

[15] In the course of the hearing it was submitted on behalf of the petitioner that when addressing the issues raised I should have regard not only to the law as it stood at the date when the petition was commenced but also to the law as it had stood before the changes made in implementation of the Morse recommendations. I reject that submission. The petitioner has no standing to challenge legislative provisions that were repealed before the time when the loan charge became payable and which cannot now affect him, or indeed anyone else.

The petitioner's circumstances

[16] The petition contains detailed averments about steps taken by the petitioner to find a "suitable solution" to the problems created by Ryanair's decision to treat him as self-employed. He avers *inter alia* that he was advised by AML that he had no alternative to using a loan scheme if he was to continue to work for Ryanair as a now self-employed contractor and continue paying tax in the UK; that he was not familiar with the details of the way in which the AML loan scheme would operate; and that he relied on assurances by AML that the loan scheme was a lawful tax efficient scheme known to and approved by HMRC. He admits that he was paid a small salary by AML and that he received loans of substantial amounts "on beneficial terms". He asserts that tax mitigation was not his motivation for entering into the scheme. He avers that he has no reasonable prospect of being able to pay the sum now sought by HMRC, and that he has been placed under financial and emotional strain by the UK Government's attempts "to coerce him into reaching a settlement by the threat of the imposition with retrospective effect of the penalty that is the loan charge".

[17] I have no reason to doubt the petitioner's averments in relation to what he was told by AML, and it may be noted in this context that the Morse review was highly critical of scheme promoters who provided their customers with misleading information about the attitude of HMRC to loan schemes. It is important to note, however, that the petitioner's challenge is to the lawfulness of the loan charge generally, and is not specific to its application to his personal circumstances, except in so far as these are material to his EU law arguments. It is clearly relevant to those arguments that the petitioner was at the time a non-UK national with an establishment in the UK, being paid for his service (or services) by entities resident in the Isle of Man, but his averments as to his personal motivation and as to

the adverse effects of the loan charge upon him are of little or no relevance to the issues that I have to decide. Nor, for the same reason, are certain averments by the petitioner, disputed by HMRC, as to what he was told during telephone conversations with revenue officials.

[18] It is also necessary to emphasise that the petitioner expressly claims to have standing to bring these proceedings "as an individual who is affected by the charge imposed by schedule 11 and schedule 12" to the Finance (No 2) Act 2017. Those schedules do not apply unless (in the case of schedule 11) there is a connection between the loan and a tax avoidance arrangement or (in the case of schedule 12) a tax advantage is obtained as a result of the loan arrangement. On behalf of the respondents it was submitted that the petitioner must therefore be taken to concede:

- in relation to the scheme in which he participated in tax years 2009-10 and 2010-11, either (a) that the loan was not on ordinary commercial terms or (b) that there was a connection (direct or indirect) between the failure to repay the loan and a tax avoidance arrangement, or (c) both of those: and
- in relation to the scheme in which he participated in tax years 2011-12 to 2014-15, that it is reasonable to suppose that he would obtain a tax advantage as a result of the scheme.

I agree that this must follow. It also follows, in my view, that in considering the petitioner's attack on the legislative provisions based upon rights under EU law, it must be borne in mind that the relevant context is loans entered into in connection with tax avoidance arrangements and not loan transactions more generally.

The issues

[19] The petition and answers raise the following issues for decision:

(i) Whether this application for judicial review is incompetent because the petitioner has an alternative remedy in the form of an appeal to the First-tier Tribunal against any assessment in relation to the loan charge:

(ii) Whether the loan charge constitutes an interference with the petitioner's right to free movement of capital:

(iii) Whether the petitioner's reliance on the right to free movement of capital is an abuse of EU law rights:

(iv) Whether the loan charge constitutes a breach of the EU principle of fiscal legality:

(v) Whether the loan charge amounts to a disproportionately severe and retrospective penalty.

I address each of these issues in turn.

Issue (i): competency of the application for judicial review

Argument for HMRC

[20] It was submitted on behalf of HMRC that the application should be refused as incompetent, because the petitioner had a statutory remedy that he had failed to exhaust. The petitioner had available to him the usual procedure for challenging an assessment to tax, namely an appeal to the specialist tax tribunals under section 31 of the Taxes Management Act 1970. It was accepted that no assessment in relation to the petitioner's liability to pay the loan charge had yet been made: that might simply be because the charge had only recently fallen due. If, however, an assessment was made, the petitioner could

appeal against it and present all of the arguments made in this petition to the First-tier Tribunal and in any subsequent appeal from that tribunal's decision. Reference was made to *Autologic Holdings plc* v *IR Commrs* [2016] 1 AC 118 and *R (Glencore Energy UK Ltd)* v *HMRC* [2017] 4 WLR 213. It would additionally be open to the petitioner in such proceedings to present arguments based upon his personal circumstances which were not being presented in the application for judicial review.

Argument for the petitioner

[21] On behalf of the petitioner, it was submitted that there was no substance to HMRC's contention. As was recognised, there was no assessment or closure notice currently extant that the petitioner could challenge by appeal under the Taxes Management Act 1970, and therefore no alternative remedy for him to exhaust before coming to this court. More fundamentally, HMRC's argument failed to recognise that the present application was a constitutional law judicial review rather than an administrative law judicial review, raising questions of whether the enactment by the legislature of the loan charge legislation, and its operation by HMRC, was or was not compatible with EU law. These were clearly matters of and for constitutional judicial review: cf *R* v *Secretary of State for Transport, ex parte Factortame (No 2)* [1991] 1 AC 603 and *R* v *Secretary of State for Transport, ex parte Factortame (No 3)* [1992] QB 680 (ECJ). Constitutional judicial review fell within the experience and expertise of judges of this court acting as a constitutional court. They were not matters which fell within the experience or expertise of an administrative tribunal with no inherent jurisdiction, such as the Tax Chamber of the First-tier Tribunal. The issue was one of appropriateness, not competency. It would not be appropriate to delay resolution of the

matters raised by requiring them to be argued again in a tax appeal which might not be heard until years from now.

Decision

[22] In my opinion, HMRC's argument is well founded. Although the nature of the petitioner's challenge could be described as constitutional, in so far as it seeks a declaration that certain provisions of UK tax legislation are unlawful because they breach principles of EU law, the critical fact that gives him standing is that he is resisting a charge to income tax that he expects to be made upon him. That, in my view, is a matter whose resolution has been allocated by Parliament to the specialist tax tribunals. The relationship in England and Wales between judicial review and the tax tribunals was recently considered by the Court of Appeal in the *Glencore* case (above), in which Sales LJ (with whom the other members of the court agreed) observed:

> "[54] …The [alternative remedy] principle does not apply as the result of any statutory provision to oust the jurisdiction of the High Court on judicial review. In this case the High Court (and hence this court) has full jurisdiction to review the lawfulness of action by the Designated Officer and by HMRC. The question is whether the court should exercise its discretion to refuse to proceed to judicial review (as the judge did at the permission stage) or to grant relief under judicial review at a substantive hearing according to the established principle governing the exercise of its discretion where there is a suitable alternative remedy.
>
> [55] In my view, the principle is based on the fact that judicial review in the High Court is ordinarily a remedy of last resort, to ensure that the rule of law is respected where no other procedure is suitable to achieve that objective. However, since it is a matter of discretion for the court, where it is clear that a public authority is acting in defiance of the rule of law the High Court will be prepared to exercise its jurisdiction then and there without waiting for some other remedial process to take its course. Also, in considering what should be taken to qualify as a suitable alternative remedy, the court should have regard to the provision which Parliament has made to cater for the usual sort of case in terms of the procedures and remedies which have been established to deal with it. If Parliament has made it clear by its legislation that a particular sort of procedure or remedy is in its view appropriate to deal with a standard case, the court should be slow to conclude in its discretion that the public

interest is so pressing that it ought to intervene to exercise its judicial review function along with or instead of that statutory procedure. But of course it is possible that instances of unlawfulness will arise which are not of that standard description, in which case the availability of such a statutory procedure will be less significant as a factor.

[56] Treating judicial review in ordinary circumstances as a remedy of last resort fulfils a number of objectives. It ensures the courts give priority to statutory procedures as laid down by Parliament, respecting Parliament's judgment about what procedures are appropriate for particular contexts. It avoids expensive duplication of the effort which may be required if two sets of procedures are followed in relation to the same underlying subject matter. It minimises the potential for judicial review to be used to disrupt the smooth operation of statutory procedures which may be adequate to meet the justice of the case. It promotes proportionate allocation of judicial resources for dispute resolution and saves the High Court from undue pressure of work so that it remains available to provide speedy relief in other judicial review cases in fulfilment of its role as protector of the rule of law, where its intervention really is required.

[57] In my judgment the principle is applicable in the present tax context. The basic object of the tax regime is to ensure that tax is properly collected when it is due and the taxpayer is not otherwise obliged to pay sums to the state. The regime for appeals on the merits in tax cases is directed to securing that basic objective and is more effective than judicial review to do so: it ensures that a taxpayer is only ultimately liable to pay tax if the law says so, not because HMRC consider that it should. To allow judicial review to intrude alongside the appeal regime risks disrupting the smooth collection of tax and the efficient functioning of the appeal procedures in a way which is not warranted by the need to protect the fundamental interests of the taxpayer. Those interests are ordinarily sufficiently and appropriately protected by the appeal regime. Since the basic objective of the tax regime is the proper collection of tax which is due, which is directly served by application of the law to the facts on an appeal once the tax collection process has been initiated, the lawfulness of the approach adopted by HMRC when taking the decision to initiate the process is not of central concern. Moreover, by legislating for a full right of appeal on fact and law, Parliament contemplated that there will be cases where there might have been some error of law by HMRC at the initiation stage but also contemplates that the appropriate way to deal with that sort of problem will be by way of appeal."

I have set out these observations at length because they appear to me to be equally applicable to the supervisory role of the Court of Session, and also to be particularly apposite to the facts of the present case. They acknowledge that the issue is not one of jurisdiction but of discretion, and explain the reasons why the court should, in exercise of its discretion, decline to exercise its supervisory function in relation to a matter that has clearly been directed by Parliament to be dealt with by a different statutory process.

[23] Sales LJ went on in *Glencore* to contrast the circumstances of that case with those of *In re Preston* [1985] 1 AC 835. In that case a taxpayer sought judicial review of a decision of the Inland Revenue Commissioners to inquire into his tax affairs, on the ground that he had previously reached an agreement with an inspector of taxes that no further inquiries would be made, provided that he withdrew certain claims for relief. The House of Lords held that the issue was amenable for judicial review because it amounted to an allegation of abuse of power that would not have fallen within the jurisdiction of the tax appeal tribunal. I respectfully agree that the contrast is helpful in illustrating circumstances in which recourse is properly made to the supervisory jurisdiction: a similar contrast may be made between *Preston* and the present case.

[24] There was a suggestion in the petitioner's written note of argument, not pursued in oral argument, that consideration of the EU law issues raised in the petition would be beyond the jurisdiction of the First-tier Tribunal. It was also contended that these were matters beyond the experience and expertise of such a tribunal. I reject both of these contentions. As regards jurisdiction, it is beyond any doubt that the tax tribunals can, and indeed must, make findings in relation to EU law issues raised by parties (and could until the UK's departure from the European Union have made references to the Court of Justice for preliminary rulings). This was made clear by Lord Nicholls of Birkenhead, delivering one of the majority judgments in *Autologic Holdings plc* v *IR Commrs* (above) at paragraphs 16 and 17:

> "[16] The second basic principle concerns the interpretation and application of a provision of United Kingdom legislation which is inconsistent with a directly applicable provision of Community law. Where such an inconsistency exists the

> statutory provision is to be read and take effect as though the statute had enacted that the offending provision was to be without prejudice to the directly enforceable Community rights of persons having the benefit of such rights. That is the effect of section 2 of the European Communities Act 1972, as explained by your Lordships' House in *R* v *Secretary of State for Transport, Ex p Factortame Ltd* [1990] 2 AC 85, 140, and *Imperial Chemical Industries plc* v *Colmer (No 2)* [1999] 1 WLR 2035, 2041.
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> [17] Thus, when deciding an appeal from a refusal by an inspector to allow group relief the appeal commissioners are obliged to give effect to all directly enforceable Community rights notwithstanding the terms of sections 402(3A) and (3B) and 413(5) of ICTA. In this regard the commissioners' position is analogous to that of the Pretore di Susa in *Amministrazione delle Finanze dello Stato* v *Simmenthal SpA* (Case 106/77) [1978] ECR 629. Accordingly, if an inconsistency with directly enforceable Community law exists, formal statutory requirements must where necessary be disapplied or moulded to the extent needed to enable those requirements to be applied in a manner consistent with Community law…"

[25] As regards experience and expertise, it is not in my view for this court to decide, where Parliament has directed that appeals against tax assessments are to be heard by the specialist tax tribunals, that some of these are unsuitable for those tribunals because they raise questions of the supremacy of EU law. Even though the facility of reference for a preliminary ruling is no longer available, there is no basis whatever for treating a dispute as inappropriate for hearing by the First-tier Tribunal (with the usual rights of further appeal) simply because an issue characterised by the taxpayer as "constitutional" has been raised.

[26] In relation to arguments based on expediency, it would be unrealistic for me not to recognise that there are broader interests in these proceedings than the tax affairs of the present petitioner. As is noted in HMRC's answers, the petitioner appears to have the support of a group entitled "Loan Charge Judicial Review European Union". That group's website refers to one, and possibly two, "lead cases" in Scotland: it is reasonable to infer that this petition is one of them, and that there are therefore other taxpayers with potential liability to pay the loan charge to whom the outcome of the present challenge is of considerable interest. (Reference is also made on the website to judicial review proceedings

raised in England.) The question is whether I should regard this wider interest as a reason to allow this application to proceed, thereby providing a decision now rather than requiring all concerned to await the outcome of an appeal (perhaps not yet even commenced) to the First-tier Tribunal. I am not persuaded that the fact that there are other taxpayers with similar interests affects the rationale set out in the observations of Sales LJ in *Glencore* for refusing to entertain an application. In my view the present application amounts to an attempt to pre-empt consideration of the issues raised by the tribunals appointed by Parliament to hear such issues. I see no reason in principle why a particular group of aggrieved taxpayers should be accorded favourable treatment in this way. It may be that those co-ordinating the challenge to the loan charge see advantage in obtaining a court declarator in general terms, as opposed to hoping for a favourable decision capable of general application in an appeal to a tribunal by a particular taxpayer. The difference may however be more apparent than real. Any declarator by this court would be pronounced against the factual circumstances of the petitioner, and it seems to me that the relevance of such a declarator to the affairs of other taxpayers would be no less uncertain than the relevance of the reasoning of an appeal tribunal.

[27] On behalf of the petitioner, reference was made to *dicta* pronounced in various cases including *Ruddy* v *Chief Constable for Scotland* 2013 SC (UKSC) 126, *Taylor* v *Scottish Ministers* 2019 SLT 288, and *Keatings* v *Advocate General for Scotland* 2021 CSOH 16, to support an assertion that HMRC's alternative remedy argument was "vexatious" and "an abuse of process". It suffices to say that all of the *dicta* referred to were pronounced in very different contexts and afford no support for this assertion.

[28] For these reasons I hold that it is not appropriate for this court to entertain the petitioner's application for judicial review and that it falls to be dismissed. However, as I

was fully addressed on the substantive issues, and in case the matter goes further, I will express my opinion on them.

Issue (ii): whether the loan charge constitutes an interference with the petitioner's right to free movement of capital

[29] Article 63.1 of the Treaty on the Functioning of the European Union ("TFEU") states:

> "Within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited."

Article 65.1 TFEU then provides:

> "The provisions of Article 63 shall be without prejudice to the right of Member States:
>
> (a) to apply the relevant provisions of their tax law which distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where their capital is invested:
>
> (b) to take all requisite measures to prevent infringements of national law and regulations, in particular in the field of taxation and the prudential supervision of financial institutions, or to lay down procedures for the declaration of capital movements for purposes of administrative or statistical information, or to take measures which are justified on grounds of public policy or public security."

[30] There are two separate questions within this issue. The first, referred to by the petitioner as the "threshold issue", is whether the petitioner's circumstances are such as to entitle him to the protection of the EU right to free movement of capital. The second is whether the circumstances of the case are such that, as a matter of fact, that right is engaged, ie whether there is a movement of capital to which the protection is capable of being applied.

[31] There was no dispute regarding the first of those questions. As already noted, the petitioner is a non-UK EU citizen established in the UK and working in the UK for an Irish

company. Where, as here, the right founded upon is a free movement right, it is unnecessary to identify a specific statutory provision implementing EU law in order to found the right. The circumstances described are clearly sufficient to engage the petitioner's free movement rights, including the right to free movement of capital. It is unnecessary in the petitioner's case to address the question whether the interposition of an entity resident in the Isle of Man (a "third country" for the purposes of article 63) is of importance. It was not conceded by HMRC that a UK national would satisfy the threshold issue.

Argument for the petitioner

[32] The real dispute is as to whether the operation of the loan scheme constitutes a movement of capital. On behalf of the petitioner it was submitted that the loans made to him were, in form, fact and law, loans and not gifts. There was nothing artificial about them. They could be called in for repayment. This was not re-directed income and not therefore within the scope of the *RFC 2012 plc* decision. There was no trust mechanism. On a proper analysis, AML contracted with Brookfield that *inter alia* the petitioner would provide services as a consultant pilot and made a profit through the provision of contracted consultants. From those accumulated profits within AML, AML made loans. By its nature, a loan is not income. The loan capital remained capital unless and until the monies transferred were not in a loan but a gift. There was a movement of capital from AML in the Isle of Man to the petitioner in the UK.

[33] EU law gave a wide definition to the word "capital" in the context of article 63. In the classification of nomenclature for the purposes of Annex 1 to Council Directive 88/361/EEC, capital movements are taken to cover *inter alia* "operations to repay credits or loans", and the list of capital movements includes short, medium and long term financial loans and

credits. Reference was made to *Ritter-Coulais* v *Finanzampt Germersheim* [2006] ECR I-1737, in which a wide definition of capital was evident. *A fortiori* the loans in these proceedings were capital. Even if the loan capital fell to be regarded as being "revenue" in nature, that did not prevent the free movement of capital provisions from being engaged. In *Sandoz* v *Finanzlandes-direktion für Wien, Niederösterreich und Burgenland* [1999] ECR I-7041, the Court of Justice determined that legislation which deprived Austrian residents of the possibility of benefiting from the absence of taxation associated with loans obtained outside Austria was likely to deter them from obtaining such loans, and therefore constituted an obstacle to the free movement of capital.

Argument for HMRC

[34] On behalf of HMRC it was submitted that article 63 had no application to the petitioner's circumstances. It was clear from his averments that the loan schemes were conduits through which flowed the money paid by Ryanair in respect of his work as a pilot, starting at Ryanair and ending at the petitioner. Whatever unusual elements may have been inserted into that structure, the movements were entirely income earned by working.

[35] Article 63 contained no definition of a capital movement. The classification in Council Directive 88/361/EEC did not indicate that all loans were capital. On the basis of Court of Justice case law, it was clear that:

- free movement of capital is a freedom based on the "object of the transaction rather than on the nature of the persons who carry them out": *Persche* v *Finanzamt Ludenscheid* [2009] ECR I-359, Advocate General (Mengozzi) at paragraph 35;

- movements of capital are financial operations essentially concerned with investment rather than remuneration for a service: *Luisi and Carbone* v *Ministero del Tesoro* [1984] ECR 377, paragraphs 19 to 22;
- in order to determine whether national legislation falls within the scope of one or other of the freedoms of movement, the purpose of the legislation concerned must be taken into consideration: see eg *Persche* v *Finanzamt Ludenscheid* (above), paragraph 28;
- if the purpose of the legislation does not determine that issue, then, "account should be taken of the facts of the case in point in order to determine [which is the fundamental freedom] to which the dispute in the main proceedings relates": *Kronos International Inc* v *Finanzamt Leverkusen* ECLI:EU:C:2014:2200, [2015] STC 351, at paragraph 37.

[36] In the present case, the object of the loans was to pass the petitioner's income to him. Given the terms of the loans, AML was plainly not making an investment. The purpose of the relevant national legislation was to secure that remuneration was appropriately charged to tax. In any event it was inappropriate to assess the petitioner's averments by reference to article 63. The primary freedoms engaged by the facts of the case were the free movement of workers and freedom to provide services. It was only necessary to consider whether schedules 11 and 12 were compatible with those freedoms: *Fidium Finanz AG* v *Bundesanstalt für Finanzdienstleistungsaufsicht* [2006] ECR I-9521, paragraphs 34, 43 and 49. No infringement of those freedoms was asserted.

Decision

[37] In my opinion the petitioner has failed to establish that there is a movement of capital that engages his EU law right. In the absence of a definition in the Treaties of the expression "movement of capital", the decision of the Court of Justice in *Luisi and Carbone* (above) provides a useful starting point. The question in that case was whether a physical transfer of bank notes was to be regarded as a movement of capital. The Court noted that physical transfer of bank notes was included in the list of capital movements in the annex to the then extant directives adopted in relation to movement of capital, but considered that this did not necessarily imply that such a transfer itself constituted a movement of capital. In particular, the Court held at paragraph 22 that it was not to be classified as a movement of capital where it corresponded to an obligation to pay arising from a transaction involving the movement of goods or services.

[38] In my opinion there is a similar correspondence in the circumstances of the present case. The movements of money and services can be looked at in one of two ways. Taking a broad purposive approach, it could be said that the overall effect of the arrangements entered into was that the petitioner's services as a pilot were provided by him to Ryanair in exchange for the payments that the petitioner received from AML, consisting partly of a small salary and partly of non-commercial loans. On the basis of the Court's analysis in *Luisi and Carbone*, that is not to be classified as a movement of capital because it amounted to payment for services. On a narrower approach it could be said that the petitioner provided service/services to AML consisting of his agreement to being supplied as a pilot to Ryanair, in exchange for payments, in the form of a small salary and non-commercial loans, received from AML. Again, in terms of *Luisi and Carbone*, there is no movement of capital because the

payments from AML corresponded to an obligation to pay arising from a transaction involving the provision of the petitioner's services to AML.

[39] This approach is consistent with the analysis of the Court of Justice in the more recent case of *Fidium Finanz* (above). Fidium was a Swiss company offering credit online to customers abroad. The German financial authorities prohibited Fidium from carrying on business in Germany without authorisation. Fidium raised proceedings based on breach of the right to free movement of capital, and a request for a preliminary ruling was made to the Court on the question whether an undertaking in a country outside the EU could rely on the free movement of capital in respect of the commercial grant of credit to residents of a member state, or whether the provision of such financial services was covered solely by the freedom to provide services. The point was that Fidium, being registered in a "third country" could rely upon free movement of capital but not upon freedom to provide services in a member state. The Court noted at paragraph 30 that:

> "Admittedly, it is possible, in certain specific cases in which a national provision concerns both the freedom to provide services and the free movement of capital, that that provision may simultaneously hinder the exercise of both of those freedoms."

At paragraph 34, the Court stated, by analogy with previous decisions:

> "Where a national measure relates to the freedom to provide services and the free movement of capital at the same time, it is necessary to consider to what extent the exercise of those fundamental liberties is affected and whether, in the circumstances of the main proceedings, one of those prevails over the other… The Court will in principle examine the measure in dispute in relation to only one of those two freedoms if it appears, in the circumstances of the case, that one of them is entirely secondary in relation to the other and may be considered together with it…"

On the facts of that case, the Court decided (paragraph 49):

> "It is apparent that, in the circumstances of the main case, the predominant consideration is freedom to provide services rather than the free movement of capital. Since the rules in dispute impede access to the German financial market for companies established in non-member countries, they affect primarily the freedom to provide services. Given that the restrictive effects of those rules on the

> free movement of capital are merely an inevitable consequence of the restriction imposed on the provision of services, it is not necessary to consider whether the rules are compatible with [what is now article 63]…"

[40] By analogy, the present case is concerned predominantly with the petitioner's freedom to provide services. Regardless of whether the petitioner is treated as providing services to Ryanair or to AML, it is not argued that the imposition of the loan charge constitutes an unjustified infringement of his freedom to provide such services. On either analysis, any restriction on free movement of capital is, in my opinion, clearly secondary to the freedom to provide services, because it arises only as a result of the method of remuneration adopted in the arrangements entered into between the petitioner and AML. I recognise that the treatment of the right of free movement of capital as secondary in *Fidium Finanz* (and also in *Test Claimants in the Thin Cap Group Litigation* v *IR Commrs* [2007] ECR I-2107: see paragraph 34) was in a context where there *was* a restriction of the primary freedom (freedom to provide services in *Fidium Finanz*: freedom of establishment in *Thin Cap Group Litigation*). That, however, does not appear to me to affect the analysis that where one of the freedoms prevails over another, the matter must be determined by reference to the prevailing freedom.

[41] The authorities relied upon by the petitioner do not, in my view, cast any doubt upon this analysis. Annex I to Directive 88/361/EEC contains a non-exhaustive classification of capital movements for the purposes of what is now article 63. Loans are mentioned under four of the headings in the classification, namely Heading I (which includes "Long-term loans with a view to establishing or maintaining lasting economic links"); Heading VII - Credits Related to Commercial Transactions or to the Provision of Services in which a Resident is Participating; Heading VIII (Financial Loans and Credits not included under I, VII and XI); and Heading XI - Personal Capital Movements (which in addition to "loans"

includes items such as gifts and endowments, and inheritances and legacies). In an explanatory note to Heading VIII, it is stated to include

> "Financing of every kind granted by financial institutions, including financing related to commercial transactions or to the provision of services in which no resident is participating. This category also includes mortgage loans, consumer credit and financial leasing, as well as back-up facilities and other note-issuance facilities".

Some of these classifications are clearly inapplicable to the loans received by the petitioner. Reliance is placed in the petitioner's argument only on Heading VIII (which is stated to include short, medium and long term loans), but the terms of this classification do not in my opinion support the argument that every loan, in whatever circumstances, is a movement of capital. As the Advocate General observed in *Persche* (above), the freedom is based on the object of the transaction, and one therefore returns to the fact that the object of the loans received by the petitioner was to pay him for his services as a pilot. For the reasons already set out, that is not a movement of capital.

[42] The *Ritter-Coulais* case was decided under reference to free movement of workers. In the course of its decision, the Court noted that failure to take account of income losses (ie expenditure) relating to a house in France for the purposes of determining liability to tax on income received in Germany might fall within the scope of the free movement of capital under what is now article 63, but that general observation does not assist in circumstances of the present case. Nor, in my view, does the case of *Sandoz* (above) provide any support for the proposition that loans are by their nature movements of capital. The loans in that case clearly were, but that was not in dispute.

[43] In summary, one comes back to the observation of the Court in *Luisi and Carbone* (at paragraph 21) that "movements of capital are financial operations essentially concerned with the investment of the funds in question rather than remuneration for a service". I hold

that in the circumstance of this case, the petitioner's EU law right to free movement of capital has not been infringed because the arrangements that he entered into through AML did not constitute movements of capital.

Issue (iii): whether reliance by the petitioner on the right to free movement of capital would be an abuse of that right

[44] In the light of my decision on issues (i) and (ii), this issue is doubly academic, but I shall express my views on it briefly. It is convenient to begin by narrating the argument for HMRC.

Argument for HMRC

[45] On behalf of HMRC it was submitted that the petitioner was not entitled to rely on article 63 because to do so would be an abuse of the freedom it conferred. A person was not entitled, under cover of EU rights, improperly to circumvent national legislation: *Cadbury Schweppes plc* v *IR Commrs* [2006] ECR I-7995: *X GmbH* v *Finanzamt Stuttgart – Körperschaften*, Case C-135/17, ECLI:EU:C:2019:136. It was not suggested that anything that the petitioner had done amounted to fraud or tax evasion: "improper" in this context meant not corresponding to economic reality. The loan schemes were artificial arrangements to avoid tax on work done that did not correspond to economic reality. If, having regard to the petitioner's averments, the court considered that there was a realistic possibility that he had had no subjective intention to avoid tax, an evidential hearing should be fixed.

Argument for the petitioner

[46] On behalf of the petitioner, it was submitted that HMRC's argument was misconceived. In the first place there was no evidential basis upon which to make allegations about the petitioner's motivation in entering into the loan scheme. Evidence would be required of (a) a combination of objective circumstances in which, despite formal observance of the conditions laid down by the EU rules, the purpose of those rules had not been achieved, and (b) a subjective element consisting in the intention to obtain an advantage from the EU rules by creating artificially the conditions laid down for obtaining it: see eg *Hungary* v *Slovakia* [2013] 1 CMLR 21. Neither was present here.

[47] Of greater assistance was the statement by the Court in *Cadbury Schweppes* at paragraph 35 that

> "the fact that a Community national, whether a natural or a legal person, sought to profit from tax advantages in force in a member state other than his state of residence cannot in itself deprive him of the right to rely on the provisions of the Treaty".

It was held in that case that only conduct involving the creation of wholly artificial arrangements which did not reflect economic reality, with a view to escaping the tax normally due on the profits generated by activities carried out on national territory, would justify a restriction on a fundamental freedom. The UK Supreme Court had found that loan schemes were not a sham, nor devoid of legal effect. They were not wholly artificial arrangements which did not reflect economic reality. They were designed at least in part and at least for some participants to cater for a gap that existed in the market for contractor workers to be engaged without acquiring the hallmarks of employment. It followed that loan schemes did not reach the very high bar required by *Cadbury Schweppes* in order to permit a restriction on a fundamental Treaty freedom.

Decision

[48] I am not impressed by the petitioner's argument based upon absence of evidence of motivation. In so far as the petitioner seeks to assert that the arrangements were designed to cater for a "gap in the market" in relation to contractor workers, he contradicts the factual grounds upon which this petition proceeds. I have already made the point that the statutory provisions in schedules 11 and 12 to the Finance (No 2) Act 2017 which the petitioner seeks to challenge apply only where the loans are made as part of a tax avoidance scheme. If that had not been the case, then the loan charge would not apply to the petitioner and he would have no standing to pursue the present application. I must proceed on the basis that the purpose of arrangements in terms of which the petitioner received most of his earnings as a pilot in the form of loans rather than salary or trading income was the avoidance of income tax that would otherwise have been payable. Whatever assurances the petitioner may have been given by the scheme promoter are of no consequence.

[49] That said, I am not convinced that an issue arises of abuse of a Treaty freedom. The question in the *Cadbury Schweppes* case was whether the right to freedom of establishment precluded national tax legislation (in this case in the UK) which imposed a charge on a parent company in respect of the profits made by a controlled foreign company, ie a subsidiary set up in another member state with a favourable tax regime (in this case Ireland). Having made the statements relied upon by HMRC and by the petitioner respectively in the present proceedings, the Court went on to make the following further observations at paragraph 49:

> "… (I)t is settled case-law that any advantage resulting from the low taxation to which a subsidiary established in a Member State other than the one in which the parent company was incorporated is subject cannot by itself authorise that Member State to offset that advantage by less favourable tax treatment of the parent company… The need to prevent the reduction of tax revenue is not one of the

grounds listed in Article 46(1) EC or a matter of overriding general interest which would justify a restriction on a freedom introduced by the Treaty."

The Court went on, however, to conclude:

"51. On the other hand, a national measure restricting freedom of establishment may be justified where it specifically relates to wholly artificial arrangements aimed at circumventing the application of the legislation of the Member State concerned…
…

55. (I)n order for a restriction on the freedom of establishment to be justified on the ground of prevention of abusive practices, the specific objective of such a restriction must be to prevent conduct involving the creation of wholly artificial arrangements which do not reflect economic reality, with a view to escaping the tax normally due on the profits generated by activities carried out on national territory.
…

64. In order to find that there is [a wholly artificial arrangement intended solely to escape a tax] there must be, in addition to a subjective element consisting in the intention to obtain a tax advantage, objective circumstances showing that, despite formal observance of the conditions laid down by Community law, the objective pursued by freedom of establishment, as set out in paragraphs 54 and 55 of this judgment, has not been achieved (see, to that effect, Case C-110/99 *Emsland-Stärke* [2000] ECR I-11569, paragraphs 52 and 53, and Case C-255/02 *Halifax and Others* [2006] ECR I-1609, paragraphs 74 and 75)."

[50] The judgment in *Cadbury Schweppes* was considered and further explained by the Court in *X GmbH* v *Finanzamt Stuttgart - Körperschaften* (above). In this case X, a German company, was charged to tax on profits received by Y, a Swiss company in which X held a 30% shareholding. The profits were derived from debts purchased by Y from another German company. The charging provisions applied only to shares held in companies established in third countries, and the question referred was whether this was an infringement of the right to free movement of capital. At paragraph 23, the Court noted that

"…the referring court is… uncertain whether the grounds capable of justifying a restriction on freedom of establishment set out in the judgment [in *Cadbury Schweppes*] apply in relationships with third countries and, if so, what qualitative and quantitative requirements must the shareholding in a company established in a third country satisfy in order for it not to be regarded as 'wholly artificial'".

The Court responded as follows (paragraph 84):

> "…(I)n the context of the free movement of capital, the concept of 'wholly artificial arrangement' cannot necessarily be limited to merely the indications, referred to in paragraphs 67 and 68 of [*Cadbury Schweppes*], that the establishment of a company does not reflect economic reality, since the artificial creation of the conditions required in order to escape taxation in a Member State improperly or enjoy a tax advantage in that Member State improperly can take several forms as regards cross-border movements of capital. Indeed, those indications may also amount to evidence of the existence of a wholly artificial arrangement for the purpose of applying the rules on the free movement of capital, in particular when it proves necessary to assess the commercial justification of acquiring shares in a company that does not pursue any economic activities of its own. However, that concept is also capable of covering, in the context of the free movement of capital, any scheme which has as its primary objective or one of its primary objectives the artificial transfer of the profits made by way of activities carried out in the territory of a Member State to third countries with a low tax rate."

[51] It can be seen that in both *Cadbury Schweppes* and *X GmbH*, the Court approached the matter not on the basis of abuse of the right to free movement of capital, but rather by posing the question whether an interference with that right was justified on the ground of prevention of abusive practices. It seems to me that a similar approach would be appropriate in the present case. I find nothing in the factual circumstances of this case to indicate that the petitioner had the subjective intention of obtaining an abusive advantage from his EU right of free movement of capital: there is nothing in either party's case to suggest that reliance upon that right was an integral part of the loan schemes into which the petitioner entered.

[52] Approaching the matter in the same way as the Court did in *Cadbury Schweppes* and *X GmbH*, I am satisfied that if I had held that the legislation under challenge constituted an interference with the petitioner's right to free movement of capital, I would have held that such interference was justified. Applying the test enunciated by the Court in *X GmbH* above to loan schemes which *ex hypothesi* have as their primary objective or one of their primary objectives the avoidance of income tax and national contributions which would otherwise be

payable on a person's earnings from an employment or from self-employment, the concept of "wholly artificial arrangement" is applicable. It is clear from the observations of the Court that the applicability of the concept is not restricted to sham transactions, or even to transactions that do not reflect economic reality. The fact that the loans made under loan schemes are not shams, in the sense that they are in theory repayable, does not therefore prevent the interference with free movement of capital from being justified. It may be noted in passing that, contrary to a submission by the petitioner, the opinion of the Advocate General (de la Tour) in *Ecotex Bulgaria EOOD*, Case C-544/19 (18 November 2020) supports this conclusion, noting at paragraph 80 that it is established by the terms of article 65.1 TFEU (above) and the jurisprudence of the Court that the need to prevent "la fraude et l'évasion fiscales", ie both tax evasion (fraude fiscale) and tax avoidance (évasion fiscale) constitutes a legitimate reason capable of justifying a restriction on free movement of capital.

Issue (iv): Does the loan charge constitute a breach of the EU principle of fiscal legality?

Argument for the petitioner

[53] On behalf of the petitioner, it was submitted that the EU law principle of "fiscal legality", captured in the maxim *nullum tributum sine lege* meant that no tax could be levied unless it was provided for by and in accordance with rules established by law which "enable a taxable person to foresee and calculate the amount of tax due and determine the point at which it becomes payable". This principle could be regarded as forming part of the EU legal order as a general principle of law: Case C-566/17 *Związek Gmin Zagłębia Miedziowego w Polkowicach* v *Szef Krajowej Administracji Skarbowej*. Rights under article 17 CFR could not be less than under article 1, protocol 1 to the European Convention on Human Rights. It was contrary to the principle of fiscal legality/legal certainty/protection of legitimate expectation,

except in exceptional circumstances shown to be justified by an objective in the general interest, for the point in time from which a measure falling within the scope of EU law took effect to be set by a national legislature as being before its publication. Retroactive application of a tax falling within the ambit of EU law would only be EU law compatible if it could be demonstrated to the court by cogent and relevant evidence to comply with the EU law principles of fiscal legality.

[54] A burden was imposed on the respondents to show that the legislation imposing the loan charge was both appropriate for securing the attainment of a legitimate objective and did not go beyond what is necessary in order to attain it. It was for the respondents to supply the court with all of the evidence necessary for this court to be satisfied that the measures taken by the UK authorities were in accordance with the EU law principle of proportionality. The court then had to examine critically and objectively such evidence - statistical or *ad hoc* data or by other means - as was supplied, in order to determine whether it could properly be concluded from the evidence that, in its application to the petitioner, the loan charge was an appropriate means of attainment of the objectives pursued or, alternatively, whether it was open to the UK authorities to attain its legitimate objectives by measures that were less restrictive of the petitioner's fundamental freedoms under EU law. In the present case the court had been supplied with no such evidence by the respondent. Mere assertions in the affidavits relied upon by HMRC did not suffice, and the court was not entitled to substitute itself for the respondents in setting out a justification.

[55] Nor had HMRC addressed the "less restrictive alternative" limb of the proportionality test. Even if it were claimed that the UK authorities had a legitimate objective of (a) closing down loan schemes for the future and (b) recovering past tax where HMRC had inadequate knowledge of arrangements taxable under the law then in place, objective (a) could be

achieved by bringing all loans and quasi-loans into charge in the circumstances set out in the amendments made to ITEPA and ITTOIA, and objective (b) could be achieved by legislation similar to schedule 18 to the Finance Act (No 2) 2017.

[56] In relation to legitimate expectation, it had to be borne in mind that loan schemes had been meeting with success in the courts during the time when the loan charge was being devised and enacted. There was accordingly no justification for retroactive imposition.

[57] In all the circumstances, the only conclusion that the court could properly draw on the evidence before it was that the retrospective imposition of the loan charge constituted an unjustified interference with a fundamental Treaty freedom. It was too broad in scope and contravened EU law, and was therefore unlawful.

Argument for HMRC

[58] On behalf of HMRC it was submitted that the loan charge legislation did not breach any of the EU law principles. As regards proportionality, it was agreed that the test was whether the measure in question was suitable for securing the attainment of the objective in question, and did not go beyond what was necessary in order to attain that objective: *X GmbH* (above), paragraph 70. The court had to be satisfied on the basis of material and submissions put to it that the test was met: *Scotch Whisky Association* v *Lord Advocate* [2016] 1 WLR 2283 (ECJ) at paragraph 56, as discussed by the Supreme Court in the same litigation at 2018 SC (UKSC) 94, paragraph 14. It was not necessary for the respondents to prove that no other conceivable means could achieve the aim pursued: *Scotch Whisky Association* (ECJ) at paragraph 55.

[59] The legislation imposing the loan charge had been designed around the need to ensure that arrangements not involving tax avoidance were excluded from it. There was a

consultation procedure during which questions were asked as to what arrangements should be excluded. In the legislation as enacted, including the amendments to ITEPA and ITTOIA, there were, apart from the general exclusions for ordinary commercial loans not connected to tax avoidance arrangements, a variety of entry conditions and exclusions. The legislation was directed at tax avoidance on income from employment and self-employment, and the tax charges were restricted to income on which tax had not otherwise been charged. Any taxpayer such as the petitioner had the opportunity, both in the course of an enquiry or investigation by HMRC that could lead to an assessment, and in an appeal to the First-tier Tribunal against any assessment, to prove that none of the main purposes of the scheme on the basis of which such assessment had been made was tax avoidance.

[60] As regards the availability of less restrictive means, the Government had previously tried to end the type of tax avoidance in issue by a number of lesser means, using not only legislation but also litigation. The types of schemes targeted by the present legislation had nonetheless continued. In all of these circumstances, the legislation was proportionate.

[61] In relation to legal certainty and legitimate expectation, it was accepted that application of the loan charge depended on facts that had occurred before it was published, but that did not make it retroactive. Tax charges arose only so far as loans remained unpaid around 2 years after publication of the legislation, and 3 years after notice had been given of the Government's intention. On many occasions from 2009 onwards, as the Morse review had accepted, HMRC had stated publicly that these amounts were liable to tax: and that users of loan schemes should not expect to escape tax and national insurance contributions on amounts received. From 9 December 2010 at the latest, it was clear that such schemes were not effective to avoid tax. In these circumstances, the legislation did not breach the

principles of legal certainty or legitimate expectation: nor was there any breach of the Charter of Fundamental Rights.

Decision

[62] I begin by considering the case of *Związek*, relied upon by the petitioner. As always in relation to ECJ jurisprudence, context is important. *Związek* was concerned not with retroactivity but with a potential conflict between a basic principle of VAT law, namely that deduction of input VAT was permissible only to the extent that the expenditure had been used for the purpose of the taxable person's economic activity, and more fundamental rights and general principles of EU law, which would override the VAT law principle. The problem was that deductibility of input VAT on supplies used only partly for the purposes of economic activities was regulated not by a provision of national law but by an administrative practice. Advocate General Sharpston observed at paragraph 78:

> "I am prepared to accept the proposition that the principle that no tax can be levied unless it is provided for by law (in other words the principle of fiscal legality: *nullum tributum sine lege*) does form part of the EU legal order. It may be seen as a specific expression, in the context of tax law, of the freedom to conduct business, the fundamental right to property and the general principle of legal certainty."

At paragraph 87, she noted that in some member states, the principle of fiscal legality formed part of a longstanding constitutional tradition, having first been enacted "in the United Kingdom" in the Bill of Rights of 1689. In the context of the case before her, she concluded (at paragraph 101) that the constitutional traditions common to the member states, like the case-law of the Strasbourg court on article 1, protocol 1 ECHR, required that the essential elements of a tax be provided for by law in a sufficiently clear, precise and foreseeable manner, but did not impose an obligation to regulate every detail exhaustively.

The Advocate General's opinion in this regard was effectively adopted by the Court at paragraph 39 of its judgment:

> "…(I)t is important to note that, as is apparent from the constitutional traditions common to the Member States, the principle of fiscal legality may be regarded as forming part of the EU legal order as a general principle of law. Although that principle requires, as observed by the Advocate General in point 110 of her Opinion, that any obligation to pay a tax, such as VAT, and all the essential elements defining the substantive features thereof must be provided for by law, that principle does not require every technical aspect of taxation to be regulated exhaustively, as long as the rules established by law enable a taxable person to foresee and calculate the amount of tax due and determine the point at which it becomes payable."

[63] In my opinion, the principle of fiscal legality, as described by the Advocate General and by the Court is not infringed by the legislation in the Finance (No 2) Act 2017 that imposed the loan charge. Although the tax base of the charge consists of loans made before the enactment (or even the announcement) of the relevant statutory provisions, the charge itself was, at the time of enactment, both precise and prospective. Taxpayers such as the petitioner knew with a high degree of certainty what the loan charge would be imposed upon, namely loans remaining outstanding some 2 years later. There was accordingly no infringement of the *nullum tributum sine lege* principle. There is nothing in the Court's expression of that principle to prohibit a tax that falls due after the time of its introduction but uses as its base a financial resource which was already in existence prior to its introduction.

[64] If, contrary to the views that I have expressed, the enactment of the loan charge did engage one of the petitioner's EU law rights, ie the right to free movement of capital or the principle of fiscal legality, it would have been necessary to address the issues of proportionality, legal certainty and legitimate expectation.

Proportionality

[65] Where a national measure has the effect of restricting an EU law freedom, the principle of proportionality requires the member state in question to satisfy the court that the restriction is necessary in order to achieve the declared objective, and that that objective could not be achieved by prohibitions or restrictions that are less extensive, or that are less disruptive of trade within the European Union: see eg *Scotch Whisky Association* v *Lord Advocate* (above) in the ECJ at paragraph 53. I accept the petitioner's submission that the burden of proving proportionality rests upon the state. What is required by way of proof will, however, vary considerably from case to case. In the circumstances of the present case, assessment of proportionality seems to me to be straightforward. The declared objective of the loan charge was to recover tax on loans made in the course of schemes whose purpose, or main purpose, was the avoidance of tax and national insurance contributions on the income of the recipients of the loans. It is not difficult to discern that the proportionality principle requires that tax be imposed on such loans but not upon any transactions not falling within the foregoing description. The key requirement is that any loan unconnected with a tax avoidance arrangement must be excluded from the scope of the restrictive provision. If that were not done, the principle would not have been observed.

[66] On the basis of the material before me, including the affidavit of Ms McGeehan, the person within HMRC who has had responsibility for income tax policy during the material period, it is apparent that the proportionality principle has been respected in that the statutory provisions in schedules 11 and 12 to the Finance (No 2) Act 2017 apply only to loans and quasi-loans falling within Part 7A of ITEPA or sections 23A to 23H of ITTOIA, ie where (as regards employment income) the loan is not on commercial terms and is connected with a tax avoidance arrangement or (as regards trading income) it is reasonable

to suppose that the recipient will obtain a tax advantage as a result of the arrangement. The legislation contains a large number of express exclusions of types of employee benefits which apply equally to the loan charge. It was not submitted that the legislation has misfired in this regard in that it catches loans unconnected with arrangements to avoid income tax: that is not the petitioner's case.

[67] In these circumstances it appears to me that HMRC have discharged the burden of showing that if the loan charge operates as a restriction on either freedom of movement of capital or on the principle of fiscal legality, it is necessary in order to achieve its declared objective, and moreover that that objective could not be achieved by restrictions that are less extensive or less disruptive of trade within the European Union.

Legal certainty and legitimate expectation

[68] As regards legal certainty and legitimate expectation, it is necessary to have regard to the background to the imposition of the loan charge in 2017. I have already mentioned that the Government's intention to introduce legislation to nullify the tax advantages of loan schemes featuring an employment relationship was announced on 9 December 2010 by the Exchequer Secretary to the Treasury, who stated *inter alia*:

> "…(T)he Government are introducing legislation to tackle arrangements involving trusts or other vehicles used to reward employees which seek to avoid or defer the payment of income tax or National Insurance Contributions (NICs)… In many cases, these third-party arrangements allow an employee to enjoy the full benefit of a sum of money paid or assets provided while arguing that, because of the structure of the ' arrangements, there is no legal right to the money or assets…
>
> The legislation inserts a new part 7A into the Income Tax (Earning and Pensions) Act 2003. The legislation ensures that where a third party makes provision of what is in substance a reward or recognition, or a loan, in connection with the employee's current, former, or future employment, an income tax charge arises…

> There will be protection for specified types of arrangements involving third parties-including registered pension schemes, approved employee share schemes and ordinary commercial transactions…
>
> The legislation will take effect from 6 April 2011 and apply to rewards, recognitions or loans which are earmarked for the benefit of an employee, or former or prospective employee, or otherwise made available on and after that date.
>
> In addition, anti-forestalling provisions apply to the payment of sums (including loans) and the provision of readily convertible assets for the purposes of securing the payment of sums (including loans) where the sum is paid or the asset is provided between 9 December 2010 and 5 April 2011 where, if paid or provided on or after 6 April 2011, they would be caught by the legislation…"

[69] It should be borne in mind that the "employer" in this regard might or might not mean the person for whom services were actually being performed. The circumstances of the petitioner's case afford an example of this: during the tax years 2009-10 and 2010-11, the petitioner was treated as self-employed by Ryanair but was an employee of AML. The anti-avoidance legislation in the Finance Act 2011 therefore applied to him in respect of that part of the tax year 2010-11 after 9 December 2010. His self-employment status so far as Ryanair was concerned was not relevant to that period or indeed subsequently.
From 2011-12 until 2014-15, the loans received by the petitioner were received not in consequence of any employment relationship but because of his membership of the AML Partners' Collective Company. Schemes of this kind, based upon provision of services rather than upon an employment relationship, were not specifically targeted by anti-avoidance legislation until 2017.

[70] Against that background, the question is whether the introduction of the loan charge in 2017, extending to payments received by employees before 2011 and to payments received by individuals providing services before 2017, constituted a breach of the principles of legal certainty and legitimate expectation. I reiterate that in these proceedings I am concerned with the loan charge provisions as they now stand, following the amendments

made to them in 2020 to reflect the recommendations of the Morse review. It is not necessary for me to express a view as to whether the above EU principles were breached by the loan charge as originally enacted, when it extended *inter alia* to loans received as far back as 1999, or to certain loans in respect of which no assessment to income tax could by 2017 have been made.

[71] So far as loan schemes falling within the scope of the Finance Act 2011 provisions are concerned, I am in no doubt that the imposition of the loan charge in respect of loans received after 9 December 2010 (the date of the Ministerial statement) was compliant with the principles of legal certainty and legitimate expectation. By 2016, when the Government's intention to introduce the loan charge was announced, no question remained as to whether such loans were chargeable to income tax and national insurance contributions: the issue had become one of collection of the tax due. There could, in my opinion, have been no legitimate expectation that any of those loans would not be charged to tax (unless of course they had been properly disclosed in a return and HMRC had failed to open a timeous enquiry). In such circumstances it was consistent with those EU principles for legislation to be introduced to recover tax that had fallen due. As Sir Amyas Morse put it in his report (at pages 3-4):

> "There was a need for a new policy in 2016. HMRC had had considerable success in getting large corporates to settle after the introduction of new legislation in 2011. However, loan schemes were still used over 10,000 times in 2011-12. This, and subsequent usage, deprived the Exchequer of tax that was clearly due following the new legislation. It was reasonable for the government to act to ensure that this tax was collected.
>
> The Loan Charge therefore emerged in 2016 out of a desire to shut down the use of loan schemes, for reasons of fairness to other taxpayers, as well as value for money, practicality, and to collect revenue for public services.
>
> This followed over 65,000 instances of loan scheme usage from April 2011 - March 2016, and a decline in the number of schemes (and taxpayer usage of them)

> being disclosed to HMRC. In spite of the law being clear, HMRC were therefore not always able to identify the relevant users or efficiently collect the tax that was due. This delay effectively delivered an unjustified advantage to taxpayers participating in loan schemes…"

[72] Could it be contended, however, that the position was different regarding loan schemes not falling within the scope of the Finance Act 2011 because they utilised partnership or self-employment instead of employment? The provisions of the Finance (No 2) Act 2017 which brought such arrangements within ITTOIA were not retrospective. There are, however, other factors to be considered. I accept the evidence of Ms McGeehan that there was a growth of such schemes after 2011 in an attempt to circumvent the provisions of Part 7A of ITEPA, inserted by the 2011 Act. The circumstances of the petitioner afford an example of an individual who participated in an employment-based loan scheme until 2011-12 and a partnership-based scheme thereafter. It is also important to recall that although their position had not always been vindicated by the courts, HMRC were continuing after 2011 to challenge loan schemes not falling within Part 7A under pre-existing law including other anti-avoidance provisions. I am not therefore persuaded that an individual participating in a non-employment-based loan scheme between 2011 and 2017 had a legitimate expectation that loans that he or she received would not, by one means or another, be held to be chargeable to income tax. The legislative policy was clear, as was the intention of HMRC to nullify any tax advantage from such schemes. In so far as the imposition of the loan charge on such schemes included any element of retrospection, it did not interfere with any legitimate expectation of the users of such schemes. Any interference with legal certainty was justified in the public interest. Accordingly, had it been necessary to do so, I would have held that neither legal certainty nor legitimate expectation was

breached by the imposition of the loan charge in either schedule 11 or schedule 12 to the Finance (No 2) Act 2017.

Issue (v): whether the loan charge amounts to a disproportionately severe and retrospective penalty

Argument for the petitioner

[73] On behalf of the petitioner it was submitted that the loan charge, properly viewed, was to be regarded as a penalty imposed by the UK Government for the purpose of forcing taxpayers such as the petitioner to reach settlements with HMRC (indeed, the charge was referred to, somewhat tendentiously, as "the loan charge penalty" throughout the petitioner's submissions). It was intended to have deterrent and punitive effect so as to encourage such settlement. The provisions of schedules 11 and 12 to the Finance (No 2) Act 2017 resulted in a penalty liability being imposed on individuals for having used schemes that were "known to and approved by HMRC".

[74] The relevant Strasbourg case law was to the effect that, in order to be compliant with *inter alia* article 1, protocol 1 ECHR, tax assessments and related obligations had to (i) have a proper basis in domestic law; (ii) be accessible, precise and foreseeable in their effect; and (iii) be applied by the domestic authorities in a manner which was consistent, coherent and ECHR proportionate. At least the same level of protection applied in terms of article 17 CFR. Separately, article 49 CFR provided that no heavier penalty could be imposed for a criminal offence than the one that was applicable at the time when the offence was committed, and that the severity of the penalty must not be disproportionate to the offence. Even if national law might classify the procedure giving rise to the imposition of the loan charge as administrative, given that the intent and effect of its imposition was not simply to

recover unpaid tax that was properly due at the time when the loan monies were received, but also to punish past conduct and to deter future like conduct, the petitioner could pray in aid the protections afforded under EU law in relation to the imposition of criminal penalties.

[75] Properly analysed under EU law, the loan charge was akin to a criminal penalty imposed in relation to the petitioner's exercise of his fundamental Treaty rights relative to free movement of capital. It had been imposed on him in breach of the principle of legal certainty. In all the circumstances it constituted an unjustified penalty imposed with retrospective effect on taxpayers such as the petitioner on the exercise of his fundamental rights.

[76] Moreover, even if the court were satisfied that the loan charge penalty legislation was capable of being operated in an EU proportionate way, it also had to be satisfied that loan charge was being administered and applied in relation to the petitioner among others in a manner that was EU law proportionate. It was clear from the findings of the Morse review that in many cases (including the petitioner's), the approach taken by HMRC to the enforcement of the legislation was designed to be heavy-handed and punitive, in order to force taxpayers to settle whether that would legitimately be in their interests or not. The review could not be regarded as a historical snapshot of a situation that no longer existed.

[77] Other features that made the loan charge disproportionately severe included:

- the fact that in addition to the charge, the loan remained outstanding and repayable if demanded. There had been cases where the loan book had been sold to a third party and repayment demanded:
- the effect of the charge was to cumulate liabilities in a 3-year period, potentially resulting in charges to tax at higher rates with a view to forcing a settlement.

Argument for HMRC

[78] On behalf of HMRC it was submitted that the loan charge was not a penalty within the meaning of EU law. To the extent that the charges exceeded tax on any alternative basis, they were imposed on amounts that were, in reality, remuneration for work done, but otherwise bore no tax because of an artificial structure put in place to avoid incurring the tax normally due. The charge was made in the normal way for an income tax charge, namely at a percentage rate by reference to the taxpayer's total taxable income for the year. Some of the charge might be covered by the taxpayer's personal allowances, and it could lead to liability at the basic or a higher rate of income tax. Credit was given to the extent that the income in question had already given rise to another income tax charge. All of this was normal for an income tax charge: but inconsistent with the concept of a penalty. There was no identifiable "offence", and no payment beyond tax charged on amounts that were, fundamentally, remuneration for work done. All that happened was that the petitioner had failed in his endeavour to escape the tax and national insurance contributions fairly due from him. The "penalty", if there was any, could not be said to be more than the tax that had been avoided by use of the schemes. To the extent they were relevant, any requirements in terms of justification, proportionality and legal certainty were met.

Decision

[79] It is not entirely clear to me what additional point the petitioner seeks to make by characterising the loan charge as a penalty. In so far as the complaint is related to interference with the right to free movement of capital or the principles of proportionality and legal certainty, I have already addressed these matters and held, for the reasons set out

above, that there is no such interference. It is not readily apparent what additional EU law protections, referable to criminal penalties in particular, are being founded upon.

[80] In any event I accept HMRC's argument that the loan charge is not properly to be characterised as a penalty for the purposes of application of EU law rights. As was submitted, it is a charge to income tax on sums received by taxpayers such as the petitioner in consideration of the provision of service or services, which sums have not otherwise borne income tax. The notion of "penalty" connotes a surcharge payable by way of punishment in addition to an amount of tax due: there is nothing of that kind here. The petitioner's characterisation of the charge as a punishment for past conduct has no foundation in fact. Cases such as *Åklagaren* v *Åkerberg Fransson* [2013] 2 CMLR 46 and *Menci* v *Procura della Repubblica* [2018] 3 CMLR 12 which are concerned with whether or not a penalty is to be regarded as a criminal penalty are of no assistance where, as here, the question is whether there is any penalty at all.

[81] I recognise that for many taxpayers, including the petitioner, the imposition of the loan charge will have come as a very unwelcome surprise when it was announced in 2016 and enacted in 2017. The Morse review noted (at paragraph 4.29) that

> "…(T)axpayers may have still entered into a scheme on or after 9 December 2010, and not understood that tax would be considered due. We received a large volume of evidence that individuals did not understand at the time that the schemes would be considered tax avoidance and would not have used them if they did. Many people affected by the Loan Charge clearly feel a real stigma through being associated with tax avoidance, which is exacerbated through not having understood the nature of loan schemes."

In this context, the review was critical of the lack of direct communication between HMRC and taxpayers into whose affairs an investigation had been opened, and even more critical of loan scheme promoters who continued to market schemes after 2010 when legislative action was announced. It would be fair to say that some of the original features of the 2017 legislation, removed in the light of the Morse recommendations, could arguably have been regarded as having a flavour of punishment about them. But these proceedings are concerned with the law as it now stands. That law does not go beyond ensuring the collection of tax on payments received since 2010 by taxpayers as remuneration for work done, in respect of which no tax has otherwise been paid. The issue of whether a loan upon which the charge has been paid could also be subject to a demand for repayment, whether by the original lender or by an assignee, seems to me to be one which lies between any taxpayer in that position and the scheme promoter responsible for devising the terms of the loan. In any event, the petitioner's characterisation of the charge as a penalty falls to be rejected.

Disposal

[82] For all of these reasons I shall dismiss the petition. Questions of expenses are reserved.