[2015] UKUT 0060 (TCC)

Appeal number: FTC/120/2013

INCOME TAX – Part 7 of the Income Tax (Earnings and Pensions) Act 2003 – restricted securities – tax avoidance scheme - the Ramsay principle

UPPER TRIBUNAL (TAX AND CHANCERY CHAMBER)

(1) TOWER RADIO LIMITED
(2) TOTAL PROPERTY SUPPORT SERVICES LIMITED

Appellants

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

TRIBUNAL:

Mr Justice Newey
Judge Colin Bishopp

Sitting in public in London on 24-26 November 2014

Mr Giles Goodfellow QC, instructed by Barnes Roffe LLP, for the Appellants

Mr Timothy Brennan QC, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

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DECISION

Introduction

1. This case concerns a tax planning scheme ("the Scheme") that was promoted by Barnes Roffe LLP, a firm of accountants. The Scheme was designed to allow companies' employees and officers to be given bonuses which would not attract income tax or national insurance contributions ("NICs") deductions. This was to be achieved by awarding the employees or officers shares in specially-formed subsidiaries of the companies rather than cash and, hence, taking advantage of Part 7 of the Income Tax (Earnings and Pensions) Act 2003 ("ITEPA"), which "contains special rules about cases where securities, interests in securities or securities options are acquired in connection with an employment" (as section 417(1) explains).

2. The appellants, Tower Radio Limited ("Tower") and Total Property Support Services Limited ("Total"), were each amongst those who made use of the Scheme. HM Revenue and Customs ("HMRC") say that the Scheme does not achieve its intended purpose and have issued determinations and decisions designed to recover the income tax and NICs for which they say the appellants should have accounted. Their appeals were designated by the First-tier Tribunal ("FTT") as lead cases. Other cases relating to the Scheme have been stayed (in England and Wales) or sisted (in Scotland) pending the resolution of matters as regards Tower and Total.

3. The FTT identified the following issue as arising:

> "Whether the sums or benefits received by officers or employees pursuant to arrangements registered as Disclosed Tax Scheme 54003391 and adopted by the Lead Case Appellants and others during the tax years 2003-04 and/or 2004-05 are:
>
> (a) chargeable to income tax as employment income, and, if so, as PAYE income; and/or
>
> (b) constitute earnings liable for National Insurance Contributions".

4. In a decision released on 11 July 2013 ("the Decision"), the FTT (Judge Peter Kempster and Mr John Whiting OBE) held that this issue fell to be resolved in favour of HMRC. The FTT concluded that the sums or benefits in question were (a) chargeable to income tax as employment income and PAYE income and (b) constituted earnings liable for NICs (see paragraph 170 of the Decision). Tower and Total, however, appeal against the Decision.

5. The case turns, essentially, on the impact (if any) of the *Ramsay* principle (see paragraph 30 below). More particularly, it raises the question of whether, in

the light of the *Ramsay* principle, the relevant employees or officers should be regarded as having acquired "money" rather than "shares in any body corporate" for the purposes of section 420 of ITEPA.

5 **Basic facts**

Tower

6. Tower has for many years supplied electrical appliances. By 2003 it had built up reserves of over £1 million, and late that year Mr Bernard Litman, the
10 managing director and largest shareholder, discussed with Barnes Roffe how money could be moved off the company's balance sheet. Barnes Roffe told him of the Scheme and were engaged to pursue it. To that end, a company called Efforsenrab (1) Limited ("SPV 1") was incorporated in March 2004 and became a wholly-owned subsidiary of Tower, which agreed to subscribe for 1
15 million "A" shares of £1 each as well as acquiring the single "B" share in the company. Thereafter, Tower's shareholders and board resolved to transfer all the "A" shares to Mr Litman as a "discretionary reward for [his] services", leaving Tower with the "B" share. Mr Litman was registered as the holder of the "A" shares with effect from 5 April 2004.

20

7. Under SPV 1's articles of association, a holder of "A" shares was to be required to transfer them to another member or members of the company for an amount equal to 95% of their market value if a "Forfeiture Event" occurred. The main such event was ceasing to hold office or employment with Tower
25 otherwise than by reason of death.

8. When Mr Litman received the "A" shares in SPV 1, it was envisaged that he would retain them for at least two years and that the company would in the meantime invest the money it held. It was thought that this approach would
30 have capital gains tax ("CGT") advantages. In July 2004, however, Barnes Roffe warned of possible changes in the tax regime. In the light of that advice, Mr Litman decided to set in train at once the winding-up of SPV 1. Accordingly, SPV 1 was put into members' voluntary liquidation on 26 July 2004, and the following day distributions of £993,999 and £1 were made in
35 favour of Mr Litman (in respect of his "A" shares) and Tower (in respect of its "B" share) respectively. Subsequently, Mr Litman received further distributions totalling £11,326.05 and an additional £0.01 was distributed to Tower. In 2005, SPV 1 was dissolved.

40 9. In a letter to Mr Litman of 10 February 2004, Barnes Roffe had advised Mr Litman that the Scheme produced a saving of tax and NICs of 47.7% as compared with "a conventional cash bonus".

Total

45 10. Total has carried on a property maintenance and general construction business since 2001. In September 2004, Barnes Roffe advised its directors, Mr Gary Coombs and Mr Alex Thorne, that the Scheme could be used to award

bonuses in a tax-advantageous manner. That same month, Efforsenrab (147) Limited ("SPV 147") and Efforsenrab (148) Limited ("SPV 148") were incorporated. Both companies became wholly-owned subsidiaries of Total, which in each case agreed to subscribe for 50,000 £1 "A" shares as well as acquiring the single "B" share. On 28 September 2004, Total's shareholders and board resolved to transfer the "A" shares in SPV 147 to Mr Thorne and those in SPV 148 to Mr Coombs, in each case as a "discretionary award for … services", and the share transfers were effected that day. The very next day, SPV 147 and SPV 148 were both put into members' voluntary liquidation, and on 1 October 2004 Mr Coombs and Mr Thorne each received a distribution of £46,612.93. Further (and final) distributions of £1,058.10 were made to Mr Coombs and Mr Thorne in January 2005,

11. Like those of SPV 1, the articles of association of SPV 147 and SPV 148 provided for "A" shares to be transferred to another shareholder or shareholders if a "Forfeiture Event" occurred. Again, the main such event was ceasing to hold office or employment with Total otherwise than by reason of death.

12. Mr Coombs and Mr Thorne were both shareholders in Total, and their wives held the remaining shares in the company.

The legislative framework

13. Part 7 of ITEPA is headed, "Employment income: Income and exemptions relating to securities". As that heading perhaps suggests, Part 7 contains provision both for amounts to count as employment income and for exemptions and reliefs from income tax (see section 417(3) and (4)).

14. Chapters 2-4 of Part 7 "apply to securities, or an interest in securities, acquired by a person where the right or opportunity to acquire the securities or interest is available by reason of an employment of that person or any other person" (see section 421B(1)). Chapter 2 (which comprises sections 422-432) is in point if such securities ("employment-related securities") are "restricted securities" or "a restricted interest in securities" at the time of acquisition (see section 422).

15. In broad terms, by virtue of Chapter 2 of Part 7 no liability to income tax generally arises in respect of the acquisition of an employment-related security that is a restricted security or a restricted interest in securities, but tax is payable if a "chargeable event" occurs in relation to the security. Section 427 explains that "chargeable events" occur on:

> "(a) the employment-related securities ceasing to be restricted securities, or a restricted interest in securities, in circumstances in which an associated person is beneficially entitled to the employment-related securities after the event,

(b) the variation of any restriction relating to the employment-related securities in such circumstances (without the employment-related securities ceasing to be restricted securities or a restricted interest in securities), and

(c) the disposal for consideration of the employment-related securities, or any interest in them, by an associated person otherwise than to another associated person (at a time when they are still restricted securities or a restricted interest in securities)."

It is important in the context of the present case that the liquidation of a company in which "employment-related securities" were held was not identified as a "chargeable event".

16. Lord Walker commented on Part 7 of ITEPA in *Gray's Timber Products Ltd v Revenue and Customs Commissioners* [2010] UKSC 4, [2010] STC 782. He noted (at paragraphs 4-7) that its provisions "reflect three different, and to some extent conflicting, legislative purposes". One is "Parliament's recognition that it is good for the economy, and for social cohesion, for employees to own shares in the company for which they work", as a result of which "[v]arious forms of incentive schemes are … encouraged by favourable tax treatment". To ensure that such schemes acted as effective long-term incentives, Parliament was concerned, secondly, that the benefits they confer should be "made contingent, in one way or another, on satisfactory performance". An employee would ordinarily be taxed on such a benefit as soon as he acquired it, but:

"The principle of taxing an employee as soon as he received a right or opportunity which might or might not prove valuable to him, depending on future events, was an uncertain exercise which might turn out to be very unfair either to the individual employee or to the public purse."

It was soon recognised that:

"in many cases the only satisfactory solution was to wait and see, and to charge tax on some 'chargeable event' (an expression which recurs throughout Pt 7) either instead of, or in addition to, a charge on the employee's original acquisition of rights".

That approach, however, "inevitably led to opportunities for tax avoidance", and the "third legislative purpose is to eliminate opportunities for unacceptable tax avoidance".

17. The expressions "restricted securities" and "restricted interest in securities" are defined by section 423 of ITEPA. Section 423(1) states that employment-

related securities are restricted securities or a restricted interest in securities if "there is any contract, agreement, arrangement or condition which makes provision to which any of subsections (2) to (4) applies" and "the market value of the employment-related securities is less than it would be but for that provision". Subsections (2) to (4) provide as follows:

> "(2) This subsection applies to provision under which—
>
> (a) there will be a transfer, reversion or forfeiture of the employment-related securities, or (if the employment-related securities are an interest in securities) of the interest or the securities, if certain circumstances arise or do not arise,
>
> (b) as a result of the transfer, reversion or forfeiture the person by whom the employment-related securities are held will cease to be beneficially entitled to the employment-related securities, and
>
> (c) that person will not be entitled on the transfer, reversion or forfeiture to receive in respect of the employment-related securities an amount of at least their market value (determined as if there were no provision for transfer, reversion or forfeiture) at the time of the transfer, reversion or forfeiture.
>
> (3) This subsection applies to provision under which there is a restriction on—
>
> (a) the freedom of the person by whom the employment-related securities are held to dispose of the employment-related securities or proceeds of their sale,
>
> (b) the right of that person to retain the employment-related securities or proceeds of their sale, or
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> (c) any other right conferred by the employment-related securities,
> (not being provision to which subsection (2) applies).
>
> (4) This subsection applies to provision under which the disposal or retention of the employment-related securities, or the exercise of a right conferred by the employment-related securities, may result in a disadvantage to—
>
> (a) the person by whom the employment-related securities are held,
>
> (b) the employee (if not the person by whom they are held), or
>
> (c) any person connected with the person by whom they are held or with the employee,

(not being provision to which subsection (2) or (3) applies)."

18. The term "securities" is defined a little earlier in the Act, at section 420. As it stood at the relevant time, section 420(1) stated:

> "Subject to subsections (5) and (6), for the purposes of this Chapter and Chapters 2 to 5 the following are 'securities'—
>
> (a) shares in any body corporate (wherever incorporated) or in any unincorporated body constituted under the law of a country or territory outside the United Kingdom,
>
> (b) debentures, debenture stock, loan stock, bonds, certificates of deposit and other instruments creating or acknowledging indebtedness,
>
> (c) warrants and other instruments entitling their holders to subscribe for securities (whether or not in existence or identifiable),
>
> (d) certificates and other instruments conferring rights in respect of securities held by persons other than the persons on whom the rights are conferred and the transfer of which may be effected without the consent of those persons,
>
> (e) units in a collective investment scheme,
>
> (f) futures, and
>
> (g) rights under contracts for differences or contracts similar to contracts for differences."

As regards subsection (1)(e), section 420(2) explained that "collective investment scheme" meant arrangements:

> "(a) which are made with respect to property of any description, including money, and
>
> (b) the purpose or effect of which is to enable persons taking part in the arrangements (whether by becoming owners of the property or any part of it or otherwise) to participate in or receive profits or income arising from the acquisition, holding, management or disposal of the property or sums paid out of such profits or income."

Section 420(5) provided:

> "The following are not 'securities' for the purposes of this Chapter or Chapters 2 to 5—

(a) cheques and other bills of exchange, bankers' drafts and letters of credit (other than bills of exchange accepted by a banker),

(b) money and statements showing balances on a current, deposit or savings account,

(c) leases and other dispositions of property and heritable securities,

(d) rights under contracts of insurance (within the meaning of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001), and

(e) options."

19. It is perhaps worth adding that, since the events with which we are concerned, an anti-avoidance provision has been inserted into Chapter 2 of Part 7 of ITEPA, by the Finance (No 2) Act 2005. This deems employer and employee to have elected for the disapplication of Chapter 2 where "the main purpose (or one of the main purposes) of the arrangements under which the right or opportunity to acquire the employment-related securities is made available is the avoidance of tax or national insurance contributions" (see section 431B).

The basis of the Scheme

20. It can be seen from what we have said about Chapter 2 of Part 7 of ITEPA that (a) no tax is payable when an employment-related security that is a restricted security or a restricted interest in securities is acquired and (b) the "chargeable events" that trigger tax liabilities do not include the liquidation of the company in which such securities are held. The Scheme was designed to exploit these features.

21. The shares that the directors were awarded in the SPVs in these cases were intended to be "restricted securities". That was to be achieved by means of forfeiture provisions such as those to be found in the articles of association of each of the SPVs relevant to this case. There would (so the theory went) therefore be no tax charge when the directors acquired the shares.

22. Nor, it was hoped, would any tax liability arise at any later stage. Chapter 2 of Part 7 provided for tax to be payable when a "chargeable event" occurred, but (because section 427 took no account of liquidation) none ever would.

The Decision

23. The FTT focused on three issues. The first is no longer relevant. The FTT expressed the second issue (which it called "The ITEPA Issue") in these terms (see paragraph 115(2) of the Decision):

> "Assuming … the provisions of Ch 2 to be applicable, did any charge to tax arise in accordance with those provisions?"

The issue gave rise to the following sub-issues:

(a) Should the forfeiture provision in the SPV articles be disregarded?

(b) If the answer to (a) was No, were the relevant shares "restricted securities" within section 423?

Finally, the third issue ("The Broad *Ramsay* Issue" – see paragraph 38 below) was identified (in paragraph 115(3)) as:

> "Can it be concluded, by application of the *Ramsay* principle as it is now to be understood, that on a realistic appraisal of the facts the scheme fell outside the scope of Ch 2 altogether (rather than that the *Ramsay* principle affected the application of particular elements of the statutory regime)?"

24. The FTT found in favour of Tower and Total on the ITEPA Issue. With respect to the first sub-issue, the FTT said this (in paragraph 134 of the Decision):

> "[T]he forfeiture clause was deliberately designed to circumvent an income tax charge by manoeuvring into the exemption afforded by s 425, on the basis that the shares met the requirements of s 423 …. Also, the likelihood of the clause being triggered was improbable. However, we do not feel able to conclude that the provision should be read to mean anything other than what it says, nor simply to ignore its existence."

As regards the second sub-issue, the FTT concluded (in paragraph 137):

> "In our opinion the forfeiture clause in the SPV's articles of association … does constitute an arrangement or condition which makes provision for a forfeiture as described in s 423(2) such that the market value of the shares is less than it would be but for that provision. HMRC made no argument to the contrary. Thus the 'A' shares in the SPV do constitute 'restricted securities' as defined in s 423."

25. On the Broad *Ramsay* Issue, however, the FTT sided with HMRC. The FTT considered (see paragraph 162 of the Decision) –

> "that the following elements of the transaction were inserted for the purpose of tax avoidance and [and] should be disregarded or treated as irrelevant for the purposes of Part 7:

(1) The incorporation of the SPVs;
(2) The inclusion of the forfeiture clause in the articles of the SPV;
(3) The award of the 'A' shares to the employee;
5 (4) The investment activities of [SPV 1] and
(5) The liquidation of the SPV and subsequent distributions by the liquidator."

Having disregarded these elements, the FTT found that "the only coherent
10 analysis of the transaction is that the surplus cash of the employer was paid to the relevant employees" (paragraph 164).

26. The FTT explained its thinking in this way in paragraph 163 of the Decision:

15 "We find that, on the facts as we have found them in the current case, we do not need to consider the detail of s 420(5)(b) or the other minutiae of Part 7. The scheme followed by the Appellants is a blatant example of what the Upper Tribunal [in *UBS AG v Revenue and Customs Commissioners*] called a 'money in, money out' arrangement.
20 If insolvency law and banking practice had permitted then we have no doubt the [Total] SPVs would have paid their cash to Messrs Coombs and Thorne the day after it was received from the employer. If Mr Litman had been satisfied with the expected income tax and NIC benefits rather than also seeking the CGT [business asset taper relief]
25 benefit then, again, the cash would have come out to him almost as soon as it went into the SPV. The employer's surplus cash was just bounced through the SPV to the employee, and everything else was merely paper-shuffling. The fact that (to use Moses LJ's phrase in *PA Holdings*) the 'process for delivery' of the cash, or (to use Warren J's
30 phrase in *Aberdeen*) the 'mechanism by which the benefit of a sum of money was to be channelled to an employee', happened to involve securities should not, we consider, sidetrack us into the detailed provisions of Part 7. That would put the cart before the horse – the 'disregarded elements' include everything to do with those securities
35 (incorporation, issue, transfer, and liquidation) and the result is that, viewed through *Ramsay* eyes, the securities are disregarded. In *UBS* the Upper Tribunal on the facts in that case considered it needed to respect the existence of the restricted securities and thus apply Part 7 to them. That cannot be a general approach to be applied regardless of the
40 facts of the individual case before the Tribunal – otherwise any planning device, even the most (to borrow Lord Walker's terminology) 'unacceptable' and 'artificial', that happened to include employee-related securities would be immune from the *Ramsay* approach, which is clearly not the case."

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27. In the course of the Decision, the FTT made the following (among other) findings of fact:

(a) The Scheme had no commercial purpose, other than the intended obtaining of a tax advantage (paragraph 107);

(b) The only purpose of the inclusion of the forfeiture provisions in the articles of the SPVs was to ensure that the "A" shares qualified as "restricted securities" for the purposes of section 423 of ITEPA (paragraph 108);

(c) The only reason for the holding and investment of cash by SPV 1 was to attempt to qualify for CGT business taper relief on the liquidation of the SPV (paragraph 110);

(d) There was no realistic possibility of any outcome other than that the bonuses would be paid exactly as detailed in the documentation prepared in advance for each employer (paragraph 111).

The parties' contentions in brief summary

28. Mr Timothy Brennan QC, who appeared for HMRC, supported the Decision. A realistic appraisal of the facts, he submitted, justified the FTT's wholesale rejection of any suggestion that the awards of "shares" were anything other than wrappers for the value of the bonuses. The employees (so it was said) dressed up what on a fair analysis were payments of money to look as though they were awards of shares. The disguise was worn for longer in the case of Tower, but it was no less transparent than with Total. The FTT was right to see through it, Mr Brennan argued, in each instance.

29. In contrast, Mr Giles Goodfellow QC, who appeared for Tower and Total, maintained that the FTT should have found that the employees were awarded "restricted securities". According to Mr Goodfellow, the FTT paid too little attention to the terms of Part 7 of ITEPA: the *Ramsay* principle notwithstanding, it was not entitled to ignore the detail of section 420(5)(b) or the other minutiae of Part 7. Mr Goodfellow submitted that the FTT ought to have concluded that Mr Litman, Mr Coombs and Mr Thorne were each awarded "shares in any body corporate" within the meaning of section 420(1)(a) (and not "money" within the meaning of section 420(5)(b)). Chapter 2 of Part 7 is, Mr Goodfellow pointed out, designed to prevent the avoidance of tax by the device of an award of securities of a low present value, attracting a modest immediate tax charge, in circumstances when it is known that the securities will later increase in value but that increase will escape tax. It does so by deferring the tax charge, and as it is an anti-avoidance measure it is deliberately cast in wide terms. It is not permissible to disregard those terms and treat what is defined as an issue of securities as if it were a payment of money.

The *Ramsay* principle

30. The *Ramsay* principle, on the basis of which the FTT dismissed the appeals before it, takes its name from the decision of the House of Lords in *W. T. Ramsay Ltd v Inland Revenue Commissioners* [1982] AC 300.

31. Lord Nicholls of Birkenhead explained the *Ramsay* case in these terms in *Barclays Mercantile Business Finance Ltd v Mawson* [2004] UKHL 51, [2005] STC 1:

> "29 The *Ramsay* case … liberated the construction of revenue statutes from being both literal and blinkered. It is worth quoting two passages from the influential speech of Lord Wilberforce. First, at p 323, on the general approach to construction:
>
> 'What are "clear words" is to be ascertained upon normal principles: these do not confine the courts to literal interpretation. There may, indeed should, be considered the context and scheme of the relevant Act as a whole, and its purpose may, indeed should, be regarded.'
>
> 30 Secondly, at pp 323-324, on the application of a statutory provision so construed to a composite transaction:
>
> 'It is the task of the court to ascertain the legal nature of any transaction to which it is sought to attach a tax or a tax consequence and if that emerges from a series or combination of transactions, intended to operate as such, it is that series or combination which may be regarded.'
>
> 31 The application of these two principles led to the conclusion, as a matter of construction, that the statutory provision with which the court was concerned, namely that imposing capital gains tax on chargeable gains less allowable losses was referring to gains and losses having a commercial reality ('The capital gains tax was created to operate in the real world, not that of make-belief') and that therefore:
>
> 'To say that a loss (or gain) which appears to arise at one stage in an indivisible process, and which is intended to be and is cancelled out by a later stage, so that at the end of what was bought as, and planned as, a single continuous operation, there is not such a loss (or gain) as the legislation is dealing with, is in my opinion well and indeed essentially within the judicial function.' (p 326)
>
> 32 The essence of the new approach was to give the statutory provision a purposive construction in order to determine the nature of the transaction to which it was intended to apply and then to decide whether the actual transaction (which might involve considering the

overall effect of a number of elements intended to operate together) answered to the statutory description. Of course this does not mean that the courts have to put their reasoning into the straitjacket of first construing the statute in the abstract and then looking at the facts. It might be more convenient to analyse the facts and then ask whether they satisfy the requirements of the statute. But however one approaches the matter, the question is always whether the relevant provision of the statute, upon its true construction, applies to the facts as found. As Lord Nicholls of Birkenhead said in *MacNiven v Westmoreland Investments Ltd* [2003] 1 AC 311, 320, para 8: 'The paramount question always is one of interpretation of the particular statutory provision and its application to the facts of the case.'"

32. In a passage endorsed by the House of Lords in the *Barclays Mercantile* case, Ribeiro PJ said this about the *Ramsay* principle in *Collector of Stamp Revenue v Arrowtown Assets Ltd* [2003] HKCFA 46, (2004) 6 ITLR 454 (at paragraph 35):

> "[T]he driving principle in the *Ramsay* line of cases continues to involve a general rule of statutory construction and an unblinkered approach to the analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically".

33. The fact that a transaction was undertaken with a view to tax avoidance will not necessarily mean that the *Ramsay* principle applies. Taxing statutes sometimes refer to purely legal, not commercial, concepts, and where that is the case (as Lord Hoffmann explained in *MacNiven v Westmoreland Investments Ltd* [2001] UKHL 6, [2003] 1 AC 311, at paragraph 58):

> "If a transaction falls within the legal description, it makes no difference that it has no business purpose."

Lord Hoffmann went on to say (at paragraph 59):

> "Even if a statutory expression refers to a business or economic concept, one cannot disregard a transaction which comes within the statutory language, construed in the correct commercial sense, simply on the ground that it was entered into solely for tax reasons. Business concepts have their boundaries no less than legal ones."

34. The *Ramsay* principle was held not to be applicable in *Mayes v Revenue and Customs Commissioners* [2011] EWCA Civ 407, [2011] STC 1269. That case concerned a seven-step tax avoidance scheme. HMRC argued that two of the steps should be ignored on the basis of the *Ramsay* principle, but the Court of Appeal decided otherwise. Mummery LJ said (at paragraph 78):

> "They were genuine legal events with real legal effects. The court cannot, as a matter of construction, deprive those events of their fiscal effects under [the Income and Corporation Taxes Act 1988] because they were self-cancelling events that were commercially unreal and were inserted for a tax avoidance purpose in the pre-ordained programme that constitutes SHIPS 2."

Similarly, Toulson LJ said (at paragraph 108):

> "the court cannot lawfully hold, as a matter of proper construction of the statute, that because the sole purpose of steps 3 and 4 was to avoid tax by the creation of a corresponding deficiency unrelated to any underlying commercial loss, those events are therefore to be treated as if they had not occurred."

UBS and Deutsche Bank schemes

35. The *Ramsay* principle was considered in the context of Part 7 of ITEPA in *UBS AG v Revenue and Customs Commissioners; Deutsche Bank Group Serices (UK) Ltd v Revenue and Customs Commissioners* [2014] EWCA Civ 452, [2014] STC 2278. That case concerned tax avoidance schemes adopted by two banks, UBS and Deutsche Bank. Each scheme (like that at issue in the present case) attempted to use Part 7 of ITEPA to enable bonuses to be provided to employees in a way that would escape liability to income tax and NICs. Whereas, however, the scheme used by Tower and Total was based on the definition of "chargeable event" given in section 427, the UBS and DB schemes were designed to exploit section 429, which provided for an exemption from tax in respect of shares in a company which (among other things) had not been under the employer's "control" during the previous year.

36. In the case of UBS, selected employees were asked whether they would like to participate in the scheme and so receive part of their bonus awards in shares rather than cash. Those who decided to take part were allocated non-voting redeemable shares ("NVS") in a newly-established SPV whose only other shareholder was the trustee of an unconnected charitable trust. To make the NVS "restricted securities" for the purposes of section 423 of ITEPA, the SPV's articles provided for the forced sale of the NVS at 90% of their unrestricted market value if the closing value of an index was greater than a "Trigger Level" on any day between 28 January 2004 (when the NVS were first issued) and 19 February 2004. The articles also gave holders of NVS the right to redeem their shares on 22 March 2004, 22 March 2006 or 22 June 2006. In the event, the index did not exceed the "Trigger Level" and more than half of the NVS were redeemed on 22 March 2004 at a price of £977.50 per share (as compared with the subscription price of £1,000 per share). On 22 March 2006, when the two years necessary to take advantage of maximum CGT taper relief had expired, further NVS were redeemed for about £1,519 a share, reflecting a large increase in the value of the UBS shares in which the

subscription money had been invested. On 22 June 2006, further NVS were redeemed for £1,429 a share, following a fall in the value of UBS shares. The few remaining NVS were redeemed in November 2006 when the SPV was wound up.

37. With Deutsche Bank, too, employees were offered the chance to take shares in an SPV in lieu of a cash bonus. The shares so allocated, in early February 2004, were subject to a restriction under which an employee would lose his shares if he ceased to be employed by Deutsche Bank before 2 April 2004 for any reason other than redundancy, death, disability or without cause. Here, the SPV's assets were to be invested in a narrow range of low risk investments such as UK gilts and triple A corporate bonds. 42% of the shares were redeemed at the first opportunity, on 8 July 2004, at a price of £1.003.73 per share (slightly up from the subscription price of £1,000 a share), and the remaining shares had been redeemed by the end of 2006.

38. HMRC advanced "broad" and "narrower" *Ramsay* points before the Court of Appeal. The "broad" submission was to the following effect (as explained by Rimer LJ in paragraph 47 of his judgment):

> "The scheme had no commercial purpose, only a tax avoidance purpose. Ch 2 [of Part 7 of ITEPA] was not intended to apply to such a scheme. It was wrong to regard it as a scheme under which employees were being rewarded by the allocation of shares. Its sole purpose was to reward them in cash. The shares were not, therefore, 'restricted securities' at all, and the scheme fell outside Ch 2. [Counsel for HMRC] did not go so far as to say that the shares issued to employees did not exist, or were to be regarded as not existing. His point was that they did not perform the function envisaged for 'restricted securities' in Ch 2."

39. The "narrower" submission focused on the fact that the restrictions imposed on the shares were inserted solely to achieve the intended tax avoidance, not for a commercial purpose. This, it was said, prevented the shares from being "restricted securities" (see Rimer LJ's judgment at paragraphs 49 and 60).

40. The Court of Appeal rejected both the "broad" and "narrower" submissions. Rimer LJ (with whom Kitchin and Christopher Clarke LJJ agreed) said this about the UBS scheme:

> "[63] I agree with [counsel for UBS] and [counsel for Deutsche Bank] that the first question is whether, under the scheme, what was provided to the employees by UBS was money or shares. If on a fair analysis of the scheme, the correct answer is that it was money, there can be no question of Ch 2 having any application. Moreover, I also agree with [counsel for UBS] that there might be cases in which, even though what was nominally awarded were shares, an objective

interpretation of the true nature of the arrangements would justify the conclusion that in fact the employee was being paid money: for example, if the shares were required to be redeemed immediately for a pre-ordained cash sum.

[64] In this case, however, there is in my view no question of the scheme being one for the payment of money, and I regard HMRC's endeavours to suggest that it was as misconceived. The FTT found that the NVS were real shares, some of which were held by employees for more than two years, and real dividends were paid on them. Moreover, although the employees had the right to redeem their shares for cash over a period of two years, the redemption money was not pre-ordained, but its amount varied with the fortunes of the UBS shares held by ESIP [i.e. the SPV], which could have risen or fallen. The shares were therefore real shares which functioned as such. It is true that the scheme could, in substance, be regarded as one in which a fixed amount of money was invested in employment-related shares for each scheme employee. But it was not a scheme under which the employee would, upon redeeming his shares, be entitled to a payment of the like sum. What he would receive was the redemption value of his shares, which might well be a very different sum. The scheme was therefore one for the provision of shares to the employees, not for the payment of money to them.

[65] As what was provided to the employees was shares, there is in my view no scope for arguing that the shares were other than 'securities … acquired in connection with an employment' within the meaning of ss 417(1) and 420 in Ch 1. They were therefore 'securities' for the purposes of Ch 2; and, provided that they satisfied the conditions of s 423, they were also 'restricted securities' for Ch 2 purposes. I do not understand the argument that because, so it is said, the 'transfer, reversion or forfeiture' circumstances had no commercial rationale, the shares could not be restricted securities. That appears simply to be another way of saying that Ch 2 does not apply to tax-avoidance schemes. But I do not follow on what basis it can be said that the 'certain circumstances' referred to in s 423(2)(a) can only be 'circumstances' included other than for tax avoidance purposes. There appears to me to be no justification for any such distinction. I of course accept, as did [counsel for UBS], that there must be a real, genuine possibility of the stated circumstances occurring: if they were never going to happen in the real world, a purposive interpretation of s 423 would exclude them from its contemplation. In this case, however, the FTT found there was a genuine possibility of a forfeiture happening on the facts of the scheme. The 'certain circumstances' were therefore real ones, even though their inclusion in the scheme was tax motivated. If, therefore, as follows, the NVS are 'restricted securities' within the meaning of s 423, from where in Ch 2 does one derive the conclusion that Ch 2

> as a whole nevertheless cannot apply simply because the scheme is driven by considerations of tax avoidance? As the [Upper Tribunal] said, Ch 2 contains a detailed and prescriptive code for dealing with restricted securities. I agree with the [Upper Tribunal] that the NVS were restricted securities whose taxation fate was governed by that code. I would reject HMRC's submissions that *Ramsay* principles, whether broad or narrow, require these genuine, employment-related NVS to be regarded other than as genuine 'restricted securities' within the meaning of Ch 2."

41. Turning to the Deutsche Bank scheme, Rimer LJ explained that HMRC's "broad" *Ramsay* point was to be rejected for the same reasons as the equivalent argument put forward in relation to the UBS scheme (see paragraph 141). As regards the "narrower" point, Rimer LJ agreed with counsel for Deutsche Bank (see paragraph 147) that:

> "there is no stress in ss 423 to 425 of Ch 2 on why the restrictions are in place, that is whether they are there for commercial reasons or otherwise, nor whether the employee can ensure that they do not apply. The stress is simply on whether the restrictions reduce value, nothing more."

Further, Rimer LJ agreed with the Upper Tribunal that the FTT had been entitled to find that the reduction in value brought about by the forfeiture provision and restriction on transfer was not so small as to be insignificant (see paragraphs 148 and 149).

The present case

<u>*The significance of the statutory wording*</u>

42. It is nowadays clear that the *Ramsay* principle is essentially one of statutory interpretation. As Mummery LJ explained in the *Mayes* case (at paragraph 74), "*Ramsay* did not lay down a special doctrine of revenue law striking down tax avoidance schemes on the ground that they are artificial composite transactions and that parts of them can be disregarded for fiscal purposes because they are self-cancelling and were inserted solely for tax avoidance purposes and for no commercial purpose". The position is rather that the *Ramsay* principle is "the general principle of purposive and contextual construction of all legislation" (see Mummery LJ's judgment, at paragraph 74). As Ribeiro PJ noted (see paragraph 32 above), the ultimate question is whether *the relevant statutory provisions*, construed purposively, were intended to apply to the transaction, viewed realistically.

43. In the circumstances, the central issue in the present case has to be whether, construing Part 7 of ITEPA purposively and taking a realistic view of the facts, Mr Litman, Mr Coombs and Mr Thorne each acquired "securities"

within the meaning of section 420 of ITEPA. More specifically, the focus must be on whether Mr Litman, Mr Coombs and Mr Thorne are to be seen as having acquired, not "shares in any body corporate" (within section 420(1)(a)), but "money" (within section 420(5)(b)). If, adopting a purposive construction and looking at the facts realistically, Mr Litman, Mr Coombs and Mr Thorne acquired "shares in any body corporate" rather than merely "money", Chapter 2 of Part 7 will be applicable even though the parties' objective was to avoid tax.

44. Mr Goodfellow contended that the FTT had paid insufficient attention to the terms of Part 7 of ITEPA. He argued that the FTT had failed to direct itself to the "primary relevant question", viz. "whether the employer company had provided the employee with securities rather than money".

45. In our view, there is force in Mr Goodfellow's submission. It is clear from the Decision that the FTT had Ribeiro PJ's "neat apothegm" well in mind (see e.g. paragraphs 140 and 160). In paragraph 160, the FTT observed:

> "To answer Ribeiro PJ's 'ultimate question', we find it inconceivable that Part 7 as construed purposively by Lord Walker was intended to apply to the realistic view of the transaction."

It seems to us, however, that the "ultimate question" could not be answered by reference only to the three general legislative purposes that Lord Walker identified as reflected in Part 7 of ITEPA (see paragraph 16 above). The FTT needed to ask itself, specifically, whether Mr Litman, Mr Coombs and Mr Thorne are to be considered to have acquired, on the one hand, "shares" or, on the other, "money" within the meaning of section 420 of ITEPA. The FTT did not address itself to that question in terms. To the contrary, it expressed the view that it did "not need to consider the detail of s 420(5)(b) or the other minutiae of Part 7".

Authorities relied on by HMRC

46. Mr Brennan argued that the case that Mr Goodfellow advanced on behalf of Tower and Total is inconsistent with a number of authorities: *NMB Holdings Ltd v Secretary of State for Social Security* (2000) 73 TC 85, *DTE Financial Services Ltd v Wilson* (2001) 74 TC 14, *PA Holdings Ltd v HMRC* [2011] EWCA 1414, [2012] STC 582 and *Aberdeen Asset Management plc v HMRC* [2013] CSIH 84, [2014] STC 438. We shall take these decisions in turn.

47. The *NMB* case involved an attempt to avoid NICs. To this end, bonuses were awarded to a company's directors by conferring on them beneficial interests in platinum sponge which was promptly sold back to the bank that always held it. Langley J concluded (at 125) that:

> "the *Ramsay* principle does entitle the Secretary of State to characterise what happened and the cash receipts the directors in fact obtained as payments in cash and not in kind within the meaning of the relevant provisions".

48. Langley J's decision was endorsed by Lord Hoffmann in *MacNiven v Westmoreland Investments Ltd* in the following passage (paragraph 68):

> "I have no doubt that Langley J was right when he recently decided in *NMB Holdings Ltd v Secretary of State for Social Security* ... that a payment of bonuses to directors in the form of platinum sponge held in a bank, accompanied by arrangements under which they could immediately sell it for cash to the bank, was not a 'payment in kind' which fell to be disregarded for the purpose of national insurance contributions. In commercial terms the directors were paid in money. It is obvious that such a transaction was not what the Social Security (Contributions) Regulations 1979, SI 1979/591 contemplated as a payment in kind."

49. The decision in the *NMB* case is undoubtedly consistent with the approach espoused by Mr Brennan in the present case. It can also, however, be reconciled with Mr Goodfellow's submissions, on the basis that the concept of a "payment of kind", as used in the relevant legislation, referred to "things of either a consumable nature or which carried with them a degree of permanence such that an employee could be expected to use or retain them rather than seek to realise them for cash" (see Langley J's judgment, at 123). It is noteworthy, too, that the *NMB* case pre-dates the clarification of the *Ramsay* principle in *MacNiven* and *Mawson*.

50. In the *DTE* case, an employer contended that the PAYE system did not apply where directors had been provided with bonuses by giving them, not immediate cash payments, but contingent reversionary interests which fell in shortly after their transfer to the directors. However, the Court of Appeal, applying the *Ramsay* principle, held the scheme to be ineffective. Jonathan Parker LJ, with whom Sedley and Potter LJJ agreed, said of the "contingent" interests (in paragraph 14):

> "The interest is 'contingent' in a theoretical sense only; in reality there is no risk of the contingency not occurring. Thus, for all practical purposes the so-called contingent reversionary interest is no more nor less than a right to a specified sum of cash on a future date; the specified sum being the amount of the intended bonus and the specified date being the date on which the employer wishes the employee to receive the bonus."

Later in his judgment (at paragraph 42), Jonathan Parker LJ said:

> "So far as the *Ramsay* issue is concerned, therefore, the only question (to my mind) is whether it is legitimate to apply the *Ramsay* principle or, if one prefers, adopt a *Ramsay* approach to the concept of 'payment' in the context of the statutory provisions relating to PAYE. In my judgment it plainly is. I accept [counsel for HMRC's] submission that in the context of the PAYE system the concept of payment is a practical, commercial concept. In some statutory contexts the concept of payment may (as Lord Hoffmann pointed out in *MacNiven*) include the discharge of the employer's obligation to the employee, but for the purposes of the PAYE system payment in my judgment ordinarily means actual payment: i.e. a transfer of cash or its equivalent."

51. In our view, the *DTE* case, like the *NMB* case, takes matters little further for present purposes. It turns on the interpretation (in the light of the *Ramsay* principle) of "payment". Rather different considerations apply to the construction of section 420 of ITEPA, on which the present case depends.

52. Nor, as it seems to us, does *PA Holdings* add much of importance. In that case, a company that wished to pay its employees bonuses had adopted arrangements whereby the employees who would have been paid bonuses were awarded shares and received dividends on them. The FTT concluded that payments to the employees were "emoluments" (within Schedule E) in the hands of the employees but that the payments also fell within the provisions of section 20 of the Income and Corporation Taxes Act 1988 ("ICTA") and so fell to be charged under Schedule F. The Court of Appeal, however, explained that income cannot fall within more than one Schedule: the finding that the income fell within Schedule E thus precluded any finding that the income fell within Schedule F (see paragraph 63).

53. Moses LJ (with whom Maurice Kay and Arden LJJ agreed) noted that this conclusion was sufficient to dispose of the case (see paragraph 66), but he went on to say that he "should not overlook the application of the principles summarised by Lord Nicholls in [*Mawson*]". Having quoted both from Lord Nicholls' speech and Ribeiro PJ's "neat apothegm", Moses LJ said:

> "[67] The purpose of the relevant statutory provisions is to classify the income according to an appropriate and mutually exclusive schedule. In the instant appeal, viewed realistically, the payments were emoluments.
>
> [68] The insertion of the steps which created the form of dividends or distributions did not deprive the payments of their character as emoluments. The insertion had no fiscal effect because s 20, construed in its statutory context, does not charge emoluments under Sch F. The exotic attempt advanced orally by [counsel for the employer] to classify both the award of the shares and the

> distributions as income and thereby raise the spectre of double-recovery fails for the same reason. The award of the shares and the declaration of the dividend were, in reality not separate steps but the process for delivery of the bonuses."

54. These comments are of course consistent with the case advanced by Mr Brennan, but they do not appear to us to lend it any substantial support. What matters in the present case is the proper interpretation of section 420 of ITEPA. *PA Holdings* revolved around the construction of different provisions.

55. The last case on which Mr Brennan relied was *Aberdeen Asset Management plc v HMRC*. Like the *DTE* case, this was concerned with the meaning of "payment" in the context of the PAYE scheme. With a view to avoiding tax, an employer had routed money to employees via an employee benefits trust and "money box" companies that were incorporated for the benefit of the employees. By the time the case reached the Inner House of the Court of Session, it had come to be accepted that the relevant sums were taxable under Schedule E as "emoluments", but there remained an issue as to whether the PAYE scheme applied. The Inner House held that it did, taking the view that the transfer to each employee of shares in the relevant "money box" company constituted a "payment" within the meaning of section 203(1) of ICTA. The core of Lord Glennie's reasoning on the point can be seen from paragraph 66, where he said:

> "[T]he test is a practical one, to be determined as a matter of fact. The findings of the First-tier Tribunal … are findings of fact that the effect of the Scheme was to place the money in the money box companies unreservedly at the disposal of the individual employees to whom the shares were allotted. Those findings are, in my view, determinative of this argument. What happened under the Scheme amounted to payment."

In similar vein, Lord Drummond Young observed that "[i]n the construction of tax legislation, in particular, it has been emphasised that payment is a practical commercial concept" (paragraph 33) and that "[t]he fact that the employee has practical control over the disposal of the funds is sufficient to constitute a payment for the purposes of the legislation" (paragraph 34). Lord Drummond Young had earlier said (in paragraph 27):

> "It is clear in my opinion that the legislative intention underlying these provisions of the Taxes Act is that all emoluments paid to employees should be subject to Sch E income tax; that such tax should be deductible by the employer in accordance with the PAYE system at latest at the time when payment is actually made to the employee; and that the employer should account for the tax deducted to HMRC, once again in accordance with the PAYE system. The definition of 'emoluments' is significant, in that it is very wide and demonstrates a

> clear intention that every form of benefit received by an employee on account of his employment should fall within the ambit of Sch E tax. It is also clearly intended that the PAYE system should be a comprehensive system for recovering Sch E tax. That is apparent from the width of the wording of s 203(1), which refers to the making of 'any payment of … any income assessable to income tax under Sch E'. Consequently, in considering whether a particular receipt or benefit obtained by an employee falls within Sch E income tax and within the PAYE system, the intention underlying the legislation that both of these should be comprehensive in nature is a consideration of the greatest importance. It is also important in my opinion to bear in mind the importance of PAYE in the tax system. PAYE secures, and is plainly designed to secure, the prompt and efficient collection of tax in respect of every sort of employment."

56. In our view, the *Aberdeen* case, like the others to which Mr Brennan referred us, is not of much help to us. It dealt with the meaning of "payment" in a specific statutory context. It casts little light on how section 420 of ITEPA, the key provision in the present case, is to be construed.

57. In short, it seems to us that, while the cases cited by Mr Brennan illustrate the application of the *Ramsay* principle, they provide no substantial guidance as to the proper interpretation of Part 7 of ITEPA or, more specifically, whether Mr Litman, Mr Coombs and Mr Thorne are to be considered to have acquired "shares" or "money" within the meaning of section 420 of ITEPA.

"Shares"/"money"

58. We turn then to the central issue: are Mr Litman, Mr Coombs and Mr Thorne to be considered to have acquired "shares in any body corporate" (within section 420(1)(a) of ITEPA) or "money" (within section 420(5)(b))?

59. As already noted, that issue has to be approached in the light of the *Ramsay* principle. It is therefore incumbent on us to construe section 420 of ITEPA purposively and to take a realistic view of the facts.

60. In the *UBS* case, Rimer LJ expressed the view that there could be circumstances in which a purported award of shares would involve the acquisition of "money", not "shares", for the purposes of section 420 of ITEPA. As can be seen from paragraph 40 above, he said:

> "there might be cases in which, even though what was nominally awarded were shares, an objective interpretation of the true nature of the arrangements would justify the conclusion that in fact the employee was being paid money: for example, if the shares were required to be redeemed immediately for a pre-ordained cash sum".

61. The present case is, Mr Brennan argued, an example of an award of money: payments of money were merely dressed up to look like awards of shares. Moreover, various distinctions exist (so it was said) between this case and the *UBS* case. Mr Brennan referred, in particular, to the "very close identity between the employers and their respective employees" which the FTT noted in the present case (see paragraph 158(2) of the Decision), as a result of which (in the FTT's words) "[i]t was, in effect, the employees who made the decision to implement the scheme proposed by [Barnes Roffe]" (paragraph 158(2) of the Decision). Mr Brennan contrasted the schemes adopted by UBS and Deutsche Bank, which, he said, involved arm's length arrangements.

62. On balance, however, we agree with Mr Goodfellow that Mr Litman is to be considered to have been awarded "shares", not "money", within the meaning of section 420 of ITEPA and, hence, that Chapter 2 of Part 7 of ITEPA is applicable in his case. Our reasons include these:

(i) There is no doubt that, in company law terms, Mr Litman acquired shares in a body corporate. He was registered as a shareholder of SPV 1 with effect from 5 April 2004, and he was still a shareholder when the company went into members' voluntary liquidation on 26 July 2004;

(ii) The words "shares in any body corporate" (which are to be found in section 420(1)(a)) are less susceptible to a non-technical reading than, say, "payment", "payment in kind" or "emolument" (with which the *NMB*, *DTE*, *PA Holdings* and *Aberdeen* cases were concerned). On the face of it, Parliament was referring to a legal, not commercial or business, concept (compare the remarks of Lord Hoffmann mentioned in paragraph 48 above);

(iii) The fact that, as the FTT found, the Scheme had no commercial purpose other than obtaining a tax advantage cannot necessarily preclude the application of Chapter 2 of Part 7 of ITEPA. The *Mayes* case shows that tax avoidance schemes can be effective. In fact, schemes which (like the Scheme) attempted to use Part 7 of ITEPA to enable bonuses to be provided to employees without incurring income tax or NICs were upheld in the *UBS* case. It cannot, accordingly, be enough for HMRC to point out that the Scheme was adopted only to avoid tax or that it was always envisaged that Mr Litman would sooner or later receive money via it;

(iv) Section 420 defines "securities" in a very broad way. That, it is fair to infer, was no accident. A narrower definition could itself have given rise to "opportunities for unacceptable tax avoidance" such as Part 7 was designed to eliminate (as Lord Walker explained in the *Gray's Timber Products* case – see paragraph 16 above). More specifically, there can be no doubt that section 420 was intended to extend to some

"artificial" schemes - Lord Walker, it will be recalled, identified the elimination of "opportunities for unacceptable tax avoidance" as the third purpose of the legislation;

(v) ITEPA nowhere indicates that Chapter 2 of Part 7 does not apply to owner-managed companies. Again, any such restriction would have facilitated tax avoidance;

(vi) When the "A" shares in SPV 1 were transferred to Mr Litman, it was envisaged that he would retain them for at least two years (albeit for CGT reasons). Even as matters turned out, he had held them for the best part of four months by the time SPV 1 was put into liquidation. That cannot be regarded as a negligible period;

(vii) In the *UBS* case, Rimer LJ contemplated that an employee could be treated as acquiring money rather than shares if, for example, "the shares were required to be redeemed immediately for a pre-ordained cash sum". There was no such requirement in Mr Litman's case;

(viii) The amount of money that Mr Litman received via the Scheme was never likely to correspond exactly to the £1 million that Tower subscribed for the "A" shares. That figure stood to be augmented by the receipt of returns on investments, but reduced by tax on those returns and the costs of SPV 1's liquidation. In the event, Mr Litman's receipts totalled slightly more than the £1 million: some £1,005,325;

(ix) It is fair to say that the redemption value of the shares used in the UBS scheme was likely to depart more radically from the cost of acquisition (since the subscription money was invested in shares in UBS), but the SPV used for the Deutsche Bank scheme had to invest in a narrow range of low risk investments such as UK gilts and triple A corporate bonds. HMRC's "broad" *Ramsay* point was nonetheless rejected by the Court of Appeal in the case of the Deutsche Bank scheme as well as the UBS scheme; and

(x) The flaw in ITEPA, as it stood during the relevant period, seems to us to have lain, not in the definition of "securities" given in section 420, but in the limited list of "chargeable events" in combination with the absence of an anti-avoidance provision such as it now contains (see paragraph 19 above). We do not think that the deficiencies in the legislation can be overcome in Mr Litman's case by unnaturally narrowing the scope of (the deliberately wide) section 420.

63. We have found it harder to decide whether Mr Coombs and Mr Thorne are to be regarded as having acquired "shares" rather than "money" for the purposes of section 420. As the FTT found, at paragraphs 40 and 42 of the Decision, Mr Coombs and Mr Thorne never intended to keep their shares for any extended

period before SPV 147 and SPV 148 were wound up, and the companies were in fact put into members' voluntary liquidation the day after their "A" shares were transferred to Mr Coombs and Mr Thorne. Further, there was no question of SPV 147 or SPV 148 making any investments. The case for dismissing the transactions as "money in, money out" arrangements is thus stronger here than with Mr Litman.

64. On the other hand:

(i) Mr Coombs and Mr Thorne, like Mr Litman, acquired shares in a body corporate as a matter of company law, and the words "shares in any body corporate" cannot easily be construed in a non-technical way;

(ii) There was no requirement for the shares transferred to Mr Coombs and Mr Thorne "to be redeemed immediately for a pre-ordained cash sum" (to quote from Rimer LJ) – they could have redeemed them at any time;

(iii) There was no prospect of the money that Mr Coombs and Mr Thorne received via the Scheme corresponding precisely to the amounts that Total paid for the "A" shares in SPV 147 and SPV 148. The costs of liquidation were bound to result (and did result) in Mr Coombs and Mr Thorne receiving slightly less than the subscription money; and

(iv) The sums that Mr Coombs and Mr Thorne received were paid to them as shareholders in the course of the liquidation of SPV 147 and SPV 148 by their liquidator. That tends to confirm that they should be seen as having acquired "shares" and not merely "money".

65. In all the circumstances, we have in the end concluded that we must again respect the words used in section 420 of ITEPA, with the consequence that Mr Coombs and Mr Thorne, like Mr Litman, should be regarded as having acquired "shares", not "money", within the meaning of that section, and that Chapter 2 of Part 7 of ITEPA applies.

Section 423(2) of ITEPA

66. Just before concluding his oral submissions. Mr Brennan introduced an argument founded on section 423(2) of ITEPA. As mentioned above (paragraph 17), this provides for the subsection to apply to provision under which there will be a transfer, reversion or forfeiture of employment-related securities "if certain circumstances arise or do not arise". Mr Brennan noted that in the *UBS* case (as can be seen from paragraph 60 of Rimer LJ's judgment) counsel for UBS "accepted there must be a real, genuine possibility of the stated circumstances occurring: if they were never going to happen in the real world, a purposive interpretation of s 423 would exclude them from its contemplation". Mr Brennan submitted that in the present case the FTT had in

effect found that the relevant circumstances were not going to happen in the real world.

67. The part of the Decision on which Mr Brennan relied in this context was paragraph 108. The FTT there said this:

> "We do not accept the assertions by the witnesses that the provision in the SPV articles that an employee could be required to dispose of his shares at 95% of their value, had any commercial purpose. We acknowledge that an *effect* of the forfeiture provisions was to reduce slightly the value of the A shares in certain circumstances connected with the employee leaving, but we do not accept that employee retention was a *purpose* of those provisions – they were included solely to ensure that the A shares constituted restricted securities under the Part 7 legislation. The discount of only 5% would be an ineffective deterrent; the employees in both appeals were effectively the long-term owner-manager or owner-managers of the respective employer companies and so were very unlikely even to consider leaving; and the advice letters from [Barnes Roffe] are transparent that the provision is driven by the requirements of s 423 (even down to the detail of the five year limit in s 425)."

68. There is, however, more than one answer to Mr Brennan's argument. In the first place, we do not read paragraph 108 of the Decision as amounting to a finding that the relevant circumstances were "never going to happen in the real world". The FTT said no more than that employees were "very unlikely" even to consider leaving. A second point is that, in the *UBS* case, the Court of Appeal accepted (at paragraph 147) a submission on behalf of Deutsche Bank to the effect that:

> "there is no stress in ss 423 to 425 of Ch 2 on why the restrictions are in place, that is whether they are there for commercial reasons or otherwise, nor whether the employee can ensure that they do not apply. The stress is simply on whether the restrictions reduce value, nothing more."

In the present case, it can be seen from paragraph 108 of the Decision, the very paragraph on which Mr Brennan placed reliance, that the FTT accepted that an effect of the forfeiture provisions was "to reduce slightly the value of the A shares in certain circumstances connected with the employee leaving", and in paragraph 137 of the Decision the FTT concluded (as mentioned previously):

> "the forfeiture clause in the SPV's articles of association … does constitute an arrangement or condition which makes provision for a forfeiture as described in s 423(2) such that the market value of the shares is less than it would be but for that provision. HMRC made no

argument to the contrary. Thus the 'A' shares in the SPV do constitute 'restricted securities' as defined in s 423."

That leads to a third point, which is that HMRC have not cross-appealed. In particular, they have not sought to challenge the FTT's finding that the forfeiture provisions reduced the value of the shares. In Mr Goodfellow's words, that ship has sailed.

Overall conclusion

69. However unattractive the result may be, it seems to us that the appeals before us must be allowed. In our view, the issue identified in paragraph 3 above falls to be answered in the negative. Chapter 2 of Part 7 of ITEPA is applicable, with the consequence that no income tax or NIC liability can have arisen. We invite the parties to make further submissions relating to the manner in which we should dispose of the appeals in the light of that conclusion.

Mr Justice Newey **Judge Colin Bishopp**

RELEASE DATE: 13 February 2015