Neutral Citation: [2025] UKFTT 295 (TC)

Case Number: TC09445

FIRST-TIER TRIBUNAL
TAX CHAMBER

Taylor House

Appeal reference: TC/2023/08230

INCOME TAX – assessments under the legislation relating to transfers of assets abroad in respect of two types of deemed income, offshore income gains and accrued income profits in respect of foreign securities, which were deemed to arise, after the Appellant was deemed to become UK domiciled, in an offshore settlement settled by the Appellant when she was not UK domiciled or an offshore company in which such a settlement was a shareholder – consideration of whether such deemed income fell within the definition of "protected foreign source income" in Section 721A of the Income Tax Act 2007 (the "ITA"), purposively construed so that it was not chargeable to income tax in the Appellant's hands as it arose – no, because, purposively construed, the definition of "protected foreign source income" applied only to income arising offshore which would have been "relevant foreign income", as defined in Section 989 of the ITA, of the taxpayer if it had been received by the taxpayer and, in this case, the offshore income gains and accrued income profits in respect of foreign securities that were deemed to arise in the offshore settlement or offshore company would not have been "relevant foreign income" had it been received by the Appellant – that being the case, should the definition of "protected foreign source income" be subject to a rectifying construction so as to include that deemed income – consideration of the principles relating to rectifying construction and their application on the facts of this case – no, because it was not clear that Parliament intended the definition of "protected foreign source income" in Section 721A of the ITA to include offshore income gains and accrued income profits in respect of foreign securities and that they had inadvertently excluded those items from the definition – appeal dismissed

Heard on: 4, 5 and 6 February 2025
Judgment date: 7 March 2025

Before

TRIBUNAL JUDGE TONY BEARE
MR JULIAN SIMS

Between

VALESCA VALENTINA YVETTE LOUWMAN

Appellant

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS
Respondents

Representation:

For the Appellant: Ms Amanda Hardy KC and Mr Oliver Marre, of counsel, instructed by Evelyn Partners LLP

For the Respondents: Mr Mark Fell KC, of counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs

DECISION

INTRODUCTION

1. This decision relates to appeals made by the Appellant against closure notices (the "Closure Notices" and, each, a "Closure Notice") issued by the Respondents under Section 28 of the Taxes Management Act 1970 in respect of the tax years of assessment ending 5 April 2019, 5 April 2020 and 5 April 2021 (together, the "relevant tax years" and, each, a "relevant tax year").

2. The appeals require us to address a narrow point of statutory construction in the light of facts that are agreed by the parties.

3. The dispute in this case relates to the realisation in the relevant tax years of two distinct types of deemed income – "offshore income gains" and "accrued income profits".

4. An "offshore income gain" arises where a person makes a gain on the disposal of an interest in a fund that is regarded for UK tax purposes as an offshore non–reporting fund. In that case, Regulation 18(1) of the Offshore Funds (Tax) Regulations 2009 SI 2009/3001 (the "OFTR")) provides that the gain in question "is treated for all the purposes of the Tax Acts as income which arises at the time of the disposal to the person making the disposal (or treated as making the disposal)". Regulation 18(3) of the OFTR provides that, in the case of a person chargeable to income tax, tax is charged on that income under Chapter 8 of Part 5 of the Income Tax (Trading and Other Income) Act 2005 (the "ITTOIA"), headed "Income not otherwise charged" ("Chapter 8"), in the tax year in which the disposal is made. In the rest of this decision:

(1) when we refer to a "Regulation", it will mean a Regulation of the OFTR; and

(2) we will refer to offshore income gains as "OIGs".

5. An "accrued income profit" arises when securities which carry (or have carried) interest are transferred, broadly to reflect the part of the disposal proceeds which represents accrued interest on the securities in question – pursuant to Part 12 of the Income Tax Act 2007 (the "ITA"), headed "Accrued income profits". In that case, Sections 616 and 617 of the ITA provide that income tax is to be charged on the full amount of the accrued income profit. Accrued income profits can arise on the disposal of securities issued by UK resident issuers as well as securities issued by non–UK resident issuers. In this case, the accrued income profits in question all arose on the disposal of securities issued by non–UK resident issuers. In this decision, we will refer to accrued income profits arising on the disposal of such securities as "AIPs", as distinct from the general term "accrued income profits", by which we will mean accrued income profits arising on the disposal of both categories of securities.

6. A common feature of both OIGs and accrued income profits is that, in both cases, the receipt of a sum which, as a matter of general tax law, has a capital nature and would generally be taken into account in calculating a capital gain, is instead treated for UK tax purposes as giving rise to deemed income.

7. The fact that the transactions described below gave rise to both OIGs and AIPs is not in dispute. However, what is in dispute is whether the Appellant was liable to income tax on those amounts when they arose. We will explain the reasons for that disagreement in due course but, before we do so, we should first set out the agreed facts.

THE AGREED FACTS

8. They are as follows:

(1) the Appellant is resident in the UK for tax purposes and was so resident in each of the relevant tax years;

(2) the Appellant is domiciled in the Netherlands as a matter of general law but has been deemed to be domiciled in the UK since 6 April 2018;

(3) the Appellant is the sole settlor of four trusts (together, the "Trusts" and, each, a "Trust"), each settled on 7 March 2017. They are:

(a) The Verubino Grantor Trust ("Verubino");

(b) The Vivarais Grantor Trust ("Vivarais");

(c) The Vestus Grantor Trust ("Vestus"); and

(d) The Vernon Court Grantor Trust ("Vernon");

(4) the trustee of each Trust is the Venosta Private Trust Company (the "PTC"), a company incorporated and resident in the Cayman Islands;

(5) each Trust other than Vernon owns, through a non–UK resident nominee company, a one-third interest in a portfolio of assets;

(6) Vernon owns a one–third interest in a non–UK resident company, Hilarion II Limited ("Hilarion") which owns, through a non–UK resident nominee company, units in a non–reporting fund;

(7) the disposals giving rise to OIGs in the tax year ending 5 April 2019 were as follows:

Investment number	Date	Holding	Gain on disposal	Disponor
1	2 November 2018	Invesco QQQ Trust Series 1 (US46090E1038)	£815,536.97	Verubino
2	11 June 2018	iShares Core S&P Small Cap ETF (US4642878049)	£356,554.49	Verubino
3	11 June 2018 and 19 June 2018	iShares Transportation Average ETF (US4642871929)	£340,070.35	Verubino
4	7 November 2018	SPDR S&P 500 ETF Trust (US78462F1030)	£1,107,150.29	Verubino
5	31 December 2018, 28 February 2019 and 31 March 2019	W.P. Stewart Holding Fund (LU0237485098)	£24,682.71	Hilarion

(8) the disposals giving rise to OIGs in the tax year ending 5 April 2020 were as follows:

Investment number	Date	Holding	Gain on disposal	Disponor
1	9 April 2019	iShares MDAX DE PART CAP (DE0005933923)	£184,364.03	Verubino
2	14 May 2019, 21 August 2019 and 10 February 2020	W.P. Stewart Holding Fund (LU0237485098)	£30,511.48	Hilarion

(9) the disposals giving rise to OIGs in the tax year ending 5 April 2021 were as follows:

Investment number	Date	Holding	Gain on disposal	Disponor
1	5 June 2020, 25 June 2020, 13 November 2020 and 3 March 2021	W.P. Stewart Holding Fund (LU0237485098)	£25,068.97	Hilarion

(10) the AIPs were realised by one or more of Verubino, Vivarais and Vestus. The aggregate AIPs realised by those Trusts in the tax year ending 5 April 2019 was £11,162.83 and the aggregate AIPs realised by those Trusts in the tax year ending 5 April 2021 was £32,969.73. In the tax year ending 5 April 2020, the Trusts realised an aggregate accrued income loss of £273.58;

(11) the Appellant disclosed the OIGs in her tax return for each relevant tax year and disclosed the AIPs in her tax return for each of the tax year ending 5 April 2019 and the tax year ending 5 April 2021;

(12) the Respondents opened enquiries into the Appellant's tax returns as follows:

(a) the enquiry into the Appellant's tax return for the tax year ending 5 April 2019 was opened on 22 January 2021;

(b) the enquiry into the Appellant's tax return for the tax year ending 5 April 2020 was opened on 10 January 2022; and

(c) the enquiry into the Appellant's tax return for the tax year ending 5 April 2021 was opened on 8 November 2022;

(13) the Respondents issued the Closure Notices in relation to those enquiries as follows:

(a) the Closure Notice in respect of the enquiry into the Appellant's tax return for the tax year ending 5 April 2019 was issued on 27 April 2023 in the amount of £2,655,157.64;

(b) the Closure Notice in respect of the enquiry into the Appellant's tax return for the tax year ending 5 April 2020 was issued on 27 April 2023 in the amount of £214,875.51; and

(c) the Closure Notice in respect of the enquiry into the Appellant's tax return for the tax year ending 5 April 2021 was issued on 27 April 2023 in the amount of £58,038.70.

The amendments made by the Closure Notices related exclusively to the OIGs and AIPs referred to above;

(14) the Appellant appealed against the Closure Notices by letter dated 23 May 2023; and

(15) the Respondents acknowledged receipt of the Appellant's appeal on 30 May 2023 and agreed to the postponement of the amounts set out in the Closure Notices.

THE BACKGROUND TO THE DISPUTE

9. Before setting out the narrow point of dispute between the parties, we need first to explain the context in which it has arisen.

10. In the closure notices, the Respondents assessed the Appellant to income tax in respect of the OIGs and the AIPs under Section 720 of the ITA, in Chapter 2 of Part 13 of the ITA, which imposes a charge to income tax on an individual in respect of income arising to a person outside the UK as a result of, inter alia, a transfer of assets by the individual in question. It is common ground that, subject to the one issue which is described below, this section applied to the Appellant in respect of the OIGs and the AIPs which arose in the Trusts and Hilarion.

11. Immediately prior to the enactment of the Finance (No 2) Act 2017 (the "F (No 2) A 2017"), where:

(1) Section 720 of the ITA was in point in relation to an individual who was not domiciled in the UK and was subject to the remittance basis of tax pursuant to Sections 809B, 809D or 809E of the ITA (a "non–UK domicile"); and

(2) the income arising to the person outside the UK would have been "relevant foreign income", as defined in Section 989 of the ITA, if it had been received by the non–UK domicile,

then the income in question was treated as "relevant foreign income" (as so defined) of the non–UK domicile. A significant consequence of this was that the income in question was not subject to tax in the hands of the non–UK domicile as it arose but was instead subject to tax only if and when it was remitted. There were provisions in the UK tax legislation – Regulation 19, Section 670A of the ITA and Section 830(4) of the ITTOIA – which expressly provided that both OIGs and AIPs were "relevant foreign income" for a non–UK domicile. The UK tax legislation contained no equivalent express provisions in relation to an individual who was not a non–UK domicile (a "UK domicile").

12. In this case, as we have already noted, although the Appellant is not generally domiciled in the UK, she was deemed to become so domiciled with effect from 6 April 2018. This was in consequence of the introduction by Section 29(1) of the F (No 2) A 2017 of a new provision – Section 835BA of the ITA – which specified that, with effect from 6 April 2018, an individual who would otherwise have fallen to be treated as non–UK domiciled in a particular tax year would be deemed to be UK domiciled in that tax year if, inter alia, he or she had been resident in the UK for at least fifteen of the twenty tax years preceding that tax year – see Condition B in Section 835BA of the ITA.

13. Parliament recognised that, unless some limitation was introduced, this change would have the effect of bringing a non–UK domicile who was then deemed to become a UK domicile in this way within the scope of income tax on an arising basis under Section 720 of the ITA on the "relevant foreign income" of a non–UK settlement that had been settled by the individual at a time before he or she had been deemed to become a UK domicile. For that reason, the new legislation contained a relief (in Rule 2 of Section 721(3B) of the ITA). That relief was to the effect that, in the case of an individual who was deemed to become a UK domicile by virtue of satisfying Condition B in Section 835BA of the ITA, certain "relevant foreign income" arising in the non–UK settlement after the individual's change in status – which it defined as "protected foreign source income" or "PFSI" – would not be subject to income tax in the hands of the individual as it arose but would instead be subject to income tax only when and to the extent that it was matched to a capital distribution or benefit provided out of the settlement to the individual or certain other persons liable to income tax. The same rule applied to such an individual where the "relevant foreign income" in question arose to a non–UK resident company beneath such a settlement.

14. The definition of PFSI is set out in Section 721A of the ITA. That definition contains various conditions but the only one which is in dispute in this case in is whether the OIGs and AIPs which arose in a Trust or Hilarion and are the subject of the Closure Notices "would be relevant foreign income if [they] were [the Appellant's]" – see Section 721A(3)(a) and 721A(4)(a) of the ITA. The Appellant's primary submission is that, on a purposive construction of the relevant legislation, the OIGs and AIPs would have been "relevant foreign income" if they were the Appellant's income and therefore fall within those provisions. The Appellant goes on to say, as its secondary submission, that, if we decide that the OIGs and AIPs would not have been "relevant foreign income" if they were the Appellant's income and therefore do not fall within those provisions, then the provisions do not give effect to Parliament's intentions and should be read in a manner which ensures that they do. The Respondents say that the OIGs and the AIPs would not have been "relevant foreign income" if they were the Appellant's income and therefore do not fall within those provisions and that there is no basis for rectifying the provisions to ensure that they do.

THE RELEVANT LEGISLATION

15. It may be seen that, at the heart of the dispute in relation to the Appellant's primary submission is the question of whether, when they arose to a Trust or Hilarion, the OIGs and/or AIPs would have been "relevant foreign income" if they had arisen to the Appellant instead.

16. In that regard, at the time when the OIGs and AIPs arose:

(1) Section 989 of the ITA provided as follows:

""relevant foreign income" has the meaning given by section 830(1) to (3) of [the ITTOIA] but also includes, for any purpose mentioned in any provision listed in section 830(4) of that Act, income treated as relevant foreign income for that purpose by that provision"; and

(2) Section 830 of the ITTOIA provided, so far as relevant, as follows:

"(1) In this Act "relevant foreign income" means income which –

(a) arises from a source outside the United Kingdom, and

(b) is chargeable under any of the provisions specified in subsection (2) (or would be so chargeable if section 832 did not apply to it).

(2) The provisions are –

…(o) Chapter 8 of Part 5 (income not otherwise charged).

(3) But “relevant foreign income” does not include income chargeable as a result of—

…

(b) section 517C or 517E of ITA 2007 (profits on certain disposals concerned with land in the United Kingdom treated as trading profits)….

(4) For the treatment of other income as relevant foreign income, see—

…

(aa) regulation 19 of the [OFTR], …

(h) section 670A of ITA 2007 (accrued income profits), …”

ISSUES

17. As outlined in paragraph 14 above, the present appeal gives rise to two issues for us to determine, and they are as follows:

(1) whether the OIGs and AIPs are “protected foreign source income” within the meaning of Section 721A of the ITA (properly construed and in the light of Parliament’s intentions) (“Issue One”); and

(2) whether, if the OIGs and the AIPs are not “protected foreign source income” within the meaning of Section 721A of the ITA, we should rectify Section 721A of the ITA (“Issue Two”).

18. For completeness, we should note that the same issues as those described above arise in connection with provisions equivalent to Sections 721(3B), 721(3)(a) and 721A(4)(a) in Sections 728(3B), 729A(3)(a) and 729A(4)(a) of the ITA. We will not refer to the latter provisions in what follows but the conclusions we set out in relation to the former provisions should be taken to apply to those latter provisions as well.

DISCUSSION

ISSUE ONE

Principles of statutory construction

19. Issue One involves a question of statutory construction.

20. In our view, the principles to be applied in construing statutory provisions may be summarised as follows:

(1) the task of a court in construing legislation is to give effect to Parliament’s intentions in enacting that legislation;

(2) in so doing, the court is seeking the meaning of the words that Parliament used – see Lord Hodge DPSC in *R (on the application of O (a minor, by her litigation friend AO)) v Secretary of State for the Home Department* [2022] UKSC 3 (“*Re O*”) at paragraph [29];

(3) the relevant provision “should be read in the context of the statute as a whole, and the statute as a whole should be read in the historical context of the situation which led to its enactment” – see Lord Bingham in *R (Quintavalle) v Secretary of State for Health* [2003] 2 AC 687 at paragraph [8], Lord Briggs and Lord Leggatt JJSC in *Hurstwood Properties Ltd v Rossendale Borough Council* [2021] UKSC 16 at paragraph [10] and Lord Hodge DPSC in *Re O* at paragraph [29];

(4) there is an important constitutional reason for having regard primarily to the statutory context. As Lord Nicholls explained in *R v Secretary of State for the*

Environment, Transport and the Regions, ex parte Spath Holme Ltd [2001] 2 AC 349 ("*Spath Holme*") at 397F: "Citizens, with the assistance of their advisers, are intended to be able to understand parliamentary enactments, so that they can regulate their conduct accordingly. They should be able to rely upon what they read in an Act of Parliament";

(5) the intention of Parliament is an objective concept and not a subjective one. The phrase is a shorthand reference to the intention which the court reasonably imputes to Parliament in respect of the language used and not the subjective intention of a minister or other persons who promoted the legislation, the draftsman or individual members, or even the majority of individual members, of either House – see Lord Hodge DPSC in *Re O* at paragraph [31] citing Lord Nicholls in *Spath Holme* at 396G and H;

(6) similarly, the subjective intentions and understandings of the executive and of particular government departments are irrelevant because it would be wholly inconsistent with the transparent and open democratic process pursuant to which Parliament enacts legislation to take into account such matters – see *Attorney General for England and Wales v Counsel General for Wales* [2014] UKSC 43 at paragraphs [36] to [39] and *Bogdanic v Secretary of State for the Home Department* [2014] EWHC 2872 (QB) at paragraph [13];

(7) given the above, external aids to interpretation must therefore necessarily play a secondary role. As regards those external aids:

> (a) consultations which preceded the enactment of legislation may disclose the background to the enactment of the legislation and assist the court to identify not only the mischief which it addresses but also the purpose of the legislation, thereby assisting a purposive interpretation of the provision – see *Re O* at paragraph [30] and *Belhaj v Director of Public Prosecutions* [2018] UKSC 33 ("*Belhaj*") at paragraphs [22] and [53];
>
> (b) explanatory notes to a bill can be considered as part of the contextual setting to an Act in order to give it a purposive interpretation – see *Belhaj* at paragraph [53] – and the same principles apply to the explanatory notes prepared by the Tax Law Rewrite Project when interpreting the modern UK tax code – see *R (Derry) v The Commissioners for Her Majesty's Revenue and Customs* [2019] UKSC 19 ("*Derry*") at paragraphs [7], [38] and [86];
>
> (c) "the context disclosed by such materials is relevant to assist the court to ascertain the meaning of the statute, whether or not there is ambiguity and uncertainty, and indeed may reveal ambiguity and uncertainty: *Bennion, Bailey and Norbury on Statutory Interpretation, 8th ed* (2020) para 11.2. But none of these external aids displace the meanings conveyed by the words of a statute that, after consideration of that context, are clear and unambiguous and which do not produce absurdity" – see Lord Hodge DPSC in *Re O* at paragraph [30];
>
> (d) statements made by a Government minister may be used to determine the meaning of a statutory provision only if the three conditions set out by Lord Browne–Wilkinson in *Pepper v Hart* [1993] AC 593 ("*Pepper*") at 640 are met. Those are:
>
> > "(i) that the legislative provision must be ambiguous, obscure or, on a conventional interpretation, lead to absurdity;
> >
> > (ii) that the material must be or include one or more statements by a minister or other promoter of the Bill; and

(iii) the statement must be clear and unequivocal on the point of interpretation which the court is considering"

see Lord Hodge DPSC in *Re O* at paragraph [32];

(8) in relation to the application of deeming provisions, in *The Commissioners for His Majesty's Revenue and Customs v Vermilion Holdings* [2023] UKSC 37 ("*Vermilion*") at paragraph [23], Lord Hodge DPSC repeated the guidance given by Lord Briggs JSC in *The Commissioners for Her Majesty's Revenue and Customs v Fowler* [2020] UKSC 22 ("*Fowler*") at paragraph [27] to the following effect:

"(1) The extent of the fiction created by a deeming provision is primarily a matter of construction of the statute in which it appears.

(2) For that purpose the court should ascertain, if it can, the purposes for which and the persons between whom the statutory fiction is to be resorted to, and then apply the deeming provision that far, but not where it would produce effects clearly outside those purposes.

(3) But those purposes may be difficult to ascertain, and Parliament may not find it easy to prescribe with precision the intended limits of the artificial assumption which the deeming provision requires to be made.

(4) A deeming provision should not be applied so far as to produce unjust, absurd or anomalous results, unless the court is compelled to do so by clear language.

(5) But the court should not shrink from applying the fiction created by the deeming provision to the consequences which would inevitably flow from the fiction being real…"

Similar views were expressed by Lord Lowry in *Marshall v Kerr* [1995] 1 AC 148 at 166H et seq.; and

(9) in determining how far to take a deeming provision, it is instructive to look at the overall pattern and history of the legislation in which that deeming is to be found – see Lord Scott in *R v Dimsey* [2001] UKHL 46 at paragraphs [42] to [51] ("*Dimsey*"). In *Dimsey*, the House of Lords rejected the proposition that a tax avoidance provision in an Act which specified that the income of a transferee was deemed to be the taxable income of the transferor should be interpreted as saying that the relevant income could not also be the income of the transferee. This was because other deeming provisions in the same Act which were also intended to combat tax avoidance specified expressly that income which was deemed to be the income of one person was not to be treated as the income of any other person.

21. Although the parties disagreed on the extent to which, and the manner in which, the principles described in paragraph 20 above applied in this case, we do not think that either party disagreed with those principles.

Legislative history – OIGs

22. In order properly to address Issue One in relation to the OIGs in this case, it is first necessary to set out, in some detail, the legislation pursuant to which the OIGs arose and the background to that legislation.

23. This is as follows:

(1) OIGs were first introduced by the Finance Act 1984 (the "FA 1984"). Section 96(1) of the FA 1984 provided that, where an OIG arose, "it was to be treated for all the purposes of the Tax Acts …as constituting profits or gains chargeable to tax under Case VI of Schedule D". At that time:

(a) the income tax schedules were located in Sections 108 and 109 of the Income and Corporation Taxes Act 1970 (the "ICTA 1970");

(b) Schedule D Case VI covered tax in respect of profits or gains not falling under any other Case of Schedule D or under Schedules A, B, C or E;

(c) income arising from securities out of the UK was taxable under Schedule D Case IV and income arising from possessions out of the UK was taxable under Schedule D Case V; and

(d) as a result of OIGs' falling within Schedule D Case VI, losses arising under Schedule D Case VI could be set off against OIGs under Section 176 of the ICTA 1970.

Section 96(5) of the FA 1984 provided that OIGs arising to an individual who did not have a UK domicile were to be taxed on a remittance basis – in the same way as capital gains arising to such a person – under Section 14 of the Capital Gains Tax Act 1979 (the "CGTA");

(2) the ICTA 1970 and the FA 1984 were subsequently consolidated in the Income and Corporation Taxes Act 1988 (the "ICTA 1988"). Under the ICTA 1988:

(a) OIGs were subject to income tax under Schedule D Case VI pursuant to Section 761(1) of the ICTA 1988;

(b) the income tax schedules, which were in Sections 15 to 20 of the ICTA 1988, were worded in the same way as the equivalent ICTA 1970 provisions;

(c) Section 761(5) of the ICTA 1988 provided that individuals who did not have a UK domicile were to be taxed on a remittance basis, pursuant to Section 14 of the CGTA (and, from 1992, pursuant to Section 12 of the Taxation of Chargeable Gains Act 1992 (the "TCGA")); and

(d) as a result of OIGs' falling within Schedule D Case VI, losses arising under Schedule D Case VI could be set off against OIGs under Section 392 of the ICTA 1988.

In short, there was no meaningful change in the treatment of OIGs as a result of the consolidating legislation;

(3) as a result of the Tax Law Rewrite Project, the income tax legislation was consolidated in two stages – first in 2005 in the form of the ITTOIA and then in 2007 in the form of the ITA;

(4) upon the enactment of the ITTOIA:

(a) the schedular system of income tax was abolished;

(b) Schedule D Case VI was replaced by Chapter 8, a chapter designed to tax income not otherwise charged to income tax. To that end, the chapter contained a charging provision – namely, Section 687 of the ITTOIA ("Section 687") – which provided for income tax to be charged on "income from any source that is not charged to income tax under or as a result of any other provision of this Act or any other Act";

(c) Section 687 was the only charging provision within Chapter 8. However, the chapter also contained Section 688 of the ITTOIA (specifying that tax was to be charged under the chapter on the amount of income arising in the tax year) and

Section 689 of the ITTOIA (which specified that the person liable for the tax was the person receiving or entitled to the income);

(d) Schedule D Case IV and Schedule D Case V were replaced by Part 8 of the ITTOIA. That part introduced the concept of "relevant foreign income" and set out:

(i) the rules applicable to individuals who were not domiciled in the UK and made a claim for their "relevant foreign income" to be subject to tax on a remittance basis;

(ii) certain deductions in calculating "relevant foreign income" where that basis did not apply; and

(iii) relief where an individual was prevented from transferring income to the UK

– see Section 829 of the ITTOIA;

(e) OIGs remained subject to tax under Section 761(1) of the ICTA 1988 but that section was amended in order to remove the reference to Schedule D Case VI in the case of income tax so that the charge to income tax was now under Section 761(1)(b)(i) of the ICTA 1988. Section 761(5) of the ICTA continued to apply as mentioned in paragraph 23(2)(c) above;

(f) Section 830 of the ITTOIA defined "relevant foreign income" by reference to:

(i) income arising from a non–UK source chargeable under one of the provisions listed in Section 830(2) of the ITTOIA but excluding income chargeable under Section 844 of the ITTOIA (unremittable income); and

(ii) "other income" treated as "relevant foreign income" under one of the provisions listed in Section 830(4) of the ITTOIA.

The charge to tax under Section 761(1)(b)(i) of the ICTA 1988 was not mentioned in either Section 830(2) or Section 830(4) of the ITTOIA;

(g) loss relief against OIGs was preserved by the inclusion in Section 392 of the ICTA 1988 of a reference to income falling within any of the provisions in a new Section 836B of the ICTA 1988, which included a reference in Part 1 of the table in Section 836B(2) of the ICTA 1988 to income arising under Section 761(1)(b)(i) of the ICTA 1988; and

(h) a new Section 827A of the ICTA 1988 was inserted which expressly acknowledged that certain amounts chargeable to income tax under the provisions specified in Parts 1 and 3 of the table in Section 836B of the ICTA 1988 (which included Section 761(1)(b)(i) of the ICTA 1988) might not have a source;

(5) upon the enactment of the ITA:

(a) Section 1016 of the ITA replaced Section 836B of the ICTA 1988. It:

(i) included a reference to Chapter 8 in Part 1 of the table in Section 1016(2) of the ITA;

(ii) included a reference to Section 761(1)(b)(i) of the ICTA 1988 in Part 3 of the table in Section 1016(2) of the ITA; and

(iii) provided in Section 1016(3) of the ITA that any reference to a provision in Part 1 of the table did "not include that provision so far as relating to relevant foreign income";

(b) Section 1015 of the ITA contained an equivalent acknowledgement to the one in Section 827A of the ICTA – which is to say an acknowledgement to the effect that certain amounts chargeable to income tax under the provisions specified in Parts 2 and 3 of the table in Section 1016(2) of the ITA (which included Section 761(1)(b)(i) of the ICTA 1988) might not have a source; and

(c) the loss provisions in Section 392 of the ICTA 1988 were re–enacted in Section 152 of the ITA. This provided that losses arising from transactions falling within one of the provisions specified in Section 1016 of the ITA could be set off against income arising from any such transactions. Since Section 761(1)(b)(i) of the ICTA 1988 was one of the provisions so specified, this meant that the relevant losses could be set off against OIGs although Section 152(8) of the ITA provided that losses arising from the disposal of interests in offshore funds could not be set off under the section;

(6) in 2008, as a result of changes to the remittance basis made in a new Chapter A1 of Part 14 to the ITA:

(a) Section 761(5) of the ICTA 1988, which, as noted in paragraph 23(2)(c) above, provided for Section 12 of the TCGA to apply to individuals who did not have a UK domicile, was repealed;

(b) Section 762ZB(2) of the ICTA 1988, which provided that income treated as arising under Section 761(1) of the ICTA 1988 to a non–UK domicile was to be treated as "relevant foreign income" of the non–UK domicile, was inserted; and

(c) that section was added to the list in Section 830(4) of the ITTOIA of enactments giving rise to "other income" which was "relevant foreign income";

(7) in 2009, following the enactment of Sections 41, 42 and 42A of the FA 2008, the OIGs legislation was moved from the ICTA 1988 to the OFTR. The key provisions in the OFTR so far as the present appeal is concerned are:

(a) Regulation 17, which states that a charge to tax arises if there is an OIG;

(b) Regulation 18, which states that:

(i) the OIG is to be treated for all purposes of the Tax Acts as income which arises at the time of the disposal to the person making the disposal;

(ii) the tax is charged on the person making the disposal (or treated as making the disposal); and

(iii) "in the case of a person chargeable to income tax, tax is charged under Chapter 8 …. (miscellaneous income: income not otherwise charged) for the year of assessment in which the disposal is made, but sections 688(1) and 689 of [the ITTOIA] (income charged and person liable) do not apply" – see Regulation 18(3));

(c) Regulation 19, which replaced Section 762ZB(2) of the ICTA 1988 and states that income which is treated as arising under Regulation 17 to a non–UK domicile is to be treated as "relevant foreign income" of the non–UK domicile; and

(d) Regulation 21(2), which states that:

(i) Chapter 2 of Part 13 of the ITA applies in relation to an OIG arising to a person resident or domiciled outside the UK as if the OIG were income becoming payable to that person; and

(ii) income treated as so arising under that chapter is to be regarded as "relevant foreign income" of a non–UK domicile to whom the income is deemed to arise under Section 720 of the ITA;

(8) upon the enactment of the OFTR:

(a) the reference in Section 830(4) of the ITTOIA to Section 762ZB(2) of the ICTA 1988 was replaced by a reference to Regulation 19; and

(b) the reference in Part 3 of the table in Section 1016(2) of the ITA to Section 761(1)(b)(i) of the ICTA 1988 was replaced by a reference to Regulation 17;

(9) upon the enactment of the Finance Act 2015 (the "FA 2015"), Section 152 of the ITA was amended so as to prevent losses from being set off against income arising pursuant to Regulation 17 – see Section 152(2A) of the ITA; and

(10) the Finance Act 2016 (the "FA 2016") inserted a new Part 9A into the ITA, which included provisions imposing income tax on disposals of land in the UK and disposals of property deriving at least 50% of its value from land in the UK – see Sections 517C and 517E of the ITA. A reference to those provisions was inserted by Section 79(11) of the FA 2016 into Section 830(3) of the ITTOIA so that they were expressly stated to be provisions giving rise to income which was not "relevant foreign income".

Common ground – OIGs

24. It is common ground that:

(1) in order for income arising in an offshore trust or company to be PFSI in relation to an individual for the purposes of Section 720 of the ITA, that income needs to be such that it would have been "relevant foreign income" if it had instead arisen to the individual in question – see Sections 721A(3)(a) and 721A(4)(a) of the ITA;

(2) in order for that to be the case, unless the income in question falls within one of the categories of "other income" comprising "relevant foreign income" mentioned in Section 830(4) of the ITTOIA:

(a) the income must be treated as having arisen from a source; and

(b) that source must be outside the UK

– see Sections 830(1) and 830(2) of the ITTOIA;

(3) it is in general no longer necessary for income to have a source before it can be subject to income tax. In *Walker v Centaur Clothes Group Ltd* [2000] UKHL 23 ("*Walker*"), Lord Hoffmann (with whom the other Law Lords agreed) held at 803D to 803G that it was no longer the case that income within the charge to tax as income was restricted to income derived from a source. As Park J later remarked in *Pumahaven v Williams* [2002] EWHC 2237 (Ch) ("*Pumahaven*") at paragraphs [19] to [21], "the source doctrine is…subject to any detailed statutory provisions to the contrary" and "there are several statutory exceptions to the source doctrine". Similar views were expressed by Henderson LJ in *Moorthy v The Commissioners for Her Majesty's Revenue and Customs* [2018] EWCA Civ 847 ("*Moorthy*") at paragraph [35]. Consistent with those views, the schedular system of income tax was abolished as part of the Tax Law Rewrite Project; and

(4) however, it is implicit in the wording of Section 687 that, in order for income to be taxable under that section, it necessarily must have a source. This is because the section refers explicitly to a source in its terms and it was held by the Court of Appeal in *The Commissioners for His Majesty's Revenue and Customs v BlueCrest Capital Management LP and others* [2023] EWCA Civ 1481 ("*BlueCrest*") that income which is taxable under that provision "must arise from an identifiable source in the relevant tax year" – see Sir Launcelot Henderson (with whom Lewison and Falk LJJ agreed) at paragraph [102]. Previously, the Upper Tribunal in *Kerrison v The Commissioners for Her Majesty's Revenue and Customs* [2019] UKUT 0008 (TCC) ("*Kerrison*") had evidently been of the same view – see *Kerrison* at paragraph [70] – although they had left the point open because it was not necessary for them to decide it on the facts in that case.

The Appellant's submissions – OIGs

25. Ms Hardy, representing the Appellant along with Mr Marre, said that, whilst she did not disagree with the legislative background we have described in paragraph 23 above, it was ultimately of little relevance to the determination of Issue One in relation to the OIGs, particularly in the light of the warning given by Lord Carnwath JSC in *Derry* at paragraphs [9] and [10] to the effect that, when construing a consolidating statute, it should not be necessary to refer back to the form taken by the legislation before the consolidation.

26. In her view, applying the principles of statutory construction referred to in paragraph 20 above, at the time when the OIGs in this case arose in a Trust or Hilarion:

(1) they would have been "relevant foreign income" for the Appellant if they had instead arisen to the Appellant; and

(2) they were therefore PFSI, as defined in Sections 721A(3)(a) and 721A(4)(a) of the ITA, for the purposes of determining the Appellant's liability to income tax in respect of the OIGs under Section 720 of the ITA.

27. As regards paragraph 26(1) above, Ms Hardy said that the reasons why the OIGs would have been "relevant foreign income" for the Appellant at the time they arose had they arisen to the Appellant were that:

(1) Regulation 17 and Regulation 18(3) made it clear that the charge to income tax on OIGs fell within Chapter 8;

(2) the only charging provision in Chapter 8 was Section 687;

(3) since OIGs were charged to income tax under Section 687, they must be deemed to have a source as noted in *BlueCrest* and *Kerrison*;

(4) that source had to be a foreign source because, by definition, OIGs arose as a result of the realisation of gains on interests in offshore funds;

(5) it followed that, if the OIGs had arisen to the Appellant, they would have fallen within Section 830(1) of the ITTOIA – by virtue of the reference, in Section 830(2) of the ITTOIA, to Chapter 8;

(6) there was no reference to Chapter 8 or OIGs in the exclusions set out in Section 830(3) of the ITTOIA; and

(7) therefore, if the OIGs had arisen to the Appellant, they would have been "relevant foreign income" falling within Section 830 of the ITTOIA and Section 989 of the ITA in the hands of the Appellant.

28. In short, Ms Hardy said that the provisions in the OFTR were deeming provisions and, as had been noted in *Fowler* and *Vermilion*, deeming provisions created a fiction to which

effect should be given unless they created an absurd or anomalous result which was not compelled by clear language. In this case, the clear language in the OFTR provisions compelled the conclusion that the OIGs must have a source because that was the only way in which they could be brought into charge under Section 687 and that section was the only charging provision within Chapter 8.

29. She added that, if we were to conclude that the OIGs did not have a source, then they could not be brought into charge to tax at all because they could not be subject to tax under Section 687. In that case, the legislative framework was defective because Regulation 18(3) was referencing a provision which had no way of applying. The Appellant reserved the right to argue that point on any further appeal in the proceedings.

30. In support of her proposition that the OIGs would have been "relevant foreign income" for the Appellant if they had instead arisen to the Appellant, Ms Hardy said that:

(1) it was clear that other receipts of a capital nature which gave rise to deemed income were capable of amounting to "relevant foreign income" falling within the ambit of Section 830(1) of the ITTOIA by virtue of Section 830(2) of the ITTOIA and therefore as having a foreign source. For example, prior to its repeal, Chapter 13 of Part 4 of the ITTOIA, which imposed tax on the proceeds of selling foreign dividend coupons, had been included in Section 830(2) of the ITTOIA; and

(2) although the OFTR did not contain an equivalent to Section 428(3) of the ITTOIA – which deemed profits arising on the disposal of deeply–discounted foreign securities to arise from a source outside the UK – or Section 658(2) of the ITTOIA – which deemed estate income arising from a foreign estate to arise from a source outside the UK – those were cases where Parliament wished to put the foreign source of the relevant income beyond doubt. The absence of any such provision in relation to OIGs did not mean that OIGs did not have a foreign source.

31. As regards paragraph 26(2) above, Ms Hardy said that, once it was accepted that the OIGs would have been "relevant foreign income" for the Appellant if they had instead arisen to the Appellant, then the OIGs must be PFSI because, on a purposive construction of the definition of PFSI in Sections 721A(3) and 721A(4) of the ITA, Parliament did not intend to exclude OIGs from being PFSI.

32. In support of that proposition, Ms Hardy said that:

(1) when the deemed domicile rules were introduced in 2017, the intention of Parliament was that an individual who had settled a non–UK settlement while he or she was a non–UK domicile and who was deemed to become a UK domicile as a result of the changes should continue to be outside the charge to tax on the foreign income and gains of the relevant non–UK settlement and any non–UK company beneath that settlement until those income and gains were paid out of the offshore structure;

(2) to that end, Parliament had made provision in the income tax context in Section 721A of the ITTOIA for PFSI to be outside the scope of income tax on an arising basis and an equivalent provision in the capital gains tax context in paragraph 5A of Schedule 5 to the TCGA;

(3) the background to the enactment of the F (No 2) A 2017 demonstrated this intention very clearly. For instance:

(a) in July 2015, HM Treasury had published a technical paper which said as follows:

"Non doms who have set up an offshore trust before they become deemed domiciled here under the 15 year rule will not be taxed on trust income and gains that are retained in the trust and such excluded property trusts will have the same IHT treatment as at present (subject to the announcement made at Budget 2015 on UK residential property held through offshore companies and similar vehicles). However, such long term residents will, from April 2017 be taxed on any benefits, capital or income received from any trusts on a worldwide basis. The government will consult on the necessary changes to the transfer of assets regime and Capital Gains Tax trust provisions. The government recognises that this is a significant change to the current rules and that changes to trust taxation are complex and will need to be considered carefully";

(b) the consultation document of 30 September 2015 (updated on 19 August 2016) which followed that technical paper said as follows:

"3.2 Treatment of offshore trusts

The government said at the outset of these reforms that it intended there to be some protection for those individuals who had set up offshore trusts before they became deemed-domiciled. Wealthy families who have set up a trust of some sort, possibly many years ago and while they were not living in or considering a move to the UK, will find it very punitive and administratively burdensome to have to recreate sufficient history of the transactions that may have taken place in the trust that would be necessary if the settlor were to be taxed on income and gains in the same way as an individual who is UK domiciled.

The government thinks it is fair to ask any individual who becomes deemed-domiciled in the UK to pay tax on benefits they receive from any offshore trust and any underlying entities.

However, the government does not intend that non–domiciliaries who become deemed-UK domiciled should have to pay UK tax on income and gains in offshore structures which were set up before they became deemed–domiciled simply because the individual was the settlor of the trust or was considered a transferor under the Transfer of Assets Abroad legislation. As a part of these reforms, the government will ensure that any individual who becomes deemed – UK domiciled will continue to be protected from UK tax on offshore trusts that they have settled while neither they nor their spouse or children receive any benefit from the trust.

The government intends to base the new rules on the taxable value of benefits received by the deemed domiciled individual without reference to the income and gains arising in the offshore structure";

(c) the consultation outcome document of December 2016 said as follows:

"2.3.3

Under the government's alternative approach, foreign income arising in overseas trusts (or any underlying corporate structure) set up by a non-dom will not be taxed on the settlor on an arising basis when the individual becomes deemed domiciled under the 15/20 test. The existing settlor charges under both the settlements legislation and Transfer of Assets Abroad legislation will be dis- applied to such income both where the settlor is deemed domiciled and where the settlor remains foreign domiciled for tax purposes. There will be no changes to the taxation of foreign income for overseas trusts set up by UK domiciled settlors.

Instead, such foreign income will be taxed on the foreign domiciled or deemed domiciled settlor only by reference to the benefits received by the settlor or close family members and where those benefits are not already subject to income tax in the hands of the recipient. The trust provisions will still remain in place even after a benefit has been received so tax is paid on amounts paid out of the trust, but amounts that remain in the trust will not be taxable. The settlor will be taxed on the remittance basis if they are non-domiciled and a remittance basis user, or on benefits received worldwide if they are deemed domiciled.

The settlor charges under the transfer of assets legislation will be dis-applied at the trust level and in respect of any underlying corporate structure without the need for the underlying company to pay dividends up to the trust. The settlor charges under the settlements legislation will not need to be dis-applied to foreign income of any corporate structure underlying the settlement, because the settlements legislation only applies to income arising to a settlement.

The trust provisions will not apply to any transferor who has become deemed domiciled and owns a non−resident company which is not held in trust. In these circumstances section 720 to 730 ITA 2007 will apply to the settlor as to a UK domiciled transferor. The remittance basis will continue to apply as at present to a foreign domiciled transferor in relation to corporate income where there is no trust structure."; and

(d) at the Public Bill Committee, Fourth Sitting, 19 October 2017, Mel Stride MP for the Government explained the purpose of the trust protections as follows:

"The provisions outlined in schedule 8 relate to trusts that were created before an individual became deemed domiciled under the new rules. As I am sure members of the Committee will appreciate, many non-doms will have set up family structures in their home country long before they ever considered moving to the UK. That is an important point. The Government believe that it would be unreasonable to expect individuals in such circumstances to pay UK tax on all the money in such a structure as it arose. The provisions therefore protect such trusts from unintended consequences and ensure that the UK remains an attractive place for those individuals to live and work.

Let me be clear: even with those protections in place, those non-doms who do become deemed UK-domiciled will only be protected on income and gains that remain inside the trust. Any moneys withdrawn, or benefits provided, will lead to a tax charge.

The Government recognise that non-doms make an important contribution to the UK's economy. In terms of tax alone, as I have already stated, they contribute more than £9 billion to the Exchequer per year. It is therefore vital that these changes are not introduced in a way that would drive non-doms out of the UK altogether";

(4) thus, applying the purposive approach to statutory construction which both parties agreed should be the basis on which to construe the legislation, it could be seen that all "relevant foreign income", whether actual or deemed, was intended to fall within the definition of PFSI; and

(5) moreover, it was clear that OIGs were "relevant foreign income" for non–UK domiciles immediately before the enactment of the F (No 2) A 2017 – even if for no other reason than by virtue of Regulation 19 – and there was no indication in the materials described above that Parliament intended to change the status of OIGs arising in non–

UK settlements and non–UK companies beneath those settlements when it enacted the F (No 2) A 2017. Indeed, the legislation in question had been enacted for the very purpose of protecting individuals such as the Appellant who were deemed to become UK domiciles by virtue of the legislation in question.

Conclusion – OIGs

Introduction

33. We have not summarised the submissions made by Mr Fell, on behalf of the Respondents, in relation to OIGs and Issue One for the simple reason that, with the exception of the one point discussed in paragraphs 50 to 53 below, we agree with them.

34. In short, we consider that, for the reasons which follow, when the principles of statutory construction outlined in paragraph 20 above are applied to the relevant legislation in this case:

(1) OIGs are not, and never have been, "relevant foreign income" as defined in Section 830 of the ITTOIA and Section 989 of the ITA for anyone apart from an individual with a non–UK domicile who is subject to the remittance basis. Therefore, had the OIGs in this case arisen to the Appellant, an individual who was a UK domicile when the OIGs arose, they would not have been "relevant foreign income"; and

(2) consequently, the OIGs in this case are not capable of constituting PFSI so far as the Appellant is concerned.

The OIGs as "relevant foreign income" for UK domiciles

No source

35. As regards the conclusion set out in paragraph 34(1) above, we consider that the structure of the legislation makes it apparent that OIGs do not have a source. We say that because:

(1) OIGs are capital sums which are not actual income but are instead deemed to be income. As such, they are an example of a type of income which does not have a source in the traditional sense. In *Walker* at paragraph 803F, Lord Hoffmann gave, as a specific example of income which does not have a source, "the receipt of a capital sum from a particular kind of transaction, which is deemed to be taxable income received in that year of assessment…". The same point was made in the explanatory notes to the ITTOIA at paragraphs 1479, 1480, 2254, 3084 and 3085 and it is expressly acknowledged in Section 577(4) of the ITTOIA that not all items of income falling within Part 5 of the ITTOIA – of which Chapter 8 forms part – have a source;

(2) having said that, if Regulation 18(3) is properly to be construed as making OIGs subject to tax under Section 687, then a necessary consequence of that construction, applying the principles of statutory construction described in paragraph 20 above, and particularly the principles applicable to deeming described in *Fowler* and *Vermilion,* is that OIGs must be deemed to have a source because, as noted in *BlueCrest* and *Kerrison*, income cannot be taxable under Section 687 unless it has a source. If OIGs were to be subject to tax under Section 687, and yet not have a source, then the legislative machinery would break down;

(3) however, even before taking into account the legislative history of OIGs described in paragraph 23 above, which we analyse in paragraph 55 below, it is apparent that Regulation 18(3) does no such thing. Instead, it brings OIGs within the charge to tax under Chapter 8 and not Section 687. The regulation refers expressly to Chapter 8 and not to Section 687 and we consider that to be perfectly deliberate and significant. For the reasons which follow, we do not agree with Ms Hardy that the mere fact that Section

687 is the only charging provision in Chapter 8 means that Regulation 18(3) should be read as bringing OIGs within the charge to tax under Section 687;

(4) nor do we agree with Ms Hardy that treating OIGs as being taxable in that way defeats the purpose of the deeming in Section 18(3). On the contrary, we think that it is entirely consistent with that deeming and does not produce an unjust or anomalous result. Instead, for reasons on which we will elaborate, we think that deeming the charge to arise under Section 687 would produce unjust and anomalous results and would therefore be contrary to the principles outlined in *Fowler* and *Vermilion*;

(5) the intended effect of Regulation 18(3) in our view is simply to bring OIGs within the charge to income tax as items of miscellaneous income in Chapter 8. In other words, Regulation 18(3) sits alongside, and performs an equivalent role to, Section 687 as a provision which brings amounts into charge under that chapter.

Indeed, the language in Section 687 itself supports that view. Section 687 applies only to "income …that is not chargeable to income tax under or as a result of any other provision of this Act or any other Act". OIGs are subject to income tax as a result of Sections 41(1) and 42 of the FA 2008, the provisions which enabled the enactment of Regulation 17 and Regulation 18(3). As a result, they are already subject to tax under Chapter 8 as a result of another Act. Section 687 is therefore precluded from applying.

It is a matter of speculation as to why Parliament felt that it was necessary to bring the charge in respect of OIGs within the ambit of Chapter 8, given that Regulation 18(3) could have imposed a self–standing charge to income tax without recourse to any part of the ITTOIA but we think that the most likely explanation is one that was proffered by Mr Fell, which is that bringing the charge within Chapter 8 fitted the charge within the taxonomy of the tax legislation as a whole. Although the Tax Law Rewrite Project removed the schedular system of income taxation, the ITTOIA and the ITA still bear its hallmarks and it would be entirely understandable that Parliament might have wished to include miscellaneous charges to income tax, such as the charge in respect of OIGs, within Chapter 8 by way of cross–reference as opposed to leaving them as self–standing charges outside that primary legislation.

That view is supported by the fact that a similar approach was adopted in relation to corporation tax. For corporation taxpayers, Regulation 18(4) brings OIGs within the charge to corporation tax under Chapter 8 of Part 10 of the Corporation Tax Act 2009 (the "CTA 2009"), the chapter which applies to income not otherwise chargeable. Again, the charge could have been left in the OFTR as a self–standing charge to corporation tax but Parliament took steps to bring the charge within the ambit of the taxonomy of the Corporation Tax Acts as a whole. Moreover, when Regulation 18(3) is read in conjunction with Regulation 18(4), it becomes clear that the reference to Chapter 8 in Regulation 18(3) is perfectly deliberate. In both cases, the relevant regulation refers to a chapter and part of the primary consolidated legislation and not a specific section number.

In passing, we would note that the charging provision within Chapter 8 of Part 10 of the CTA 2009 – Section 979 of the CTA 2009 – does not refer to source.

36. In support of her proposition that OIGs were subject to income tax under Section 687 and not Chapter 8, Ms Hardy made two points in addition to her reliance on the fact that Section 687 was the only charging provision in Chapter 8.

37. The first was that the language used in Regulation 18(3) – to the effect that "tax is charged under Chapter 8 … (miscellaneous income: income not otherwise charged) for the year of assessment in which the disposal is made" – was very similar to the language used in Section

687 itself – to the effect that "[income] tax is charged under this Chapter on income from any source that is not charged to income tax under or as a result of any other provision of this Act or any other Act".

38. The second was that, apart from Section 687, Chapter 8 contained only three provisions, two of which (Sections 688 and 689 of the ITTOIA) were expressly precluded from operating in the case of OIGs by Regulation 18(3) and the third of which (Section 689A of the ITTOIA) post–dated the enactment of the OFTR and related to temporary non–residents so that it was irrelevant in this context. Ms Hardy said that this further supported the proposition that the reference in Regulation 18(3) to Chapter 8 must be read as a reference to Section 687.

39. We think that, on the contrary, both of those points tend to support our conclusion rather than cast it into doubt.

40. As regards the first point, we consider that the fact that the language in Regulation 18(3) is so similar to the language in Section 687 suggests to us that Regulation 18(3) is performing precisely the same role as Section 687 in that both provisions are bringing income into charge under Chapter 8. As such, there is no role for Section 687 to play in this regard. Its role – that of bringing income into charge under Chapter 8 – has already been fulfilled by Regulation 18(3).

41. As regards the second point, we consider that the very fact that the other provisions in Chapter 8 are either required by Regulation 18(3) to be expressly disregarded or, in the case of Section 689A of the ITTOIA, post–dated Regulation 18(3) and is effectively irrelevant seems to us to support the conclusion that the reference in Regulation 18(3) to Chapter 8 and not Section 687 was perfectly deliberate. After all, if there was no need to bring any other provision in Chapter 8 into play by virtue of the cross–reference, then why not refer expressly to Section 687 specifically? Moreover, Section 688 of the ITTOIA, which brings Part 8 of the ITTOIA into play in relation to "relevant foreign income", is expressly precluded from applying to OIGs by Regulation 18(3). If OIGs were intended to be "relevant foreign income", that would not have been the case. There would seem to be little point in disapplying a section which brings the provisions relating to "relevant foreign income" into play as regards a particular type of income if the intention was that that type of income should be so treated after all.

Location of source

42. The fact that OIGs have no actual source and are not deemed to have a source by virtue of falling within Section 687 means that they cannot be "relevant foreign income" for a UK resident individual who is UK domiciled by virtue of Section 830(2) of the ITTOIA – see Section 830(1)(a) of the ITTOIA. It is therefore unnecessary for us to consider whether, had OIGs been subject to tax under Section 687 and therefore been deemed to have a source, that source would necessarily have been foreign. However, we will address that question at this stage because it has some relevance in the context of Issue Two.

43. Had we been required to consider the location of the source of OIGs, it would not have been entirely straightforward given that OIGs, as deemed income, do not actually have a source. Since they would merely be deemed to have a source by virtue of falling within Section 687, the location of that source would not be easy to identify by reference to the usual source principles.

44. By way of exemplifying this difficulty, in 2006, the Respondents had to consider whether OIGs counted as eligible income "deriving from shares or securities" for the purposes of the then–definition of "investment trust". In Tax Bulletin IRI 272, they concluded that OIGs did not so qualify because:

"notwithstanding the tax treatment accorded by [Section 761 of the ICTA 1988], the disposal of a material interest is, in essence, a disposal of a capital asset. Whilst [Section 761] deems the gain arising on disposal to be income for the purposes of the Tax Acts it does not recharacterise the source of the deemed income. The deemed income cannot be said to be derived from the share or security in the generally understood sense of "flowing from" the holding of the share or security. It is therefore not eligible income for the purpose of [Section 842 of the ICTA 1988] as it arises from disposal of an asset." (Emphasis added).

45. Consistent with that conclusion, in the Finance Act 2007, Parliament amended the definition of "investment trust" by inserting a new Section 842(3A) of the ICTA 1988 which confirmed that references in that section to income "do not include income treated as arising under [Section 761 of the ICTA 1988]". The same approach was continued in the successor legislation in Sections 1159 and 1160 of the Corporation Tax Act 2010 (the "CTA 2010") – see Section 1160(4) of the CTA 2010 in particular – until the income qualification in the definition of "investment trust" was revoked in 2012.

46. Notwithstanding this difficulty, had we been required to consider where the source of the OIGs would have been if OIGs had been deemed to have a source, we would have concluded that that was outside the UK. This is because:

(1) by definition, OIGs arise on the disposal of interests in offshore funds and therefore the rights under those interests are enforceable outside the UK;

(2) the fact that Regulation 19 deems OIGs to be "relevant foreign income" for non–UK domiciles suggests that Parliament, when it enacted that provision, considered that OIGs should be treated as if they had a foreign source for those taxpayers. Otherwise, such taxpayers would have been subject to tax in respect of OIGs on an arising basis;

(3) a similar point may be made in relation to Regulation 21(2), which deems income arising under Chapter 2 of Part 13 of the ITA in relation to OIGs to be "relevant foreign income" in the case of a non–UK domicile; and

(4) in this regard, it is noteworthy that, whereas Section 670A of the ITA is expressed to apply only to accrued income profits arising as a result of the transfer of "foreign securities" – which is to say, securities the income on which would be "relevant foreign income" – and a similar approach is evident in Sections 428 and 658 of the ITTOIA – each of which distinguishes between profits on securities outside the UK and other profits of the relevant type – Regulations 19 and 21 contain no such limitation. It is simply assumed that OIGs are foreign source income.

47. We note that the, now–repealed, Chapter 13 of Part 4 of the ITTOIA, which applied to the proceeds of sale of foreign dividend coupons and therefore operated in a similar manner to the OFTR in deeming to be income proceeds of sale which might otherwise have fallen to be regarded as capital, provided expressly that such proceeds of sale were to be treated as arising from "foreign holdings" (see Sections 570(1) and 570(2) of the ITTOIA) and that there is no equivalent to that language in the OFTR. However, in our view, that omission sheds no light on where the source of OIGs, were they deemed to have a source, would be located. On the contrary, it is entirely consistent with the conclusion we have reached to the effect that OIGs do not have an actual source or a deemed source.

48. It is clear from the terms of Section 572 of the ITTOIA (which expressly referred to Part 8 of the ITTOIA) and the reference to Chapter 13 of Part 4 of the ITTOIA in Section 830(2) of the ITTOIA that Parliament's intention was that income falling within that chapter was to be treated as "relevant foreign income". That was why the chapter appeared in the list of provisions set out in Section 830(2) of the ITTOIA to which Section 830(1)(b) of the ITTOIA

refers. However, that reference alone was insufficient for income falling within that chapter to constitute "relevant foreign income" because an additional requirement of Section 830(1) of the ITTOIA was that any income chargeable by a provision referred to in Section 830(2) of the ITTOIA could be "relevant foreign income" only if it arose from a source outside the UK. For that reason, it was necessary for Parliament to provide expressly in Section 570 of the ITTOIA that the income arising under that chapter arose from a foreign holding.

49. It is not surprising that a similar approach was not adopted in relation to OIGs. Not only did OIGs not have an actual source or a deemed source, for the reasons articulated above, but they were also not intended to be "relevant foreign income" except in circumstances where Regulation 19 applied. There was thus no need for Parliament to specify where the source of OIGs would have been located if OIGs had had an actual source or a deemed source.

50. Mr Fell submitted that the Court of Appeal decision in *BlueCrest* at paragraphs [119] to [124] was authority for the proposition that, if OIGs were deemed to have a source, that source would be the place where the decision to make the disposal of the interest in the offshore fund giving rise to the OIGs was taken. We do not agree that *BlueCrest* does establish so broad a principle. The Court of Appeal in *BlueCrest* was addressing the question of whether the source of the income which was the subject of that case was the underlying trade of the partnership that gave rise to the income or was instead the decision of the corporate partner to make allocations to the appellants of capital reflecting the income of that underlying trade, which was the more immediate cause of the taxable income in question for the appellants.

51. In our view, both that case and the decision in *Cunard's Trustees v Commissioners of Inland Revenue* (1946) 27 TC 122, which was cited by the Court of Appeal in its decision, were dealing with the identification of the source of a particular category of income on the specific facts of the cases in question, which involved the exercise of a discretion as the most proximate cause of the sums received by the taxpayers. The same is true of the Court of Appeal decision in *The Commissioners for His Majesty's Revenue and Customs v HFFX LLP* [2024] EWCA Civ 813, which followed *BlueCrest*. (The other case cited by the Court of Appeal in this context in *BlueCrest* – the Upper Tribunal decision in *Spritebeam Limited v The Commissioners for Her Majesty's Revenue and Customs* [2015] STC 1222 – was dealing with a different question, which was whether income arising pursuant to a legal obligation owed to someone other than the recipient of the income can be said to have a source for the recipient notwithstanding that the recipient cannot enforce the obligation to pay. As such, it has no relevance in this context.)

52. None of the above decisions seems to us to establish a more general principle to the effect that the source of income that is deemed to arise as a result of the disposal of a capital asset should be regarded as being the place where the decision to make the disposal was made, as opposed to, for example, the location where the rights attaching to the asset which was the subject of the disposal were enforceable.

53. Moreover, there are a number of reasons for concluding that Mr Fell's approach to identifying the source of OIGs cannot be the correct. Those are that:

(1) first, it would make the location of the source of OIGs entirely arbitrary, as it would depend on where the disponor happened to be when the decision to make the disposal giving rise to the OIGs in question was taken. That, in turn, would mean that some OIGs arose abroad and some OIGs arose in the UK without any indication in the legislation of a distinction between them;

(2) secondly, it would be inconsistent with the clear understanding which is implicit in Regulations 19 and 21(2), as referred to in paragraphs 46(2) and 46(3) above, to the effect that OIGs always have a foreign source. After all, many OIGs are realised as a result of

decisions taken in the UK. If that meant that those OIGs had a UK source, why would they not be subject to tax in the hands of non–UK domiciles in the same way as other UK source income, which is to say on an arising basis? The very fact that the remittance basis is stated to apply to OIGs realised by non–UK domiciles is indicative of the fact that OIGs have always been considered by Parliament to have a foreign source; and

(3) finally, in the specific context of the PFSI definition, which is based on a hypothetical scenario and not the circumstances of the actual disposal that has given rise to the OIGs in question – which is to say, would the OIGs in question have been "relevant foreign income" in the hands of the individual who is being assessed under Section 720 of the ITA – the answer cannot depend on where the hypothetical decision to make the disposal that would have given rise to the OIGs for the individual would have been taken by the individual in question. The mere fact that the individual is UK resident does not mean that the individual would necessarily have taken that decision in the UK. He or she might well have been outside the UK at the relevant time. Consequently, it would make no sense for the source of OIGs to depend on where the decision to make the disposal giving rise to the OIGs was taken.

54. For the above reasons, if we had been called upon to decide the point in determining Issue One, we would have held that the deemed source of OIGs was always outside the UK because that is where the rights attaching to the interests in the offshore fund whose disposal has given rise to the OIGs are enforceable. Whilst the fact that we have concluded that OIGs do not have either an actual source or a deemed source means that the question of how to identify the location of any source for the OIGs in the context of Issue One is moot, a somewhat similar question arises in the context of Issue Two. It is for that reason that we have gone into the detail we have on this question in paragraphs 42 to 53 above.

Legislative history – OIGs

55. The conclusion we have drawn to the effect that OIGs are not "relevant foreign income" except in the circumstances where Regulation 19 deems them to be so gains considerable support when the legislative history of OIGs is taken into account. For example:

(1) during the period prior to the abolition of the schedular system by the Tax Law Rewrite Project, OIGs were subject to tax under Schedule D Case VI pursuant to the FA 1984 and then the ICTA 1988 and the remittance rules which applied to them were those set out in the capital gains tax legislation – initially Section 14 of the CGTA and then Section 12 of the TCGA. This suggests that Parliament viewed OIGs as something other than income from foreign securities or possessions because, had that been the case, the relevant charge would have been imposed under either Schedule D Case IV or Schedule D Case V and the remittance rules which applied to OIGs would have been the remittance rules in the ICTA 1970 and the ICTA 1988 which applied to income chargeable under those cases;

(2) the phrase "relevant foreign income" made its first appearance in the legislation when the ITTOIA was enacted as part of the Tax Law Rewrite Project. According to paragraph 3061 of the explanatory notes to the ITTOIA, the label "relevant foreign income" was introduced "to describe the income and other amounts charged to income tax in this Act that are charged under Schedule D Cases IV or V in the source legislation".

Consistent with that approach, at that time, and indeed throughout the period from the enactment of the ITTOIA in 2005 until the enactment of the OFTR in 2009, OIGs were demonstrably not "relevant foreign income" for individuals who were domiciled in the UK. This is because OIGs continued to be subject to income tax under Section

761(1)(b)(i) of the ICTA 1988 and there was no reference to that section in either Section 830(2) or Section 830(4) of the ITTOIA.

It follows that, in order for OIGs now to constitute "relevant foreign income" for a UK domicile, it is necessary to conclude that, when the OFTR was enacted with the cross reference in Regulation 18(3) to Chapter 8, items of income which had not hitherto been "relevant foreign income" for UK domiciles now fell within that definition.

We have been presented with no evidence that Parliament intended to make so fundamental a change at that time. Indeed, paragraph 5.22 of the discussion paper which was published by HM Treasury before the OFTR was enacted, entitled "Offshore funds: a discussion paper", simply stated that "the Government is proposing that the current offshore income gains treatment be retained". If so fundamental a change to the treatment of OIGs for income tax purposes had been intended, we would have expected that to be mentioned at the consultation stage;

(3) the introduction of Section 762ZB of the ICTA 1988 in 2008 and then the enactment of its successor, Regulation 19, in 2009 – and the cross references to those provisions in Section 830(4) of the ITTOIA as "other income" that qualifies as "relevant foreign income" – suggest that OIGs are not "relevant foreign income" for UK domiciles. This is because those sections expressly state that OIGs are to be treated as "relevant foreign income" for non–UK domiciles. We recognise that arguments from redundancy carry limited weight, as noted by Lewison LJ in *DMWSHNZ v The Commissioners for Her Majesty's Revenue and Customs* [2015] EWCA Civ 1036 at paragraph [38] and Lord Hoffman in *Walker* at 805D. As such, we might well hesitate to base our conclusion solely on the existence of these provisions. However, the fact that the terms of these provisions are entirely consistent with the conclusion we have reached for other reasons tends to support that conclusion;

(4) it is apparent from the legislative history that the phrase "relevant foreign income" has relevance in two distinct areas:

(a) first in ensuring that particular types of income are taxable only on a remittance basis for non–UK domiciles; and

(b) secondly to apply some specific rules for the calculation of particular types of income for individuals who are not non–UK domiciles.

So far as OIGs are concerned, the first of those areas has been dealt with since 2005 by the express rule in Section 762ZB(2) of the ICTA 1988 and then Regulation 19. Those provisions make it clear, however, that OIGs are "relevant foreign income" only for those individuals who are non–UK domiciles.

As for the second of those areas, the computational rules in question are set out in Part 8 of the ITTOIA. That part includes Section 838 of the ITTOIA, which provides that, when calculating the amount of "relevant foreign income" which is to be subject to tax, a deduction is allowed for expenses incurred outside the UK that are attributable to the payment or collection of the income in question. It is hard to see how that provision can have been intended to apply to OIGs. In the first place, "collection" and "payment" are concepts which are difficult to apply in relation to OIGs. More significantly, the OFTR contains detailed rules in Regulations 38 and 39 for the calculation of OIGs by reference to capital gains tax principles. Those principles include Section 38 of the TCGA, which sets out detailed rules for determining the amounts which are allowable in calculating the gain in question. It is inconceivable that Parliament would have intended the deductions for "collection" and "payment" in Section 838 of the ITTOIA to have applied in addition

to Section 38 of the TCGA in the determination of the amount of OIGs to be subject to tax.

Tellingly in our view, in the one circumstance where OIGs qualify as "relevant foreign income" – which is to say, where the remittance basis applies in the case of a non–UK domicile by virtue of Regulation 19 – Section 838 of the ITTOIA is precluded from applying – see Sections 832 and 838(2) of the ITTOIA;

(5) there are provisions elsewhere in the legislation which are designed to make it clear that particular types of income have a foreign source and are subject to Part 8 of the ITTOIA – see Sections 428 and 658 of the ITTOIA. The purpose of those provisions was outlined in the explanatory notes to the ITTOIA at paragraph 3085. No equivalent provision is made in relation to OIGs. Whilst it is conceivable that this was because the status of OIGs as "relevant foreign income" was sufficiently clear without needing an express provision to that effect, we think that a more likely explanation is that OIGs have never been considered to be "relevant foreign income" except in the circumstances described in Section 762ZB(2) of the ICTA 1988 and then Regulation 19;

(6) when construed in the light of the explanatory notes to the ITTOIA, both Sections 827A and 836B of the ICTA 1988 and Section 1015 of the ITA can be regarded as acknowledging that OIGs do not have a source because:

(a) Section 827A of the ICTA 1988 acknowledged that an amount arising from one of the provisions listed in Parts 1 and 3 of the table in Section 836B of the ICTA 1988 might not have a source and Section 761(1)(b)(i) of the ICTA 1988 was listed in Part 1 of that table; and

(b) Section 1015 of the ITA acknowledges that an amount arising from one of the provisions listed in Parts 2 and 3 of the table in Section 1016(2) of the ITA may not have a source and Regulation 17 is listed in Part 3 of that table;

(7) if OIGs were intended to be "relevant foreign income" for UK domiciles, then the way that Section 1016 of the ITA is set out would make no sense. That is because:

(a) Chapter 8 is included in Part 1 of the table in Section 1016(2) of the ITA whereas Regulation 17, which feeds into the charge to tax under Chapter 8, is included in Part 3 of the table in that section; and

(b) there is then a provision – Section 1016(3) of the ITA – which states that "any reference to any provision of ITTOIA 2005 does not include that provision so far as relating to relevant foreign income".

It follows that, if OIGs were to be "relevant foreign income", the reference to Chapter 8 in Part 1 of the table in Section 1016(2) of the ITA could not apply to them, but the reference to Regulation 17 in Part 3 of the table in that section would remain applicable. It is unclear how that interaction would work but the exclusion from Chapter 8 would certainly mean that no reliance could be placed on Section 687 to establish a source for OIGs. In addition, it would mean that, prior to the change to Section 152 of the ITA made by the FA 2015, when losses could still be set off against income charged to tax under Section 1016 of the ITA, some doubt would have arisen over whether losses could be set off against OIGs because OIGs were charged to tax under Chapter 8 and not Regulation 17 itself; and

(8) finally, we note that Section 878(1) of the ITTOIA – which provides that the word "income" is to be treated as including "amounts treated as income (whether expressly or by implication)" – is expressly precluded from applying in Section 687 by Section 687(4)

of the ITTOIA. Since OIGs are clearly deemed income, that exclusion sits somewhat uncomfortably with the Appellant's analysis. In our view, it is further evidence that OIGs are not chargeable to tax under Section 687.

56. For the reasons set out in paragraphs 35 to 55 above, we consider that OIGs are not, and never have been, "relevant foreign income" for a UK domicile.

The OIGs as PFSI

57. As for the conclusion set out in paragraph 34(2) above, given the conclusion in paragraph 56 above, to the effect that OIGs are not "relevant foreign income" for a UK domicile, the extra–statutory materials on which the Appellant has relied to show that OIGs were not intended to be excluded from PFSI, whilst they have considerable relevance in the context of Issue Two, cannot assist the Appellant in relation to Issue One.

58. In our view, the language used in each of Sections 721A(3)(a) and 721A(4)(a) of the ITA is clear and unambiguous. A category of income can be PFSI for a UK domicile only if it would have been "relevant foreign income" as defined in Section 830 of the ITTOIA and Section 989 of the ITA had it been received by the UK domicile in question. There is no other way in which those provisions could be construed.

59. It follows that no purposive construction of the definition of PFSI using the principles described in paragraph 20 above can have the result of including within PFSI income that is not "relevant foreign income" for a UK domicile. Since the OIGs would not have been "relevant foreign income" for the Appellant had they arisen to her, they were not PFSI when they arose in a Trust or Hilarion.

60. We therefore find in favour of the Respondents in relation to the OIGs and Issue One.

AIPs

Legislative history – AIPs

61. The legislation pursuant to which the AIPs arose and the background to that legislation is as follows:

(1) the concept of accrued income profits was first introduced in the Finance Act 1985 (the "FA 1985") as an anti–avoidance measure. The aim was to ensure that each holder of securities was subject to tax as income on the interest that accrued on the securities during the holder's period of ownership. Section 73 of the FA 1985 deemed a sum equal to such accrued interest to be income and Section 74 of the FA 1985 provided that, where a person was treated as being entitled to income on that basis, he or she was to be "treated as receiving annual profits or gains…; and the profits or gains shall be chargeable to tax under Case VI of Schedule D".

At that time, as was the case with OIGs, as a result of falling within Schedule D Case VI, losses arising under Schedule D Case VI could be set off against accrued income profits under Section 176 of the ICTA 1970.

Section 75(1)(h) of the FA 1985 provided that accrued income profits arising to non–UK domiciled individuals who would be liable to tax on a remittance basis in respect of interest on the securities transferred under Schedule D Case IV and Schedule D Case V were exempt from tax;

(2) the ICTA 1970 and the FA 1985 were subsequently consolidated in Chapter 2 of Part 17 of the ICTA 1988. Under the ICTA 1988:

(a) accrued income profits remained subject to income tax under Schedule D Case VI pursuant to Sections 713 and 714 of the ICTA 1988;

(b) as a result of the accrued income profits' falling within Schedule D Case VI, losses arising under Schedule D Case VI could be set off against accrued income profits under Section 392 of the ICTA 1988; and

(c) the exemption from tax on accrued income profits arising to a non–UK domiciled individual who would be liable to tax on a remittance basis in respect of interest on the securities transferred under Schedule D Case IV and Schedule D Case V remained (in Section 715(1)(j) of the ICTA 1988).

In short, there was no meaningful change in the treatment of accrued income profits as a result of the consolidating legislation;

(3) Section 46 of the Finance Act 2000 (the "FA 2000") introduced an exemption from tax for the income of charities falling with Schedule D Case VI;

(4) upon the enactment of the ITTOIA:

(a) the schedular system of income tax was abolished;

(b) the charge to income tax under Chapter 2 of Part 17 of the ICTA 1988 was retained;

(c) no reference to that provision was included in Section 830(2) or Section 830(4) of the ITTOIA;

(d) the exemption from tax in Section 715(1)(j) of the ICTA 1988 on accrued income profits arising to a non–UK domiciled individual who would be liable to tax on a remittance basis in respect of interest on the securities transferred under Schedule D Case IV or Schedule D Case V was amended so that the exemption referred instead to accrued income profits arising to an individual who would be liable to tax under Section 832 of the ITTOIA in respect of interest on the securities transferred;

(e) Section 832 of the ITTOIA provided for the remittance basis to apply to a non–UK domicile in respect of "relevant foreign income" and Sections 830(1) and 830(2) of the ITTOIA made provision for interest arising from non–UK securities to be "relevant foreign income";

(f) the reference to Schedule D Case VI in Section 714 of the ICTA 1988 was removed and not replaced by any reference to the ITTOIA;

(g) since accrued income profits did not fall within the charge to income tax under the ITTOIA, loss relief against accrued income profits and the exemption for charities in respect of accrued income profits were preserved by the inclusion in Section 392 of the ICTA 1988 and Section 46 of the FA 2000 of references to income falling within any of the provisions in the new Section 836B of the ICTA 1988, which included a reference in Part 1 of the table in that section to income arising under Section 714(2) of the ICTA 1988; and

(h) a new Section 827A of the ICTA 1988 was inserted which expressly acknowledged that certain amounts chargeable to income tax under the provisions specified in Parts 1 and 3 of the table in Section 836B of the ICTA 1988 (which included Section 714(2) of the ICTA 1988) might not have a source;

(5) upon the enactment of the ITA:

(a) the legislation governing accrued income profits was moved into Part 12 of the ITA. The charge to income tax under that part in Section 714(2) of the ITA echoed the original legislation in the FA 1985 and the ICTA 1988 in that it deemed

the amount equal to the accrued interest to be income which was subject to income tax. There was no reference to a charge under the ITTOIA;

(b) the exemption from tax in Section 715(1)(j) of the ICTA 1988 for non–UK domiciled individuals who would be liable to tax on a remittance basis in respect of interest on the securities transferred under Section 832 of the ITTOIA was re–enacted in Section 644 of the ITA;

(c) the loss provisions in Section 392 of the ICTA 1988 were re–enacted in Section 152 of the ITA. This provided that losses arising from transactions falling within one of the provisions specified in Section 1016 of the ITA could be set off against income arising from any such transactions;

(d) the exemption for charities was re–enacted in Section 527 of the ITA which also referred to the provisions specified in Section 1016 of the ITA;

(e) Chapter 2 of Part 12 of the ITA was included in the list of provisions specified in Part 2 of the table in Section 1016(2) of the ITA (which meant that losses could be set off against accrued income profits and the charity exemption for accrued income profits continued to apply). Although Section 1016(3) provided that any reference in Section 1016 of the ITA to a provision in the ITTOIA "does not include that provision so far as relating to relevant foreign income", that exclusion did not apply to the charge in respect of accrued income profits because that charge was under Chapter 2 of Part 12 of the ITA; and

(f) Section 1015 contained an equivalent acknowledgement to the one in Section 827A of the ICTA 1988 – which is to say an acknowledgement to the effect that certain amounts chargeable to income tax under the provisions specified in Parts 2 and 3 of the table in Section 1016(2) of the ITA (which included Chapter 2 of Part 12 of the ITA) might not have a source; and

(6) the changes made in 2008 to the regime for non–UK domiciles included:

(a) the replacement of the exemption in Section 644 of the ITA by Section 670A of the ITA, which specified that, for a non–UK domicile, AIPs were to be treated as "relevant foreign income"; and

(b) the amendment of Section 830(4) of the ITTOIA to add Section 670A of the ITA as a circumstance where "other income" was to be treated as "relevant foreign income".

Conclusion – AIPs

62. Ms Hardy bravely sought to argue that similar arguments applied to AIPs as applied to OIGs. However, her submission that AIPs should be regarded as falling within the definition of PFSI, purposively construed, foundered on the rock of the ITA, pursuant to which AIPs are chargeable to tax. Since AIPs are subject to tax under Chapter 2 of Part 12 of the ITA and are not, and never have been, subject to tax under any provision of the ITTOIA, there is no reason why they need to be deemed to have a source and there is nothing in the legislation to suggest that they might be "relevant foreign income" for a UK domicile.

63. So far as AIPs are concerned, there is no equivalent argument to the one outlined above in relation to OIGs because:

(1) there is no reference in Section 830(2) of the ITTOIA to any provision within Chapter 2 of Part 12 of the ITA; and

(2) the reference in Section 830(4) of the ITTOIA to Section 670A of the ITA as giving rise to "other income" which is to be treated as "relevant foreign income" makes it clear that income falling within Chapter 2 of Part 12 of the ITA is not "relevant foreign income" except in the circumstances described in Section 670A of the ITA – which is to say, except where they are deemed to be received by a non–UK domicile.

64. As such, a central plank of the Appellant's arguments in relation to OIGs – to the effect that the OIGs are "relevant foreign income" for a UK domicile because OIGs are chargeable under Section 687 and a source is a necessary requirement in order for Section 687 to apply – is not relevant in the case of AIPs and, since income cannot constitute PFSI in the case of an individual settlor unless it would be "relevant foreign income" if received by the individual in question, that is the end of the matter so far as the AIPs are concerned.

65. Many of the points made in paragraph 55 above in relation to the legislative history of OIGs apply equally to the legislative history of AIPs and support the conclusion that AIPs are not "relevant foreign income". For instance:

(1) during the period prior to the abolition of the schedular system by the Tax Law Rewrite Project, AIPs were subject to tax under Schedule D Case VI pursuant to the FA 1985 and the ICTA 1988 and the regime operated by exempting from tax AIPs realised by non–UK domiciled individuals who would have been liable to tax on a remittance basis in respect of interest on the securities transferred. This suggests that Parliament viewed AIPs as something other than income arising in respect of foreign securities in and of themselves because, had that been the case, the regime would simply have imposed the relevant charge under either Schedule D Case IV or Schedule D Case V and the remittance rules which applied to AIPs would have been the remittance rules in the ICTA 1970 and the ICTA 1988 which applied to income chargeable under those cases;

(2) the phrase "relevant foreign income" made its first appearance in the legislation when the ITTOIA was enacted as part of the Tax Law Rewrite Project. According to paragraph 3061 of the explanatory notes to the ITTOIA, the label "relevant foreign income" was introduced "to describe the income and other amounts charged to income tax in this Act that are charged under Schedule D Cases IV or V in the source legislation" rather than amounts charged to tax under Schedule D Case VI. Consistent with that approach, the exemption from tax for non–UK domiciled individuals who would have been liable to tax on a remittance basis in respect of interest on the securities transferred was amended to refer to interest which would have been "relevant foreign income" falling within Section 832 of the ITTOIA but the AIPs regime continued to operate outside the scope of the ITTOIA;

(3) it was only when the exemption from tax for non–UK domiciled individuals who would have been liable to tax on a remittance basis in respect of the interest on the securities transferred because that interest would have been "relevant foreign income" for the purposes of Section 832 of the ITTOIA was replaced by Section 670A of the ITA in 2008 that AIPs themselves were deemed to be "relevant foreign income". That section applied only to non–UK domiciles;

(4) there are provisions elsewhere in the legislation which are designed to make it clear that particular types of income have a foreign source and are subject to Part 8 of the ITTOIA – see Sections 428 and 658 of the ITTOIA. The purpose of those provisions was outlined in the explanatory notes to the ITTOIA at paragraph 3085. No equivalent provision is made in relation to AIPs;

(5) when construed in the light of the explanatory notes to the ITTOIA, both Sections 827A and 836B of the ICTA 1988 and Section 1015 of the ITA can be regarded as acknowledging that AIPs do not have a source because:

(a) Section 827A of the ICTA 1988 acknowledged that an amount arising from one of the provisions listed in Parts 1 and 3 of the table in Section 836B of the ICTA 1988 might not have a source and Section 714(2) of the ICTA 1988 was listed in Part 1 of that table; and

(b) Section 1015 of the ITA acknowledges that an amount arising from one of the provisions listed in Parts 2 and 3 of the table in Section 1016(2) of the ITA may not have a source and Chapter 2 of Part 12 of the ITA is listed in Part 2 of that table; and

(6) Chapter 2 of Part 12 of the ITA contains its own regime in relation to unremittable AIPs in Sections 668 to 670 of the ITA and there would be no need for such provisions if AIPs were "relevant foreign income" because the regime generally applicable to unremittable "relevant foreign income" in Sections 841 to 845 of the ITTOIA would apply.

66. In short, no purposive construction of the definition of PFSI using the principles described in paragraph 20 above can have the result of including, within PFSI, in the case of an individual settlor, income that would not be "relevant foreign income" if received by the individual in question and, since the AIPs would not have been "relevant foreign income" for the Appellant had they arisen to her, they were not PFSI when they arose in a Trust or Hilarion.

67. We therefore find in favour of the Respondents in relation to the AIPs and Issue One.

ISSUE TWO

Common ground

68. In relation to Issue Two, it was common ground that the leading case in relation to the circumstances in which the courts can correct an error in legislation is the House of Lords decision in *Inco Europe Limited v First Choice Distribution* [2000] 1 WLR 586 ("*Inco*"). In *Inco,* the House of Lords held that it was permissible for a court to correct obvious drafting errors in legislation in certain narrowly–defined circumstances. Those were where "the court [is] abundantly sure of three matters:

(1) the intended purpose of the statute or provision in question;

(2) that by inadvertence the draftsman and Parliament failed to give effect to that purpose in the provision in question; and

(3) the substance of the provision Parliament would have made, although not necessarily the precise words Parliament would have used, had the error in the Bill been noticed.

The third of these conditions is of crucial importance" – see Lord Nicholls in *Inco* at 592F.

69. It is not entirely clear from *Inco* whether, if the three stages of the test outlined in that decision are satisfied in a particular case, the relevant court has a duty to correct the obvious error in the legislation or merely has a power to do so. In *Inco* at 592C, Lord Nicholls described the process as part of "the role of the courts in construing legislation", which implies that a court has an obligation to correct the error in such circumstances, in the same way as it always has a general obligation to construe the applicable legislation. However, he then refers, at 592E, to the process as involving the exercise of a "power" by the court. Very little turns on this in the present context because, were we to determine that the three stages of the test in *Inco* were met and that we merely had a power to correct the error in the legislation and not a duty

to do so, we would be likely to exercise that power, given the high threshold implicit in those three stages.

The parties' submissions

70. Although the parties were in agreement that the principles set out in paragraph 68 above should determine whether rectification was appropriate in particular circumstances, they disagreed on how those principles should apply in the present case.

71. Mr Fell submitted that it was far from certain that Parliament intended either category of deemed income to qualify as PFSI. As such, any rectification construction which made the OIGs or AIPs PFSI would amount to an unjustified and impermissible piece of judicial legislating.

72. Ms Hardy said that, if we were to find against the Appellant in relation to Issue One, with the result that OIGs and AIPs fell outside the definition of "relevant foreign income" for a UK domicile and hence fell outside the definition of PFSI, then their omission from the latter definition would be a manifest error in the legislation and contrary to the intention of Parliament. As such, we either had a duty to apply a rectifying construction of the definition of PFSI or we had a power to do so which we should exercise.

73. By way of expanding on the above, Mr Fell said that it was not abundantly clear that OIGs and AIPs were intended to fall within the relieving provisions. Since OIGs and AIPs had never fallen within the definition of "relevant foreign income" for UK domiciles and were items of deemed income arising from anti–avoidance legislation, it was perfectly possible that Parliament did not intend to include them within the relieving provisions. Consequently:

(1) it was not abundantly clear that Parliament's purpose in enacting the relieving provisions was to include OIGs and AIPs within their ambit and, hence, not abundantly clear that the omission of OIGs and AIPs from their ambit was the result of an error; or

(2) even if that were not the case, it was not abundantly clear what the substance of the corrected relieving provisions would say.

74. The submission in paragraph 73(1) above effectively corresponded to the first two stages of the test in *Inco* and the submission in paragraph 73(2) above effectively corresponded to the third stage of the test in *Inco*.

Parliament's purpose and the absence of error in the legislation

75. The submission made by Mr Fell in paragraph 73(1) above was based on six points. We set out below each of those points, along with Ms Hardy's response in relation to them.

First point – no specific reference to OIGs or AIPs

76. The first point made by Mr Fell was that the extra–statutory material set out in paragraph 32(3) above merely disclosed a general intention on the part of Parliament to provide relief from foreign income and gains and did not expressly refer to OIGs or AIPs specifically.

77. There were two parts to this point.

78. The first part related to admissibility. Mr Fell said that, before recourse could be had to a ministerial statement in determining that the existing legislation contained an error, the three conditions set out in *Pepper* needed to be satisfied.

79. In *Enviroco Ltd v Farstad Supply A/S* [2011] UKLSC 16 ("*Enviroco*") at paragraphs [47] and [48], Lord Collins had said that, although the legislation which was in issue in that case led to a result which was "certainly odd and possibly absurd", there was no relevant ambiguity in the provisions in question and no clear statement which cast any light on any question of interpretation which arose on the appeal.

80. In the view of Lord Collins, the ministerial statements on which reliance was being placed fell far short of a case for the application of even the most generous application of *Pepper* and the drafting history did not throw any light on the reason for the form taken by the statutory provisions. Lord Collins said that, although it seemed likely that there had been an error, the ministerial statements at the time of the legislation shed no light on precisely what that error was. There was therefore no clear basis on which the court could be abundantly sure that there was a drafting error of a nature which the court could correct.

81. Mr Fell took us to the judgments of Lord Browne–Wilkinson at 634F to 635B and 640C, Lord Bridge at 617B and Lord Oliver at 620C to 620F in *Pepper*. Each of the Law Lords in the case had stressed the importance of examining what it was that Parliament had been considering and debating when enacting the relevant legislation. In this case, there was no evidence that Parliament had been considering whether or not OIGs and AIPs should be PFSI. Instead, Parliament had simply focused on foreign income and gains in general without regard to specific categories of foreign income or gains.

82. Since neither OIGs nor AIPs were addressed specifically in the statement made by Mel Stride MP during the passage of the legislation through Parliament, it followed that, under the rule in *Pepper*, that ministerial statement was not admissible in the present proceedings. It did not contain "a clear statement directed to the matter in issue", as was required by the decision in *Pepper* – see Lord Bridge, Lord Oliver and Lord Browne–Wilkinson in *Pepper* at 617B, 620D, 635A and 640C.

83. The second part was that, even if the ministerial statement was admissible, Mr Fell said that it, and the other extra–statutory material, did not demonstrate a clear intention on Parliament's part to include OIGs and AIPs within the relieving provisions because there was no express reference in that material to those categories of income.

84. In response to the first part of this point, Ms Hardy said that the ministerial statement by Mel Stride MP did satisfy the three conditions necessary for admissibility set out in *Pepper*, as required by Lord Collins in *Enviroco*.

85. As regards the first condition, whilst there was no ambiguity in the manner in which the definition of PFSI was drafted, excluding items of deemed foreign income which had hitherto been treated as "relevant foreign income" for affected individuals prior to the change in domicile effected by the legislation and in circumstances where relief was being provided to affected individuals in relation to all items of actual foreign income and gains was an absurd result. Consequently, the first condition was satisfied.

86. The second condition was also clearly satisfied by the statement as it was made by the promoter of the bill.

87. The third condition was also satisfied because the statement by the minister was clear and unequivocal on the point of interpretation in question. It clearly and unequivocally referred to all items of foreign income and gains and the OIGs and AIPs clearly and unequivocally fell within those general words.

88. In response to the second part, Ms Hardy said that it was incorrect to say that, in order to be taken into account in determining Parliament's purpose in relation to including OIGs and AIPs within the definition of PFSI, the extra–statutory materials needed to refer expressly to OIGs and AIPs. In her view, the fact that those materials were expressed in general terms, and encompassed all items of foreign income and gains, amounted to a clear and unequivocal expression that all of the individual specific items of foreign income and gains which were encompassed by those general terms were intended to be included. If a statement said that the purpose of legislation was to provide relief in relation to all foreign income and gains, then it

clearly and unequivocally applied to all such foreign income and gains and there was no need for the statement to specify that particular items of foreign income and gains falling within the general term were included. For example, the statements did not include references to foreign source interest income specifically but no–one could doubt that such income was intended to be included in the references to foreign income and gains.

Second point – OIGs and AIPs are deemed income

89. The second point made by Mr Fell was that OIGs and AIPs were not actual income but were instead deemed income. The extra–statutory material, to the extent that it was referring to foreign income, was merely referring to actual foreign income and not deemed foreign income.

90. In response, Ms Hardy pointed out that the Respondents had never explained why, if Parliament intended to provide relief in relation to items of foreign income and items of foreign gains, as the extra–statutory material made clear, capital proceeds arising on the disposal of foreign securities which were deemed to give rise to foreign income instead of foreign capital gains should be excluded. It made no sense for that to be the case. The clear intention of Parliament in enacting the F (No 2) A 2017 was to create protection for all items of foreign income and foreign gains and it would defeat those intentions if a category of foreign income which was deemed to arise instead of a foreign gain on the disposal of foreign assets were to be precluded from being PFSI simply because it was neither foreign gain nor actual foreign income but instead deemed foreign income.

Third point – OIGs and AIPs are anti–avoidance income

91. The third point made by Mr Fell was that it was perfectly possible that Parliament intended to exclude OIGs and AIPs from the definition of PFSI because OIGs and AIPs arose under anti–avoidance legislation and Parliament had shown by its reference in Section 830(3) of the ITTOIA to Sections 517C and 517E of the ITA that it did not think that income arising as a result of anti–avoidance legislation should be included in the definition of "relevant foreign income".

92. Ms Hardy said that it was true that OIGs and AIPs arose from anti–avoidance legislation in that the provisions giving rise to both categories of income were designed to prevent the conversion of income into capital gains by taxpayers. However, that was dealing with a very different kind of avoidance from the anti–avoidance legislation referred to Sections 517C and 517E of the ITA. Those provisions related to arrangements pursuant to which value was derived from UK land. It was perfectly understandable why Parliament would have wished to exclude income arising from such arrangements from the definition of "relevant foreign income" altogether. That same logic did not inform avoidance in the form of converting foreign income into foreign capital gains, particularly in the context of legislation which was designed to provide relief for both foreign income and foreign gains. There was therefore no reason why the exclusion from Section 830 of the ITTOIA of Sections 517C and 517E of the ITA shed any light on Parliament's purpose as regards OIGs and AIPs.

Fourth point – OIGs do not have a foreign source

93. The fourth point made by Mr Fell was that, so far as OIGs were concerned, and consistent with the point he had made in the context of Issue One, OIGs were not foreign income at all because they arose as a result of decisions taken to dispose of the interests in offshore funds giving rise to the OIGS and those decisions might well be taken in the UK.

94. Ms Hardy said that the fact that OIGs arose from the disposal of interests in offshore funds and that Parliament had seen fit in Regulation 19 (and Regulation 21 for that matter) to allow non–UK domiciles to treat OIGs as "relevant foreign income" and apply the remittance

basis demonstrated not only that OIGs should properly be regarded as foreign income but, more relevantly in the present context, that Parliament considered them to be foreign income.

Fifth point – treatment of UK domiciles

95. The fifth point made by Mr Fell was that OIGs and AIPs had never been "relevant foreign income" for UK domiciles and it was perfectly possible that Parliament intended the individuals affected by the change to be placed in the same position as other UK domiciles as regards all income other than "relevant foreign income". It was perfectly possible that Parliament's policy in enacting the F (No 2) A 2017 was to align the position of those individuals who were acquiring a deemed domicile in the UK with other UK domiciles. That was a perfectly reasonable and plausible decision for Parliament to have reached.

96. In that regard:

(1) it was apparent from the way in which the Sections 721A(3)(a) and 721(4)(a) were worded that Parliament must have been aware that, in order for income to be PFSI, the income in question had to be such that it would have been "relevant foreign income" if it had been the individual's; and

(2) it was apparent from the way in which Section 989 of the ITA and Section 830 of the ITTOIA were worded that Parliament must have been aware that:

(a) there was a distinction between those provisions which gave rise to "relevant foreign income" in general (the ones specified in Section 830(2) of the ITTOIA) and those provisions which gave rise to "relevant foreign income" only in certain specific circumstances (the ones specified in Section 830(4) of the ITTOIA); and

(b) since the provisions relating to OIGs and AIPs did not appear in Section 830(2) of the ITTOIA and Regulation 19 and Section 670A of the ITA appeared in Section 830(4) of the ITTOIA, OIGs and AIPs were not "relevant foreign income" for UK domiciles, but were instead "relevant foreign income" only for non–UK domiciles.

97. Ms Hardy said that the intended scope of the relieving provisions needed to be considered in the knowledge that, prior to the enactment of the F (No 2) A 2017, OIGs and AIPs were "relevant foreign income" for the individuals who were affected by the changes effected by the new legislation because they were non–UK domiciles. As such, the fact that OIGs and AIPs were not "relevant foreign income" for UK domiciles was neither here nor there. The critical feature was that they were "relevant foreign income" as far as the affected individuals were concerned. To bring them within the scope of the charge to income tax on an arising basis would have been entirely contrary to the clearly–stated purpose of the relieving provisions.

Sixth point – Parliament must have been aware of the scope of the "relevant foreign income" definition

98. The sixth and final point made by Mr Fell was that, at the time when it enacted the legislation, Parliament must have appreciated the fact that OIGs and AIPs did not fall within the definition of "relevant foreign income" in Section 989 of the ITA because:

(1) the only circumstance in which such items of income amounted to "relevant foreign income" were the ones described in Regulation 19 and Section 670A of the ITA;

(2) those provisions applied only to non–UK domiciles;

(3) the effect of the legislation was to deem an individual who had hitherto been a non–UK domicile to be a UK domicile; and

(4) therefore, it was inconceivable that, in enacting legislation which had the effect of changing each affected individual from being a non–UK domicile to being a UK domicile and thereby preventing the provisions specified in paragraph 98(1) above from applying to the affected individual, Parliament did not also appreciate that the income in question would cease to be "relevant foreign income" for the affected individual and would therefore be incapable of qualifying as PFSI.

99. In other words, it was apparent from the nature of the change which was effected by the F (No 2) A 2017 – which was that certain individuals were going to be deemed to be UK domiciled and would thus be deprived of the ability to rely on Regulation 19 and Section 670A of the ITA – that Parliament must have been aware that OIGs and AIPs would cease to be "relevant foreign income" for such individuals. This was a case where the operation of one provision was envisaged in the operation of another provision so that it could be inferred that the draftsman of the latter provision clearly had the former provision in mind when drafting the latter provision – see *Ward v Commissioner of Police of the Metropolis* [2006] 1 AC 23 at 27.

100. Ms Hardy said that, whilst it might be surprising that, in the very act of depriving an affected individual of the ability to rely on Regulation 19 and Section 670A of the ITA by taking away the affected individual's status as a non–UK domicile, Parliament overlooked the fact that OIGs and AIPs would cease to be "relevant foreign income" for the affected individual, there was a reasonable explanation for this error. This was that the draftsman viewed the relieving provisions as allowing the affected individual to benefit from the disapplication of the arising basis for all "relevant foreign income" and overlooked the fact that, whereas most categories of "relevant foreign income" remained the same both before and after the change in the affected individual's domicile, OIGs and AIPs ceased to be "relevant foreign income" for the affected individual as a result of that change.

101. Whilst that might have been an odd mistake to make in the circumstances, it was abundantly clear that that is what it was, for the reasons articulated above. There was absolutely no reason why Parliament would have intended OIGs and AIPs to become subject to tax on an arising basis as a result of the change in the affected individual's domicile when OIGs and AIPs had been subject to the remittance rules in the same way as the other "relevant foreign income" of the affected individual prior to his or her change in status and the extra–statutory material made it so apparent that all items of foreign income and gains were intended to benefit from the relief.

The substance of the rectified provision

102. Turning then to the submission in paragraph 73(2) above – which related to the third stage of the *Inco* test – Mr Fell said that it was not clear what the substance of the rectified provision would say. For instance, treating OIGs and AIPs as "relevant foreign income" in general would mean that:

(1) the courts would have to determine the rules for identifying the source of the relevant income and the location of that source and it is unclear what those rules would be;

(2) the courts would have to determine which of the provisions listed in Section 830(2) of the ITTOIA should be taken to apply to the income in question and it was unclear which of those provisions it would be;

(3) the courts would have to identify the rules for quantifying the OIGs and AIPs. For example, the courts would need to determine:

(a) whether, in calculating OIGs, only the disposal costs allowed under Section 38 of the TCGA should be taken into account or whether account should also be taken of expenses attributable to collection and payment pursuant to Section 838 of the ITTOIA; and

(b) which of the overlapping provisions for unremittable foreign income in Sections 668 to 670 of the ITA and Sections 841 to 845 of the ITTOIA should apply to AIPs; and

(4) the courts would need to determine whether, despite the fact that OIGs and AIPs were "relevant foreign income" and that Section 1016(3) of the ITA excluded references to any provision of the ITTOIA to the extent it related to "relevant foreign income":

(a) claims for losses to be set off against OIGs (before the changes made by the FA 2015) and AIPs could be made under Section 152 of the ITA; and

(b) the charity exemption in Section 527 of the ITA could apply to AIPs.

103. In response, Ms Hardy said that it would be quite wrong to approach this question on the assumption that the provision to be rectified was the definition of "relevant foreign income" itself. If we disagreed with her submissions in relation to Issue One, and held that OIGs and AIPs were not within the definition of "relevant foreign income" for UK domiciles, then the remedy was not to rectify the definition of "relevant foreign income" to include OIGs and AIPs for such individuals. That would involve rectifying the original legislation stemming from the Tax Law Rewrite Project. Instead, the provisions which needed to be rectified were the ones introduced by the F (No 2) A 2017 – namely, Sections 721A(3)(a) and 721A(4)(a) of the ITA in the definition of PFSI. It was notable that none of the arguments made by Mr Fell in relation to the third stage of the test in *Inco* referred to in paragraph 102 above related to bringing OIGs and AIPs within the definition of PFSI. They were all focused on bringing OIGs and AIPs within the definition of "relevant foreign income".

Conclusion

Introduction

104. For the reasons which follow, we have, somewhat reluctantly, reached the conclusion that this is not a case where rectification is appropriate. We say that we have reached our conclusion reluctantly because we suspect that the omission of OIGS and AIPs from the definition of PFSI may well have been inadvertent and we can see how that omission operates unfairly for the individuals who have been affected by the change in law. However, given the strict nature of the test in *Inco*, we consider that the circumstances of this case do not support rectifying the relevant legislation. In our opinion, it would amount to an impermissible usurpation of the legislative function of Parliament.

105. Before we set out the reasons for our conclusion, we should make it clear that the relevant legislation in this context is not the definition of "relevant foreign income" in general, stemming from the Tax Law Rewrite Project, which is to say the ITTOIA or the ITA (prior to its amendment by the F (No 2) A 2017), but rather the legislation introduced by the F (No 2) A 2017, which introduced the definition of PFSI in the ITA.

106. The underlying purpose of Condition B in Section 835BA of the ITA was to deem individuals who had been resident in the UK for a specified number of years to be UK domiciles and thus to deprive those individuals of the ability to rely on the remittance basis to which they had been entitled hitherto in relation to foreign income and gains. In carrying out that purpose, a concern naturally arose that an individual falling within that category who had set up an offshore structure at a time when he or she was a non–UK domicile would find it punitive and administratively burdensome to be subject to UK tax on the foreign income and gains of such

a structure as those foreign income and gains arose and before any benefits were received from the structure in question. It was felt that this would be unreasonable and unfair on the individuals who were affected by the change in domicile and might encourage them to leave the UK. The provisions we are now considering were designed to alleviate that concern.

107. Parliament saw fit to achieve the relieving purpose mentioned above by including provisions in both Chapter 2 of Part 13 of the ITA and the chargeable gains legislation. Those relieving provisions were designed to ensure that, unless and until any benefits were received from the offshore structure in question, there would be no charge to income tax or capital gains tax, for an individual settlor who was deemed to have become a UK domicile as a result of satisfying Condition B of Section 835BA of the ITA, on the "foreign income and gains" arising within the offshore structure in question.

108. What we have said so far is very clear from the extra–statutory material summarised in paragraph 32(3) above and is common ground.

109. Where the disagreement has arisen is in determining what Parliament intended to do in that context in relation to OIGs and AIPs given that, at the time when the change in law was enacted, OIGs and AIPs were not "relevant foreign income" in general but were "relevant foreign income" only for non–UK domiciles, some of whom were to be affected by the change in law.

110. We have found this to be a very difficult question to answer, not least because we suspect that Parliament may well have overlooked the fact that an affected individual's change in domicile would have the effect of changing the status of that individual's OIGs and AIPs from being "relevant foreign income" – by virtue of Regulation 19 and Section 670A of the ITA – to falling outside that definition.

The first and second stages of the test in Inco

111. Turning then to consider the submissions made by the parties in relation to the first and second stages of the test in *Inco*, our views are as follows.

Points which do not necessarily negate rectification

112. We agree with Ms Hardy that a number of the points which were made by Mr Fell do not necessarily negate rectification in this case. Those are Mr Fell's second, third and fourth points.

Second point – OIGs and AIPs are deemed income

113. We agree with the submission made by Ms Hardy in paragraph 90 above. In other words, we think that nothing turns on the fact that OIGs and AIPs are deemed income and not actual income. That is not a significant factor in any way because, in the tax context, income which is deemed to arise for tax purposes is no different from income which actually arises. This is particularly true of a case where the deemed income arises from the receipt of a capital sum and relief is being provided for capital gains as well as income.

Third point – OIGs and AIPs are anti–avoidance income

114. Similarly, like Ms Hardy, we do not see that anything turns on the fact that OIGs and AIPs arise as a result of anti–avoidance legislation.

115. In particular, we see no equivalence between OIGs and AIPs, on the one hand, and the provisions in Sections 517C and 517E of the ITA, on the other. The latter provisions relate to value derived from UK land and it is not surprising that they are expressly precluded from being "relevant foreign income". In contrast, OIGs and AIPs, whilst they arise from anti–avoidance legislation, stem from a desire on the part of Parliament to prevent foreign income – which would, if received, be "relevant foreign income" – from being converted into capital gains. It is perfectly logical for the deemed income so arising to qualify as "relevant foreign

income", as it has done for individuals on a remittance basis since the definition was first enacted.

Fourth point – OIGs do not have a foreign source

116. We also agree with Ms Hardy that, for the reasons we have given in paragraphs 42 to 53 above, OIGs have always been considered to be foreign in nature and that Parliament has always equated them to "relevant foreign income" for those individuals who are on a remittance basis.

Points which negate rectification

117. However, in our view, Mr Fell's first, fifth and sixth points in relation to those two stages were telling and ultimately decisive in relation to this issue.

First point – no specific reference to OIGs or AIPs

118. Starting with the first of those points, Ms Hardy's submission to the effect that the phrase "foreign income and gains", when used in the extra–statutory material, must have encompassed all items of foreign income and gains and was therefore apt to include OIGs and AIPs as specific categories of foreign income encompassed by the whole, is superficially attractive. After all, why would the phrase not clearly include all items of foreign income and gains even though none of those items of income and gains had been enumerated specifically?

119. However, we think that this would be to overlook a critical factor. In our view, it is important to construe the phrase "foreign income" in the extra–statutory material against the background that:

(1) at the time when the extra–statutory material came into existence, the legislation contained a definition of "relevant foreign income";

(2) Sections 726(2) and 726(3) of the ITA provided that income arising in an offshore structure which would be "relevant foreign income" if it were received by the non–UK domicile to whom it was deemed by Section 721 of the ITA to accrue would be treated as the "relevant foreign income" of the non–UK domicile in question; and

(3) when the new legislation was enacted, Parliament adopted a similar phraseology in Section 721A(3)(a) and 721A(4)(a) of the ITA, which is to say that income would fall within those provisions if it would be "relevant foreign income" of the affected individual in question if it were received by the individual.

In our view, the inescapable conclusion to be drawn from those features is that, when it was said in the extra–statutory material that "foreign income" was going to be protected, the material must have meant that what was going to be protected was "relevant foreign income" rather than "foreign income" in a general sense.

120. Once that conclusion is drawn, there are only two ways that the reference to "foreign income" in the extra–statutory material can possibly be construed. Either:

(1) it was intended to encompass all income that would qualify as "relevant foreign income" for the affected individual at the time when the income arose; or

(2) it was intended to encompass all income that would qualify as "relevant foreign income" for the affected individual at the time when the income arose if the affected individual had not been affected by the change in law and remained a non–UK domicile.

121. Whilst the latter construction may well be a possible explanation of what was meant by the reference to "foreign income" in the extra–statutory material, it is only one of two possible interpretations each of which seems to us to be equally tenable. After all, following the change in domicile of the affected individual, OIGs and AIPs would not qualify as "relevant foreign

income" for the affected individual at the time they arose. Therefore, they would not be "foreign income" of the affected individual at that time. If the purpose of Parliament was to include, within the phrase "foreign income", items which were not foreign income at the time they arose but merely would have been foreign income at the time they arose if the change in the affected individual's domicile had not occurred, we would have expected the extra–statutory material to have made that explicit.

122. Putting the case in favour of rectification at its strongest, even if the second interpretation is to be preferred to the first, it is impossible to be certain that that is what was meant in the extra–statutory material.

123. Just to be clear, we are not suggesting that OIGS and AIPs were not "foreign income" because they are deemed income, which was Mr Fell's second point. We agree with Ms Hardy that, in the context of statements referring to both foreign income and foreign gains, the fact that OIGs and AIPs arise out of capital sums which are deemed to be income makes no difference. Instead, it is because OIGs and AIPs were not "relevant foreign income" for the affected individual at the time they arose and the phrase "foreign income" should be construed by reference to the defined term "relevant foreign income".

Fifth point – treatment of UK domiciles

124. In our view, that first point is sufficient, in and of itself, to mean that the first two stages of the test in *Inco* are not satisfied in this case. There is insufficient certainty as to Parliament's intentions in relation to OIGs and AIPs to conclude that the legislation has failed to meet those intentions through a drafting error.

125. That conclusion is reinforced by Mr Fell's fifth point.

126. The legislative background to OIGs and AIPs which we have addressed in some detail in dealing with Issue One suggests that the phrase "foreign income", when used in the extra–statutory material, was intended to encompass items of income that fell within Schedule D Case IV or Schedule D Case V under the schedular system of income tax that prevailed before the Tax Law Rewrite and which then fell within the general definition of "relevant foreign income" for both non–UK domiciles and UK domiciles once the schedular system was abolished in the ITTOIA. As items of income that fell within Schedule D Case VI, OIGs and AIPs fell outside that definition. They were treated as "relevant foreign income" only for non–UK domiciles and that was only because the capital sums which gave rise to them represented income that, had it been received by the individual in question, would have fallen within Schedule D Case IV or Schedule D Case V (before the ITTOIA was enacted) or would have been "relevant foreign income" (after the ITTOIA was enacted). That causative link is exemplified by the fact that Section 670A defines AIPs by reference to the nature of the income which would have arisen on the securities the disposal of which gave rise to the AIPs – see Section 670A(4) of the ITA.

127. In the light of that explanation, it can be seen that OIGs and AIPs are very different from items of income which are "relevant foreign income" in general and therefore that, when the extra–statutory material referred to "foreign income", it is perfectly possible that OIGs and AIPs were not intended to be included or that Parliament did not turn its mind to whether or not they ought to be included. In either case, the position is sufficiently uncertain for us to conclude that the first two stages of the test in *Inco* are satisfied.

Sixth point – Parliament must have been aware of the scope of the "relevant foreign income" definition

128. The view we have reached in paragraphs 118 to 127 above gains further traction when we take into account Mr Fell's sixth point.

129. We agree with Mr Fell that it would be somewhat surprising that, in the very act of depriving an affected individual of the ability to rely on Regulation 19 and Section 670A of the ITA by taking away the affected individual's status as a non–UK domicile, Parliament would have overlooked so obvious a point as that OIGs and AIPs would inevitably cease to be "relevant foreign income" for the affected individual by virtue of that change. As we note in paragraphs 131 and 132 below, it would have been very easy for Parliament to have referred, in the definition of PFSI, both to income which was "relevant foreign income" for the affected individual and to income which would have been "relevant foreign income" for the affected individual if the affected individual had not become a UK domicile. The fact that the definition does not say that, when Parliament ought to have been aware that that was the effect of the change it was making, suggests that that may not have been Parliament's intention. Whilst it is possible that the draftsman simply made an error, an error of that nature would have been so egregious as to suggest that it might well not have been an error at all. In any event, it is important to bear in mind the level of certainty required before the first two stages of the test in *Inco* can be said to be satisfied. It is not sufficient to say that there may have been an error in the provision which was enacted to fulfil a clear purpose of Parliament or even that it is more likely than not that such an error was made. Instead, it is necessary to conclude that Parliament's purpose was clear and that there was clearly an error in the provision which was enacted to fulfil that purpose. We are some way away from that conclusion, for all the reasons we have set out above.

Conclusion in relation to the first two stages of the test in Inco

130. For the reasons set out in paragraphs 104 to 129 above, we believe that this is not a case where rectification is appropriate.

The third stage of the test in Inco

131. The conclusion we have reached in relation to the first two stages of the test in *Inco* means that it is unnecessary for us to address the third stage of that test. However, for completeness, we would say that, were we to have concluded to the requisite level of certainty that the legislation in this case contained an error that satisfied the first two stages of the test in *Inco*, the substance of the remedy would be straightforward.

132. Since the error in question would be that, in drafting the definition of PFSI, the draftsman failed to appreciate that OIGs and AIPs would cease to be "relevant foreign income" for an affected individual by virtue of the change in the affected individual's domicile under Condition B in Section 835BA of the ITA, the logical and straightforward way to remedy that error would be to extend those paragraphs within the definition of PFSI to encompass, in addition to items of income which would have been "relevant foreign income" had they been received by the affected individual, items of income which would have been "relevant foreign income" had they been received by the affected individual and had the affected individual not been deemed to be a UK domicile by virtue of Condition B of the new Section 835BA of the ITA. That is a perfectly straightforward change which would avoid any of the issues mentioned by Mr Fell set out in paragraph 102 above. OIGs and AIPs would continue to fall outside the definition of "relevant foreign income" for UK domiciles.

Our conclusion in relation to Issue Two

133. For the reasons set out in paragraphs 104 to 132 above, we determine Issue Two in favour of the Respondents.

DISPOSITION

134. We therefore find for the Respondents in relation to both Issue One and Issue Two, with the result that we dismiss the appeals against the Closure Notices.

135. It remains for us to thank Mr Fell, Ms Hardy and Mr Marre for the clarity of their submissions, which we have found to be of great assistance in determining the appeals.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

136. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

Release Date: 07th MARCH 2025