[2016] UKFTT 0253 (TC)

TC05028

Appeal number: TC/2013/03364

INCOME TAX – tax avoidance scheme – Partnership purchasing rights to dividends and receiving dividends – whether dividends are excluded from the computation of income of the Partnership for tax purposes giving rise to a loss – section 730 ICTA 1988 – held no – whether Partnership trading in short-dated securities – held yes – whether the purchase of dividend rights and receipt of dividends were transactions in the course of that trade – held no – whether certain fees in respect of tax advice were a deductible trading expense – held no – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

CLAVIS LIBERTY 1 LP (acting through Mr D J COWEN) Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS Respondents

TRIBUNAL: JUDGE JOHN WALTERS QC
ELIZABETH BRIDGE

Sitting in public at The Royal Courts of Justice, London on 9 to 13 March 2015

Andrew Thornhill QC and Jonathan Bremner, for the Appellant

David Goy QC and Imran Afzal, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. This is an appeal by Mr D J Cowen, a former member of the limited partnership known as Clavis Liberty Fund 1 LP ("the Partnership"), against a closure notice, dated 1 February 2013, issued to Mr Cowen as "successor" to the Partnership. That closure notice amended to nil, from £60,942,061, the amount of the trading loss claimed to have been sustained by the Partnership in respect of its accounting period running from 14 March to 5 April 2006.

2. The dispute between the Partnership and the Respondents ("HMRC") relates principally to the tax treatment of a dividend of £60 million paid to the Partnership by Helios Limited ("Helios") on 5 April 2006. Helios had been incorporated in the Cayman Islands on 6 January 2006 and resolved, on 19 January 2006, that it would be managed and controlled from the offices in the UK of its sole director, SG Hambros Trust Company Limited ("SGHTC").

3. The Partnership's case is that, by virtue of section 730 Income and Corporation Taxes Act 1988 ("ICTA"), that dividend of £60 million, although actually received by the Partnership, is deemed to be the income of Dickens Ventures Limited ("Dickens"), a company incorporated in 2004 in the British Virgin Islands, because the right to receive it was sold to Helios by Dickens without any sale of the shares, in respect of which the dividend was paid. Those shares were owned and retained by Dickens. HMRC submit that section 730 ICTA does not have the effect for which the Partnership contends.

4. The Partnership has also claimed a trading deduction for a fee of £761,363.45 in respect of tax advice, rendered by Mercury Tax Strategies Limited ("Mercury") in an invoice dated 15 March 2006. This deduction has also been disallowed in the closure notice amendment.

5. The appeal was conducted on the basis that four issues arise for our determination. They are: (1) was the Partnership carrying on a trade in its accounting period ended 5 April 2006?; (2) if so, were the particular transactions claimed to produce the loss (namely the transactions by which the Partnership arranged to receive the dividend from Helios) trading transactions?; (3) does section 730 ICTA have the effect claimed by the Partnership?; and (4) if the Partnership was trading, were the fees in respect of tax advice paid to Mercury deductible in computing the profit/loss of the trade?

6. We received a Witness Statement from Mr Christopher Derricott, Chief Executive of Curzon Capital Limited ("Curzon"), investment adviser to the Partnership. Mr Derricott gave oral evidence and was cross-examined by Mr Goy QC, for HMRC. We also received a witness statement from Mr Andrew Fitton, presented by the Partnership as an expert witness able to assist the Tribunal in determining whether the Partnership's business strategy could be considered to be a valid trading strategy. Mr Fitton also gave oral evidence and was cross-examined by Mr Goy.

7. We also had a Witness Statement from Mr Terence Mowschenson QC (an expert witness instructed by the Partnership) dealing with certain matters of Cayman Islands law. Mr Mowschenson's evidence was accepted by Mr Goy and he was not called to speak to his statement.

8. We should mention that the Partnership had attempted to obtain evidence from Mr Simon Young, Managing Director of Sanne Trust Company Limited ("Sanne") and from Mr Peter Machon, a director of Sanne. (Sanne was appointed by the General Partner of the Partnership, Clavis Liberty 1 G.P. Limited ("the General Partner"), to be the administrator of the Partnership.) The Tribunal did issue witness summonses to these two individuals, neither of whom is resident in the UK, but subsequently set the summonses aside. This occasioned satellite litigation in this appeal, ultimately resulting in a decision of the Upper Tribunal (Warren J) given on 12 February 2015 (under reference [2015] UKUT 72 (TCC)) whereby the Partnership's appeal was dismissed, Warren J holding that the Tribunal had no jurisdiction to summons Mr Young and Mr Machon.

9. We also had before us extensive documentation to which we shall make reference as appropriate.

10. From the evidence, we find facts as follows.

Facts

11. The Partnership was registered in Jersey under the Limited Partnership (Jersey) Law 1994 on 9 March 2006. It was 'established' by an agreement dated 14 March 2006 ("the Limited Partnership Agreement") between the General Partner and Sanne in its capacity as trustee of a declaration of trust dated 29 July 2004 known as the SL2 Charitable Trust. Recital A of the Limited Partnership Agreement records that the parties thereto had agreed to establish the Partnership 'for the purpose of making a profit other than by means of investment principally through the acquisition of short dated fixed income receivables, dividends and the rights to receive dividends and to carry out all functions and acts in connection therewith'.

12. Subsequently over 100 individuals were admitted to the Partnership as further limited partners (in addition to Sanne, the original limited partner). They subscribed over £62 million capital to the Partnership.

13. On 21 March 2006 a facility was arranged whereby SG Hambros (Channel Islands) Limited ("SGHCI") would advance funds to partners in the Partnership. Pursuant to that facility, on 23 March 2006, the General Partner, as agent for the limited partners, requested an advance of £59,700,707. On the same day (21 March 2006) SGHCI made a formal offer to the General Partner, as agent for the limited partners, who were to be the borrowers, of an amount of up to £61 million, available for drawdown. The loans were to be made for a maximum period of 60 days following drawdown. They were to be secured against the assets of the Partnership pursuant to a guarantee and security agreement in SGHCI's standard form.

14. On the same day (21 March 2006) a board meeting of the General Partner took place at the Sofitel Hotel, Gatwick. There were present Mr Young (Chairman) and Mr Machon, and also in attendance were a Mr William Graham from Curzon, described as Investment Advisor to the Fund (the Partnership) and Sponsor and Operator to the Fund, as well as a Mr Neil Buckley from Mercury, described as Tax Advisor to the Fund. At that meeting the General Partner resolved to approve the facility, it being noted that, pursuant to a power of attorney, the directors of the General Partner were authorised to execute a facility letter on behalf of the General Partner acting as agent for the limited partners as borrowers.

15. Curzon's advice was tendered with the intention of applying the Partnership's 'strategy' which was formulated as being 'to improve on the return then available through holding the funds on deposit with a bank (then around 4.1% per annum) with a similar level of risk by trading in short-dated highly-rated financial instruments including bonds and equity dividend rights'. This 'strategy', described in the minutes of the board meeting of 21 March 2006 as a 'trading strategy set at the meeting on 15 March 2006', had not, at that stage, been implemented due to lack of sufficient cleared funds.

16. However, on 23 March 2006, a further board meeting of the General Partner was held, this time at Clarges Street, London W.1, at which (according to the board minutes) 'trading recommendations' by Curzon were received. This time, in addition to Mr Graham, Mr Derricott (who gave evidence at the hearing) was present at the meeting, representing Curzon, and the minutes record that Curzon recommended to the directors of the General Partner that certain trades in US Dollar Treasury Stock and UK commercial paper should be made, confirming that the proposed trades were in accordance with the 'trading strategy' agreed at the meeting of the General Partner on 15 March 2006 and with the Information Memorandum, and that the proposed trades were in the best interests of the Partnership. The General Partner formally resolved to approve the recommendation.

The Information Memorandum

17. The Information Memorandum, inviting subscriptions to the Partnership from individuals who were resident and ordinarily resident in the UK for tax purposes had been issued in January 2006. It informed the public that the 'Clavis Liberty Fund Partnerships' (of which the Partnership was one) were sponsored by Curzon (who issued the Information Memorandum). It gave general information about the Partnerships, in particular that they had been established for the purpose of making a profit other than by means of investment, principally through the acquisition of short-dated fixed income receivables, dividends and the rights to receive dividends. (We note that at the time the Investment Memorandum was issued, the Partnership had not, in fact, yet been established.)

18. Section 1 of the Information Memorandum, besides describing the business of the Partnerships, explained that they intended to fund their operations by raising up to £70 million per Partnership through capital contributions from individual partners. The minimum capital contribution for an individual partner was stated to be £109,000, with an initial capital contribution of £9,000 per £109,000. It was stated that the

General Partner had made arrangements whereby partners (if they so desired) could provide up to 100 per cent. of their capital contribution (less their initial capital contribution) by way of capital loans, defined as ‘full recourse loans to enable an individual partner to increase his or her capital contribution to a Partnership’.

19. The capital contributions to the Partnership (of £62,685,745) were in fact substantially funded by capital loans made by SGHCI – see below, but it is to be noted that other cash to the amount of £9,000 per £109,000 invested was to be provided by the subscribing partners from other resources.

20. The Information Memorandum advised intending subscribers, under the heading “Short-Term Tax Relief” that ‘under current UK tax legislation, the Partnerships should be able to write off up to 100 per cent. of their initial expenditure in the first year of operation. As a result, the Partnerships may expect to incur trading and/or tax losses in their first year.’ Any such trading and/or tax losses would be allocated to partners in accordance with their individual Partnership participations and partners ‘should be able to offset their share of the losses in a variety of ways’ as described in section 2 of the Memorandum.

21. Section 2 of the Memorandum, under the heading “Taxation” contained detailed guidance. However it was introduced by a caveat stating that it was based on Mercury’s understanding of relevant UK taxation law and practice “(which is subject to change)” as at the date of the Memorandum. There followed a general disclaimer of responsibility for the tax advice given on the part of Curzon, the Partnership and its advisers. There followed a mention that the General Partner had sought advice from named tax counsel, who had given their opinion that tax relief should be available to partners in the Partnerships, but that no guarantee could be given that tax relief would be available.

22. Section 2 of the Memorandum stated that the main ways of treating the expected losses for tax purposes were by set-off against general income in the year of assessment in which the loss was incurred, or the preceding year or by carry-back for set-off against income of the preceding three years, or by carry-forward against future profits of the same trade. There was also guidance that interest on loans taken out by a partner to make a capital contribution to the Partnership should qualify for tax relief. Mention was also made of the restriction to the availability of sideways loss relief provided by sections 118ZE and 118ZG ICTA.

23. The Information Memorandum contained application forms including a pro forma subscription agreement, a power of attorney (in particular to sign, execute and deliver a loan agreement to provide a capital loan), a pro forma capital loan application letter, addressed to SGHCI, and a money laundering certificate.

The business transactions entered into by the Partnership

24. A schedule was prepared by HMRC for the Tribunal’s use containing a summary of financial trades undertaken by the General Partner ‘from inception to 30 April 2007’. It was put to Mr Derricott and Mr Fitton. No objection as to the accuracy of

the schedule was made by the Partnership. We find that it accurately recorded the transactions entered into by the Partnership.

25. The trades are divided in that schedule into 4 periods: the period from 14 March 2006 to 5 April 2006; the period from 6 April 2006 to 18 May 2006 – the day before the individual limited partners sold their partnership interests, a matter we will come to later – the period from 19 May 2006 to 29 September 2006 – the date when the Partnership ceased to be resident in the UK – and the period from 30 September 2006 to 30 April 2007.

26. In the period from 14 March 2006 to 5 April 2006 there were four acquisitions. On 27 March 2006, $102,100 US Treasury Bills with a redemption date of 30 March 2006 were purchased. This stock was held to redemption and a profit of £17,778.21 was recorded (the difference between the redemption proceeds and the acquisition price). Also on 27 March 2006, two holdings of Dexia commercial paper with a redemption date of 12 April 2006 were purchased. The first holding (£800,000 nominal) was in fact sold before redemption, on 3 April 2006, for a profit of £680.45. The second holding (£1,700,000 nominal) was held to redemption and a profit of £3,343.96 was recorded on 12 April 2006.

27. The final acquisition in the period from 14 March 2006 to 5 April 2006 was the dividend rights with which this appeal is principally concerned. The date of acquisition is recorded on the schedule as 3 April 2006 and the date of redemption (payment of the dividend) as 5 April 2006. The cost of acquisition is recorded as £59,958,000 (immediately funded by the proceeds of redemption of the US Treasury Bills (£59,013,929.83) as recorded in the minutes of the board meeting of the General Partner on 31 March 2006) and the proceeds (the dividends) are recorded as £60,000,000. The apparent profit on the transaction was therefore £42,000.

28. The minutes of the board meeting of the General Partner on 31 March 2006 show that a resolution to purchase the dividend rights was made at that meeting. The profit of £42,000, if attributed to a holding of the rights for the period from 31 March 2006 to 5 April 2006 (counted as 6 days according to the evidence of Mr Fitton), would give an annual rate of return of about 4.26%, which was in line with the Partnership's "strategy" as we have recorded it. Obviously if the profit of £42,000 is attributed to a holding of the rights for the period from 3 April 2006 to 5 April 2006 (counted as 3 days), the annual rate of return is double (8.52%).

29. This matter was explored at the hearing and the position appears to have been, and we find, that the transaction yielding a profit of £42,000 was presented to the Partnership as at 31 March 2006, on the basis that the dividend rights would be purchased on that day. However, although authority to conclude the transaction was given by the General Partner to SGHCI on 31 March 2006, in fact the purchase was not made until 3 April 2006, and, despite that delay in paying the purchase price of £59,958,000, the price for the rights was not adjusted and the deal was concluded on the terms that had been arranged. In the result, the Partnership actually achieved an annualised return of 8.52% on its investment, double the level anticipated by the Partnership's "strategy".

30. In the period from 6 April 2006 to 18 May 2006, the schedule already referred to records that the Partnership made 14 further acquisitions of short-dated commercial paper. The stocks acquired were all held to redemption, which occurred in that period, so that the Fund was entirely invested in cash at 18 May 2006. The total purchase price (which will have included redemption proceeds used for further acquisitions) was £173,032,573.41 and the total redemption proceeds was £174,986,996.86, and a profit of £257,767.41 resulted. The sums laid out for these acquisitions varied from £3,993,189.97 to £29,548,030.20. The Partnership was conducting a substantial business in this period.

31. In the period from 19 May 2006 to 29 September 2006 (some 4 months), the Partnership operated at a much lower level of activity, both in terms of the amounts of money deployed in the business and the frequency of transactions. There were 8 acquisitions of commercial short-dated paper in that period. They were all held to maturity. The sums laid out ranged from £499,450 to £1,147,858.40 and the total profit recorded was £10,551.16.

32. In the period from 30 September 2006 to 30 April 2007 (some 8 months), the Partnership operated at an even lower level of activity. There were 9 acquisitions and the amounts laid out ranged from £289,110.92 to £1,195,754.42. All the stocks acquired were held to maturity, producing a profit of £11,758.66.

The transaction in dividend rights with which the appeal is principally concerned

33. We now turn to the transaction with which this appeal is principally concerned. The rights to interim dividends totalling £60 million, declared on 30 March 2006 by SG Hambros Trust Company Limited as sole director of Helios, were the subject of a Dividend Purchase Agreement dated 31 March 2006 ("the DPA") between Dickens and a company called Hanon I Limited (as nominee for Dickens as beneficial owner) on the one hand and the General Partner acting as general partner of the Partnership on the other.

34. It was stated in the DPA that Helios was an exempted company (incorporated – as we have noted above – in the Cayman Islands). The DPA provided for the sale of the rights to the interim dividends concerned to the Partnership for the total consideration of £59,958,000 which 'must be paid' on 31 March 2006. The consideration was to be paid into an account of Dickens with Schroder and Co. Limited ("Schroder").

How Helios could declare interim dividends of £60 million – the loan from Schroders

35. The circumstances in which Helios was in a position to declare interim dividends totalling £60 million on 30 March 2006 were as follows.

36. On 2 March 2006, Schroders granted a loan facility of up to £65 million to Dickens. On 15 March 2006 the board of Dickens approved the execution of the letter providing for that facility, noting that it was the intention of Dickens to use the facility to make a capital contribution to Helios. On 20 March 2006, pursuant to the facility, Dickens drew down £61 million. Dickens requested Schroders to pay the funds into an account with Schroders in the name of Helios. The capital contribution was treated by Helios as if it were a share premium available for distribution.

37. By a document dated 20 March 2006 entered into between Helios and Schroder, Helios guaranteed the loan, and by another document of the same date between the same parties, Helios secured its guarantee by a charge, in favour of Schroders, of the account to which the funds drawn down had been credited, and those funds.

How the Partnership could purchase the dividend rights from Dickens for £59,958,000 – the loan from SGHCI and the limited partners' contributions

38. The circumstances in which the General Partner was in a position to purchase from Dickens the rights to the interim dividends declared by Helios on 31 March 2006 for £59,958,000 under the DPA were as follows.

39. On 23 March 2006, the General Partner (acting through Mr Machon and Mr Young), on behalf of the limited partners in the Partnership, requested an advance of £59,700,707 to be paid by SGHCI into an account with SGHCI in the name of the General Partner as general partner of the Partnership. This request was made pursuant to the letter dated 21 March 2006 between SGHCI and the General Partner acting as agent for the limited partners in the Partnership, which granted the facility which we have already mentioned. A payment of £59,103,700 (the amount drawn down, net of fees of £597,007) was paid by SGHCI on 23 March 2006. As already noted, the facility letter included the term that an advance would be made for a maximum period of 60 days following drawdown and had to be repaid (with interest) at the end of that period. The advance was secured by a charge in favour of SGHCI over the assets of the Partnership.

40. In addition, the Partnership received a total of £3,582,045 in personally funded contributions from the limited partners. These contributions were received by 21 March 2006.

Dickens repays Schroders

41. Dickens applied the £59,958,000 received from the Partnership as sale consideration for the interim dividend rights in the repayment of the loan of £61 million by Schroders which had been drawn down on 20 March 2006. £61,115,374 was required to repay the loan with interest.

42. The balance needed to do this, over and above the sale consideration for the interim dividend rights, was in large part made up by a further interim dividend of £1,000,000 paid by Helios to Dickens, also declared on 30 March 2006 and paid on 12 April 2006. The right to receive that interim dividend was not part of the sale to the Partnership under the DPA. The payment of £1,000,000 was made by Helios out of the £61 million contributed by Dickens and provided by way of loan by Schroders.

43. Dickens was also in receipt of a 'facilitation fee' of £610,000 payable by Mercury under an agreement dated 7 March 2006 and billed by an invoice of the same date. The facilitation fee was payable by Mercury to Dickens under the agreement for Dickens's assistance to Mercury 'in providing its support and services to facilitate a product code-named Liberty'. Dickens was also entitled to a fee of 'an amount not exceeding £100,000' under an agreement with Westall Services Limited ("Westall"), a company incorporated in the British Virgin Islands, also dated 7 March 2006.

Under this agreement the fee due to Dickens was in respect of assistance provided to Westall by Dickens 'to assist [Westall] in providing its support and services to facilitate a product code-named Liberty'. There was also in our papers a copy of an agreement, also dated 7 March 2006, between Mercury and Westall. Under this agreement 'an amount not exceeding £82,000' was due immediately and payable within 12 months by Mercury to Westall for Westall's assistance to Mercury 'in providing its support and services to facilitate a product code-named Liberty2 [*sic*]'. It appears, and we find, that pursuant to these agreements an amount of approximately £710,000 was paid by ways of fees directly or indirectly by Mercury to Dickens. These fees, together with the further interim dividend of £1,000,000 paid by Helios to Dickens made up the shortfall in the full amount payable to Schroders on repayment of the advance made by Schroders to Dickens, over and above the sale consideration for the interim dividend rights received by Dickens from the Partnership.

44. It appears (and we find) that the amount of approximately £710,000 paid by Mercury to Dickens was in fact funded by the Partnership. There is in our papers an invoice dated 15 March 2006 raised by Mercury against the General Partner in the amount of £761,363.45 in respect of 'taxation advice to [the Partnership]'. This is the fee which is the subject of Issue 4 in this appeal. We find that, whatever the nature and value of any taxation advice rendered by Mercury to the Partnership, the main purpose of this flow of funds was to enable Dickens to pay its debt to Schroders.

Pirouet purchases the limited partners' interests in the Partnership and SGHCI obtains repayment

45. Helios paid to the Partnership on 5 April 2006 the interim dividends of £60 million, the rights to which had been purchased from Dickens under the DPA of 30 March 2006.

46. On 19 May 2006, as we have indicated above, all the limited partners sold their interests in the Partnership to a purchaser, Pirouet Investments Limited ("Pirouet"), a company with an address in the British Virgin Islands. This was following an offer made to the General Partner on behalf of the limited partners by Pirouet (from an address in Jersey) dated 25 April 2006. A sample agreement for the sale and purchase of a limited partner's interest was with our papers. The consideration for the sale of the interest was stated in the agreement to be: "The amount outstanding pursuant to the Loan [being the loan to the selling limited partner which had been made to him/her by SGHCI pursuant to the facility granted on 21 March 2006 to the General Partner on behalf of the limited partners] which is attributable to the Vendor [the selling limited partner] ("the Outstanding Amount") plus any interest which has accrued to (and including) the Completion Date [the date of payment to SGHCI or such later date as agreed in writing] in respect of such Outstanding Amount".

47. On 19 May 2006 Pirouet paid £60,129,942 to the General Partner as agent for the limited partners under these sale and purchase agreements, and the General Partner remitted that amount to SGHCI in repayment of the loans made by SGHCI to the limited partners under the facility granted on 21 March 2006.

48. Pirouet obtained an advance of this amount from SGHCI on 18 May 2006 to make the payment to the General Partner. Pirouet also received this amount on 19 May 2006 from the Partnership as a distribution (funded as to £60 million out of the interim dividends received from Helios), enabling it to repay the advance to SGHCI on the same day.

49. The limited partners, although protected from any shortfall in repayment of their indebtedness to SGHCI, entirely lost their personal contributions to the capital of the Partnership (in total £3,582,045). However there was no evidence of any complaint from any of the limited partners about this. Mr Derricott said in evidence that he (for Curzon) had never received any complaints from limited partners to the effect that the Partnership had performed very badly. We conclude (and find) that the limited partners regarded their personal contributions to the capital of the Partnership as payment for the tax losses which they hoped would result from the arrangements.

The application for the loan to be made to the limited partners – how the arrangements were viewed

50. There is also in our papers a document, apparently emanating from SG Hambros Private Banking ("SGHPB"), recording a credit application made in relation to "the Liberty Plan" by a customer "Liberty". The document is undated, but we were told that it dates from some time before 20 December 2005. It describes the tax planning with which this appeal is concerned and anticipates that SGHPB would lend to the limited partners the funds which were necessary to implement it – as happened by the advance of £59,700,707 by SGHCI to the General Partner on behalf of the limited partners, as noted above.

51. The SGHPB document is informative as it is evidence of the nature of the arrangements as it was expected in 2005 that they would be carried out. The document notes that the purpose of the credit application was "to enable UK resident individuals to participate in the 'Liberty Plan' which is a structure designed to mitigate income tax liabilities". It also notes that there were 2 potential sources of repayment "which are expected to occur within a maximum period of 3 months: 1 Distribution from the Partnership; [and] 2 Sale of the Partnership interest to a third party".

52. The document noted that "the Liberty Plan structure has been introduced to us [SGHPB] by [Mercury] who have developed the plan in conjunction with two leading Tax Counsels … [Mercury] are a well known small firm of tax advisers made up of specialist tax accountants and lawyers with whom we [SGHPB] have worked on previous planning arrangements, and are involved in developing UK Income and Capital Gains tax shelters".

53. Under the heading 'Plan Structure', the document explains that the plan involved UK resident individuals becoming members of a limited partnership resident in Jersey. The individuals would make capital contributions to the limited partnership "through a combination of personal contributions and the loan arrangements described in this proposal". The funds would be immediately used "to establish a 'trade' in buying and selling UK or French gilt strips, US Treasury Bills or short term

commercial paper issued by banks rated AAA to AA-". It was explained that the investments would mature within the loan period "(indeed before the dividend is purchased)" and "after a short time the [limited partnership] will use its funds to buy the right to a distribution from an arm's length third party". It explained the technical basis for the plan, namely that the consideration paid for the right to the distribution would be deductible for tax purposes but the receipt of the distribution would be tax free, giving rise to a tax loss available to the partners. It also explained that "following the purchase and receipt of the dividend, the [limited partnership would] continue to trade in various investments …".

54. The document also explains the steps involved in purchasing the rights to the distribution. It started with a proposed loan by SGHCI to a nominee company set up for the limited partners (eventually, the General Partner), which would be paid into an account with SGHCI, who would have the benefit of a security charge over the account. It emphasised that the stocks acquired by the Partnership would be held in the custody of SGHCI and subject to its charge. It mentioned that Schroders would establish the seller of the rights (eventually, Dickens) and lend it up to £65 million to acquire preference shares at a large (approximately £65 million) premium (in the event a capital contribution was made) in a subsidiary company (eventually, Helios). It noted that a SG Hambros company (eventually, SGHTC) would be the directors [*sic*] of the subsidiary.

55. The subsidiary would deposit the preference share subscription proceeds with Schroders as security for the loan to the seller of the rights. The subsidiary would declare the dividend, and prior to the payment of the dividend the Partnership would purchase the right to receive the dividend from the seller – the payment of the sale proceeds would be conditional on the seller using those funds to repay its loan from Schroders and would be used for that purpose. This would 'free up' the funds held by the subsidiary (from the charge in favour of Schroders) enabling it to pay the dividend. The funds held by the subsidiary, once released from that charge, would be transferred to a SG Hambros company and held on deposit by them for the subsidiary. The dividend 'of roughly £65 million' would be paid on the due date by the subsidiary to the Partnership and 'a 3rd party purchaser, which will not be a SG Hambros subsidiary, will most likely be sought to purchase the interest of [*sic*] the Partnership from the individual partners and will seek a 1 month loan for this purpose from SG Hambros. The collateral for this loan would be a charge over the assets of the Partnership (cash) which would be received by the Purchaser' (eventually, Pirouet). 'The cash assets received would be used immediately to repay the loan' [taken out, in the event, by Pirouet from SGHCI]. 'Simultaneously, the cash received by the [limited partners] will be used immediately by them to repay the [General Partner's] loan. The cash will always remain subject to the charge that [SG Hambros] has to support the [General Partner's] loan'.

A composite transaction

56. It can be seen from this document, and from the quick succession in which the relevant transactions were carried out in the event, to all intents and purposes following the planning set out in the document, that in all essentials (except the identity of the eventual purchaser of the limited partners' interest in the Partnership,

Pirouet, which we regard as an insignificant exception) the arrangements had been pre-planned before the end of 2005. They emanated from Mercury and were to be facilitated (in the true sense of the word) by funds made available by SG Hambros and Schroders and kept under the respective lender's control at all times. We find that the loan by Schroders to Dickens, the contribution by Dickens to Helios using the loaned funds, the resolution by Helios to pay the interim dividends of £60 million, the sale by Dickens to the Partnership of the rights to receive those dividends, the use by Dickens of the sale proceeds (and other funds as explained above) to repay Schroders, and the payment of the dividends by Helios to the Partnership was, as Mr Goy submitted on behalf of HMRC, a single composite transaction or 'a series or combination of transactions, intended to operate as such' which may, in accordance with the report of the Appellate Committee of the House of Lords in *Barclays Mercantile Business Finance Ltd v Mawson* [2005] STC 1 at [30] be taken into account when the application of section 730 ICTA to the facts of this appeal is considered.

The money flows

57. The evidence discloses three circular money flows of £60 million or more, one starting and finishing with Schroders and two starting and finishing with SGHCI. The funds have interlocking trajectories as follows.

58. First, Schroders lent £61 million to Dickens on 20 March 2006. That sum was advanced to Helios as a capital contribution. It was deposited with Schroders and secured by a charge in their favour. Helios then declared the interim dividends and sold the rights to £60 million of them to the Partnership. The funds lent by SGHCI to the limited partners and contributed to the Partnership (just under £60 million – the second circular money flow: see below) were applied by the Partnership on 3 April 2006 in the payment of the consideration for the dividend rights due to be paid by the Partnership to Dickens. This payment 'freed up' the funds held by Helios from the charge in favour of Schroders, but that charge applied to the consideration payment received by Dickens. In this way Dickens was in funds to pay back the loan to Schroders with interest on 12 April 2006, thus closing the first circle of money flows. Schroders had maintained valuable security for their loan throughout.

59. Second, SGHCI lent the limited partners just short of £60 million on 23 March 2006. These funds were paid into the account with SGHCI maintained by the General Partner on behalf of the Partnership. They were secured by a charge in favour of SGHCI. They were applied by the Partnership on 3 April 2006 in the payment to Dickens of the consideration for the dividend rights (and so were used in the first circular money flow: see above). SGHCI remained secured because their charge covered the right to receive the dividends. The Partnership received the dividend payment of £60 million from Helios on 5 April 2006, SGHCI's charge attaching also to those funds on receipt by the Partnership. On 19 May 2006 just over £60 million was paid by the Partnership to Pirouet as a distribution in respect of its interest acquired from the limited partners (see the third circular money flow, below) but on the same day Pirouet paid the General Partner on behalf of the limited partners the same sum as consideration for the purchase of their interests in the Partnership. This enabled the General Partner, on behalf of the limited partners, to repay SGHCI, with

interest, the loans originally made by SGHCI to the limited partners, thus closing the second circle of money flows. SGHCI had maintained valuable security for their loans throughout.

60. Third, SGHCI advanced just over £60 million to Pirouet on 18 May 2006. This was used by Pirouet to purchase the limited partners' interests in the Partnership on 19 May 2006 (see the second circular money flow, above). The distribution of the same amount made on the same day by the Partnership to Pirouet in respect of its newly acquired interest in the Partnership was applied on the same day in the repayment of the advance which had been made to Pirouet by SGHCI the previous day. In this way the third circle of money flows was closed.

61. These circular money flows show that Schroders and SGHCI retained control over the funds advanced by them respectively and obtained repayment together with interest (their profit). Mercury and Westall also received profits for their participation in the arrangements. The interest and those profits were effectively funded by the personal contributions of the limited partners (totalling just over £3.5 million in aggregate) which were all lost by them.

62. It is the Partnership's case in this appeal that in these circumstances the Partnership incurred a trading loss of £60 million, attributable to the limited partners.

The evidence of the witnesses

63. Mr Derricott, of Curzon, the company who approved the Investment Memorandum, made sure it was compliant with the requirements of the Financial Services Authority and was the investment/trading adviser of the Partnership. He said in cross-examination that he had not been aware at the time that the Investment Memorandum was produced that it was a necessary part of the tax strategy implemented by the arrangements involving the Partnership that the Partnership would be carrying on a trade. Nevertheless, his evidence was that the investment strategy adopted by the Partnership 'always was a very short-term strategy anyway, so it folded very neatly into a view that it should be trading'. He went on to say: 'from our perspective, I mentioned it before, and I'll say it again, the trading aspects of this, in my mind, were never in doubt … there was never any doubt in my mind that this was a proper trading strategy with a proper commercial purpose'.

64. Mr Derricott became a partner in certain of the limited partnerships on the basis, as he said, that he 'understood the trading strategy' and that if it delivered a tax result, that was a bonus as far as he was concerned. When pressed, he said that he hoped to receive a tax loss.

65. Mr Derricott said that the terms 'investment adviser' and 'trading adviser' were used interchangeably in the agreement under which Curzon was appointed investment adviser to the Partnership. Although he acknowledged, in answering Mr Goy's questions, that an investor could invest in short dated gilts, his evidence was that 'in my world, in my definition, if I'm buying a whole series of – contiguous series of short dated investments over a period, I wouldn't describe that as investing, because it

isn't. It's a trading yield curve.' He said that it was a strategy commonly adopted in the market.

66. Mr Derricott said that Curzon did not suggest the trading strategy adopted by the Partnership – it had probably been suggested by Mercury or Hambros, but Curzon endorsed the strategy because they thought commercially it was a sound strategy. From the evidence we find that in practice, Curzon made recommendations and orders in generic terms and left it to Hambros to decide precisely what acquisitions would be made. Mr Derricott explained this by saying that Hambros required to check whether what was to be purchased would provide adequate security for their loans. When an acquisition of equity dividend rights was suggested by Curzon, Mr Derricott said that had been 'just speculation as to what might be purchased' because it was not possible to buy such rights in the market at the time.

67. Mr Derricott accepted that the first acquisition made by the Partnership, on 27 March 2006, had to be in paper that would mature before the purchase of dividend rights, because the proceeds of that redemption on maturity were needed to be reinvested in the purchase of dividend rights. Mr Goy put to Mr Derricott that the timing of that first acquisition and the timing of the redemption were dictated by tax, in that it was advantageous to the Partnership to be able to demonstrate that it had started trading before the dividend purchase. Mr Derricott disclaimed any knowledge of whether such tax motivations had been behind that purchase.

68. Mr Goy pointed out that the Partnership's fund was wholly in cash at the end of 18 May 2006 or the beginning of 19 May 2006, which Mr Derricott accepted. He denied, however, that this had been intentional.

69. Mr Derricott accepted that the return made from the stocks acquired was 'totally predictable' and that he understood that the purchase of the Helios dividend rights was intended to produce a tax loss of about £60 million. He accepted that in the context of the intended tax loss, the profit of £42,000 on the payment of the dividend to the Partnership by Helios was insignificant and that in the context of the Partnership's trading strategy the acquisition of the dividend rights was 'extraordinary', in the sense of not being ordinary. Mr Derricott had learned of the proposal to acquire the rights to the interim dividends to be paid by Helios a day or two before the meeting on 30 March 2006 where the acquisition was discussed. He, and Curzon, had known in general terms that it was proposed to acquire dividend rights, but did not know until that late stage of the details. The acquisition opportunity was introduced to Curzon by a Mr Joe Dickens of Mercury Ventures Ireland (an associate of Mercury). Curzon advised on the merits of the minimum yield of the dividends in comparison with the rate specified in the Partnership's find trading strategy.

70. Mr Goy put to Mr Derricott that following Pirouet's acquisition of the limited partners' interests in the Partnership on 19 May 2006, the scale of the Partnership's activity was radically diminished, and asked if he had enquired the reason for this. He said that he had not. Mr Goy put it to Mr Derricott that Curzon would have been concerned about the withdrawal of £60 million from the Partnership by Pirouet

because it would have minimised Curzon’s ability to make a profit itself (which was an annual fee of 0.25% of partners’ total capital contributions remaining in the Partnership at the start of any accounting period, subject to a minimum fee of £10,000). Mr Derricott’s response was that Curzon was not concerned by this development because they had been very grateful for any fees that came their way.

71. Mr Fitton’s evidence was that in his expert opinion the Partnership had adopted a valid trading strategy. He suggested that the Partnership had not been investing, simply because it knew the outcome of each deal on acquisition. Another factor pointing to trading in the Partnership’s case was the short-term nature of the assets acquired. He considered the Partnership had carried out the practice of “scalping” or “high frequency trading”, which is very common in financial markets where traders deliberately take very short-term positions for very small amounts of profit, but do so with great frequency.

72. Mr Fitton accepted, in cross-examination, that buying short-dated stocks before redemption is a strategy capable of being adopted by either a trader or an investor. The return (excluding tax considerations) is the same from this type of transaction as it would be from an interest-bearing deposit of cash at the acquisition date, equal to the acquisition cost.

Conclusions from the evidence of the witnesses

73. We find from the evidence of both witnesses that, so far as the perception of persons participating in the relevant markets is concerned, the activities undertaken in the market by the Partnership could be recognised as a trade.

74. From Mr Derricott’s evidence we find that Curzon’s rôle in the Partnership’s activities was not in substance that of investment advisor because the advice as to which acquisitions the Partnership made was in reality given by Hambros and/or Mercury. Curzon took responsibility for issuing the Information Memorandum and for confirming that the proposed acquisitions conformed to the ‘trading strategy’ adopted by the Partnership, but did nothing more of substance in return for their (quite modest) fees. This explains the lack of reaction the part of Curzon when Pirouet withdrew £60 million from the Fund immediately after it purchased the limited partners’ interests. It also explains the fact that Mr Derricott learned the details of the acquisition of the Helios dividend rights so late in the day and his vagueness as to the detail of the tax planning which he knew was an objective of the arrangements.

Issue 1: *Was the Partnership carrying on a trade in the accounting period ending 5 April 2006? The parties’ submissions.*

75. Mr Thornhill QC submitted that the wide ambit of the meaning of ‘trade’ for relevant tax purposes, that it includes ‘every trade, manufacture, adventure or concern in the nature of trade’ (section 832(1), ICTA) well covered the Partnership’s activities. He cited *Lewis Emanuel & Son Ltd v White* (1965) 42 TC 369 and *Cooper v Clark* [1982] STC 335. Those cases establish that whether a given state of affairs does or does not amount to a trade is a question of fact and degree, in relation to which there is a ‘no man’s land’ between the two extremes of cases where as a matter

of law there is a trade and those where as a matter of law there is not a trade, in which the fact finding tribunal must evaluate the evidence.

76. Mr Thornhill emphasised in his submissions the authority of the decision of the Court of Session in *IRC v Livingston* (1926) 11 TC 538, and especially the statement, which he called one of principle, of the Lord President (Clyde) at *ibid.* p.542, which was cited by Lord Morris in *Ransom v Higgs* [1974] STC 539 at 550/1:

> 'I think the test, which must be used to determine whether a [venture of a complex character] is, or is not, "in the nature of trade" is whether the operations involved in it are of the same kind, and carried on in the same way, as those which are characteristic of ordinary trading in the line of business in which the venture was made.'

77. Mr Thornhill relied on the evidence of Mr Derricott and Mr Fitton to show that the operations carried on by the Partnership were trading operations carried on in the same way as ordinary trading in short-dated stocks on the market. He pointed to the evidence that the Partnership has carried out its business in an organised and systematic manner, securing specialist advice as to the financial markets, its overall strategy and particular transactions from Curzon and embarking on a course of dealing in which it entered into a number of transactions in financial instruments employing very substantial sums of money in doing so. He submitted that the securities acquired by the Partnership were not acquired so that income might be obtained from them. They were acquired in order to make a profit from the disposal of them.

78. Mr Thornhill referred to the terms of the Information Memorandum stating that it was intended that the Partnership should make a profit 'other than by means of investment'.

79. Mr Thornhill acknowledged that the arrangements whereby the Partnership acquired the Helios dividend rights and received the dividends were artificial, but he submitted that that was irrelevant to the Tribunal's assessment of whether the activities of the Partnership (taken as a whole) amounted to trading. He pointed to the profit made by the Partnership by holding the stocks acquired to maturity (or in one case selling them before maturity), reminding us that the tax loss claimed was an artificial product of the application of section 730 ICTA.

80. Mr Thornhill referred to *FA and AB Ltd v Lupton* [1972] AC 634 and sought to distinguish this appeal from *Lupton* in submitting that in *Lupton* the whole transaction under review had been 'shot through' with tax considerations. He submitted that in this case even the consideration for the acquisition of the Helios dividend rights owed nothing to tax considerations, but was calculated on a commercial basis. The tax advantage sought, he submitted, was entirely based on the wording and intendment of section 730 ICTA and had nothing to do with the manipulation of any transactions undertaken by the Partnership in the course of its trade of dealing in short-term securities.

81. Mr Goy submitted that the transactions which the Partnership contended were trading were in reality merely a “wrapper” in which the arrangements involving the Helios dividends would take place – a device necessary if the tax avoidance scheme was to work.

82. He referred us to the decision of the Court of Appeal in *Eclipse Film Partners No. 35 LLP v Commissioners for HMRC* [2015] EWCA Civ 95. In that decision (*ibid.* at [123]), the Court said that ‘[t]he proper characterisation of the business of Eclipse 35 depends on the totality of its activity and enterprise’. He submitted that, in a case where marketable securities are dealt with, there is a problem in determining whether the activity amounts to a trade, in that securities are commonly the subject matter of investment, and therefore the distinction between trading and investing in securities can be difficult. Citing *Clarke v British Telecom Pension Scheme* [2000] STC 222 (per Robert Walker LJ) he submitted that frequency of transactions and organisation cannot be determinative in making this distinction.

83. Mr Goy submitted that we should find that the Appellant was investing, not trading, in short-dated securities. He pointed to the evidence that the investments involved minimal risk, particularly, he suggested, because SGHCI was concerned not to imperil its security. He also referred to the evidence that there was no significant speculative element in what the Partnership did, the stocks acquired being, with one exception, held to maturity. He submitted that by holding assets to redemption, there was no dealing with such assets by the Partnership, nor were there customers with whom the Partnership dealt. He pointed out that the return on the investments made by the Partnership were in the order of that which could have been made by simply depositing money at interest with a bank. He submitted that the number and frequency of the transactions entered into by the Partnership and the manner of investment was not such as to indicate that the Partnership was trading. He summed up his submissions on this issue by saying that the arrangements entered into by the Partnership lacked commercial purpose, being tax avoidance arrangements from start to finish. He supported this submission by referring to the fact that the loan to the limited partners by SGHCI was made on 23 March 2006 for a maximum of 60 days, he referred to the evidence that a third-party purchase of the limited partners’ interests was envisaged from the outset and in fact took place on 19 May 2006, when every limited partner sold his/her interest at a total loss of the investment not funded by way of loan from SGHCI. He added that the third-party purchaser, Pirouet, was associated with Mercury, the deviser of the scheme.

84. Mr Goy referred to the Partnership’s results for the period to 5 April 2006. Commercially computed losses of £907,828 were reported – to a large extent reflecting the tax advisory fee of £761,363 paid to Mercury. Although a profit was reported in the year to 5 April 2007, there was a loss in the following year, and, taking all three years together, the Partnership was loss-making. Having regard to the predictable yield from the investments, it is reasonable, in Mr Goy’s submission, to conclude that it would have been apparent from the inception of the Partnership’s activities that such activities would not be profitable.

Issue 1: *Discussion*

85. It was accepted by Mr Thornhill for the Partnership, and we find, that the transactions involving the acquisition of the Helios dividend rights at the heart of this appeal, and the payment of the dividends to which the rights had been acquired, were artificial. Mr Derricott described them as 'extraordinary'. Although it is the fact that these arrangements were planned to take place as part of the series of transactions entered into by the Partnership, we have concluded that this fact is not, of itself, determinative of the question of whether the transactions entered into by the Partnership (taken as a whole) were or were not trading transactions. It is, however, relevant to our determination of that question.

86. As the Court of Appeal noted in *Eclipse* (*ibid.* at [117]), citing Lord Templeman in *Ensign Tankers (Leasing) Ltd v Stokes* [1992] 1 AC 655, 677 (and as Mr Goy accepted in argument), 'it is elementary that the mere fact that a taxpayer enters into a transaction or conducts some other activity with a view to obtaining a tax advantage is not itself determinative of whether the taxpayer is carrying on a trade'.

87. The task of the Tribunal is to assess the effect of what the Partnership has in fact done (see: per Lord Morris in *Ransom v Higgs* (*ibid.*) at p.550 c/d). If the taxpayer's acts are equivocal, as to the question of whether a trade, as opposed to an investment activity, is being carried on, then the taxpayer's subjective purpose 'may be a very material factor when weighing the total effect of all the circumstances' (per Lord Reid in *Iswera v Commissioners of Inland Revenue* [1965] 1 WLR 663 at 668). Trading requires an intention to trade and, as Lord Wilberforce said in *Simmons (as liquidator of Lionel Simmons Properties Ltd) v Inland Revenue Commissioners* [1980] STC 350 at 352 f/g, 'normally the question be asked is whether this intention existed at the time of the acquisition of the asset. Was it acquired with the intention of disposing of it at a profit, or was it acquired as a permanent investment?'

88. Were the Partnership's acts equivocal as to the question of whether it was carrying on a trade, as opposed to an investment activity? The acquisitions of stocks (other than the acquisition of the Helios dividend rights) were, we find, acquisitions in the market from wholly unconnected parties on commercial terms. As stated above, we find from the evidence of Mr Derricott and Mr Fitton that, so far as the perception of persons participating in the relevant markets is concerned, the activities undertaken in the market by the Partnership (which would exclude the acquisition of the Helios dividend rights and the receipt of the Helios dividends) were such as could be recognised as a trade. Applying the *Livingston* test, the activities of the Partnership in the market were of the same kind, and carried on in the same way, as those which are characteristic of ordinary trading in short-dated securities – but we add the qualification that we must take into account the fact that, inserted into the activities in the market, were the wholly artificial transactions involving the Helios dividends. We consider that we should not simply conclude that the Partnership's acts unequivocally demonstrated that it was trading by an application of the *Livingston* test.

89. The factors referred to by Mr Goy – minimal risk, no significant speculative element, holding assets to redemption so that there was no significant dealing with them, comparable return to bank interest, number and frequency and manner of

investment – seem to us not to be determinative either way, because they are consistent both with trading and with investment activity.

90. On consideration of all the evidence and the facts found, we consider that the Partnership's acts are equivocal as to the question of whether it was carrying on a trade, as opposed to an investment activity, in relation to its acquisitions in the market.

91. This brings the Partnership's subjective intention into play and we find that this, as demonstrated by Recital A of the Limited Partnership Agreement and the Information Memorandum, was to make a profit 'other than by means of investment' – which we take to mean by trading. While we do not regard the involvement of Curzon as indicative of trading as opposed to investment, we do take account of the fact that the stocks acquired were acquired in order to be disposed of at a profit rather than as a source of investment income.

92. Our decision on this issue is that the Partnership was carrying on a trade of dealing in short-dated securities in the accounting period ending 5 April 2006.

Issue 2: *Were the particular transactions claimed to produce the loss (namely the transactions by which the Partnership arranged to receive the dividends from Helios) trading transactions? The submissions of the parties.*

93. Mr Goy, for HMRC, submits that if, contrary to his submissions on Issue 1, we find that the Partnership carried on a trade of dealing in short-dated securities, the transactions by which the Partnership arranged to receive the dividends from Helios were not transactions entered into in the course of that trade or any trade.

94. Mr Thornhill, for the Partnership, submits that the transactions involving the Helios dividends were of the same character as the other transactions into which the Partnership entered and were trading transactions, for the same reasons as relate to those other transactions. Furthermore they were trading transactions undertaken in the course of the Partnership's trade of dealing in short-dated securities.

95. Mr Thornhill's argument is that a tax avoidance motive does not alter or transform the essential nature of a transaction and that the essential nature of the Partnership's transactions involving the Helios dividends – viz: the acquisition of the rights to the dividends and the receipt of the dividends when paid out by Helios – demonstrated that they were trading transactions, for the same reasons as the other transactions in short-dated securities carried out by the Partnership were trading transactions. In support of this submission, Mr Thornhill cited *Bupa Insurance Ltd v Revenue and Customs Commissioners* [2014] UKUT 262 (TCC), [2014] STC 2615 at [69], where the Upper Tribunal (Asplin J and Judge Ghosh QC) rejected a submission advanced by HMRC on the basis of the '*Ramsay*' principle (see: below) that transactions effected solely for tax avoidance purposes are properly to be disregarded for that reason alone, in construing tax statutes purposively.

96. Mr Thornhill also cited Lord Templeman's speech in *Ensign Tankers* (*ibid.* at p.742) in which he rejected the proposition that a finding of fact that the sole object of

a transaction was fiscal advantage could only lead to one conclusion – viz that it was not a trading transaction. He reminded us that Lord Templeman's speech was followed by the Court of Appeal in *New Angel Court Ltd v Adam (HMIT)* [2004] STC 779 – see: [89].

97. He submitted, as noted above, that in *Lupton* the whole transaction under review had been 'shot through' with tax considerations, but that in this case even the consideration for the acquisition of the Helios dividend rights owed nothing to tax considerations, but was calculated on a commercial basis. The tax advantage sought, he submitted, was entirely based on the wording and intendment of section 730 ICTA and had nothing to do with the manipulation of any transactions undertaken by the Partnership in the course of its trade of dealing in short-term securities.

98. Mr Goy submitted that the transactions by which the Partnership arranged to receive the Helios dividends were very different from other transactions entered into by the Partnership. In particular, those other transactions involved unconnected third parties being the vendors of the debt obligations and the debtors under the debt obligations. The profit made on each of those other transactions was dictated by purchase prices fixed by the market. But the position regarding the purchase of the rights to the Helios dividends was fundamentally different. These were not transactions effected on any public market. The ability of Helios to pay out the dividends had been artificially brought about by Dickens making a contribution to Helios of the funds loaned by Schroders – artificial in the sense that it had no commercial rationale beyond facilitating the tax avoidance scheme. The profit of £42,000 apparently made by the Partnership when the Helios dividends were paid to it was there merely to give the whole transaction 'a faint air of commercial verisimilitude' (per Lord Templeman in *Coates v Arndale Properties Limited* [1984] STC 637 at 639). That profit had in fact been funded by the limited partners by way of fees paid to Mercury by the Partnership, which in turn had been passed on by Mercury to Dickens, in one case via Westall.

99. Mr Goy cited *Lupton* for the proposition that 'some transactions may be so affected or inspired by fiscal considerations that the shape and character of the transaction is no longer that of a trading transaction' (see: per Lord Morris, *ibid.* at p.647G).

100.Mr Goy also advanced an argument based on the '*Ramsay*' principle (*W T Ramsay Ltd v IRC* [1981] STC 174) to the effect that viewed realistically, the facts including the sale by Dickens to the Partnership of the rights to receive the Helios interim dividends and the payment of those dividends by Helios to the Partnership were a single composite transaction – and we have so found (see: above [56]).

Issue 2: *Discussion*

101. Although the thrust of Mr Goy's argument based on the '*Ramsay*' principle was directed at his case on Issue 3 (whether section 730 ICTA has the effect claimed by the Partnership), we consider it is relevant to this Issue (2), because a single composite transaction involving both the purchase of rights to dividends and the

payments of those dividends pursuant to those rights cannot, in our judgment, be regarded as a trading transaction.

102.To the same, or similar, effect, we have concluded that the principle in *Lupton* does indeed cover this case. In *Lupton*, it was acknowledged that the taxpayer was at all relevant times trading as a dealer in stocks and shares (*ibid.* p.643G/H). The question which arose in *Lupton* was originally whether five particular transactions entered into by the taxpayer were transactions carried out in the course of its trade. By the time that the appeal reached the House of Lords only one of the transactions remained in issue, and their decision dealt with that one transaction. Lord Morris, giving the leading speech, was at pains to reject the proposition that the presence of a motive of securing tax recovery caused a trading transaction to cease to be such. However, he drew a distinction between trading transactions motivated by an intention to secure a tax advantage (as we consider the other transactions in short-dated securities in this case to have been) and transactions 'so affected or inspired by fiscal considerations that [their shape and character] is no longer that of a trading transaction' (*ibid.* p.647G). Lord Guest, agreeing with Lord Morris, said that the shares in *Lupton* 'were not bought as stock in trade of a dealer in shares but as pieces of machinery with which a dividend-stripping operation might be carried out' (*ibid.* p.651D). Lord Simon, to similar effect, said that 'what is in reality merely a device to secure a fiscal advantage will not become part of a trade of dealing in shares just because it is given the trappings normally associated with share-dealing within the trade of dealing in shares (*ibid.* p.660C).

103.In our judgment, these dicta apply to the transactions by which the Partnership acquired the rights to the Helios dividends from Dickens and subsequently received the dividends pursuant to those rights. These were not trading transactions carried out with a tax avoidance motive – they were not trading transactions at all, but artificial arrangements entered into in order to enable the Partnership to claim a tax loss pursuant to its interpretation of section 730 ICTA. This is, in our view, cogently demonstrated by the fact that the delay in purchasing the dividend rights, from 31 March 2006 to 3 April 2006, had no effect at all on the purchase price (despite reducing from 6 days to 3 days the period before payment of the dividends). The fact that the sought for tax advantage originates in a particular interpretation of section 730 ICTA rather than from the intrinsic properties of the transactions themselves is, in our view, entirely beside the point. We consider that nothing in *Ensign Tankers* or *New Angel Court* precludes us from deciding (as we do, disposing of this Issue (2)) that the transactions concerned were not trading transactions at all.

Issue 3: *Does section 730 ICTA have the effect claimed by the Partnership? The parties' submissions*

104.Section 730 ICTA provides, so far as material, as follows:

'730 Transfers of rights to receive distributions in respect of shares

> (1) Where in any chargeable period the owner of any shares ("the owner") sells or transfers the right to receive any distributions payable (whether before or after the sale or transfer) in respect of the shares without selling

or transferring the shares, then, for all the purposes of the Tax Acts, that distribution, whether it would or would not be chargeable to tax apart from the provisions of this section –

> (a) shall be treated as the income of the owner or, in a case where the owner is not the beneficial owner of the shares and some other person ("a beneficiary") is beneficially entitled to the income arising from the shares, the income of the beneficiary, and
>
> (b) shall be treated as the income of the owner or beneficiary for that chargeable period, and
>
> (c) …'

105. By section 39 and paragraph 2 of Schedule 7, Finance (No. 2) Act 2005 ("F(2)A 2005"), the former subsection (1)(c) of section 730 ICTA was repealed. Before its repeal, section 730(1)(c) provided that a distribution within section 730(1) "shall not be deemed to be the income of any other person". That is, a distribution within section 730 ICTA was to be treated as the income of the owner of the shares concerned (or the beneficial owner of them) for the chargeable period in which the right to receive it was transferred *and was not to be deemed the income of any other person*. The amendment of section 730 ICTA by F(2)A 2005 had effect in relation to sales or transfers on or after 2 December 2004.

106. Mr Thornhill, for the Partnership, submits that the conditions for section 730(1) ICTA to apply are fulfilled in relation to the Helios dividends. We understood this to be agreed as a matter of language by HMRC. In particular, Mr Mowschenson's advice that the payments Helios resolved to make constituted a dividend or distribution as a matter of the law of the Cayman Islands, is accepted by HMRC.

107. Mr Thornhill submits that section 730 ICTA was originally introduced (by section 24 of the Finance Act 1938) to reverse the decision of the Court of Appeal in *Paget v Commissioners of Inland Revenue* 21 TC 677 (that where coupons for interest payable on bonds were sold, the purchase price received was not assessable as income on the seller) and, where section 730 ICTA applies to treat a distribution as the income of the owner of shares (Dickens), it follows that the distribution cannot be treated as the income of the purchaser or transferee of the right to receive it (the Partnership). In support, he cites the well-known passage from the judgment of Peter Gibson J, sitting in the Court of Appeal in *Marshall (HMIT) v Kerr* [1993] STC 360 at 366, as follows:

> 'I take the correct approach in construing a deeming provision to be to give the words used their ordinary and natural meaning, consistent so far as possible with the policy of the Act and the purposes of the provisions so far as such policy and purposes can be ascertained; but if such construction would lead to injustice or absurdity, the application of the statutory fiction should be limited to the extent needed to avoid such injustice or absurdity, unless such application would clearly be within the purposes of the fiction. I further bear in mind that because one must treat as real that which is only deemed to be so, one must treat

as real the consequences and incidents inevitably flowing from or accompanying that deemed state of affairs, unless prohibited from doing so.'

108.This passage was approved in the House of Lords by Lord Browne-Wilkinson (see: [1995] 1 AC 148 (HL) 164-5).

109.Mr Thornhill submitted that a consequence, inevitably flowing from the deemed state of affairs that the distribution was the income of Dickens, is that the distribution cannot also be the income of the Partnership. To hold otherwise would be to permit double taxation, against which there is a presumption of high authority – see: per Lord Wilberforce in *IRC v Garvin* [1981] STC 344 at 350 and *Vestey v IRC* [1980] AC 1148 (HL) at 1173.

110.Mr Thornhill submitted that following his submission that the transactions by which the Partnership arranged to receive the Helios dividends were transactions carried out in the course of its trade (a submission we have rejected) together with his submission that the dividends cannot be regarded as the income of the Partnership by reason of the application of section 730 ICTA, the result is that the Partnership's tax computations are required to be prepared on the basis that the dividends are not the income of the Partnership. This gives the Partnership the trading loss which it has claimed.

111.Mr Thornhill addresses the amendment of section 730(1) by the F(2)A 2005 in removing the former section 730(1)(c) as follows. He submits that section 730(1) must be construed as it stands with the results he contends for. He also submits that the effect of the repealed section 730(1)(c) was to prevent any other deeming provision having effect, and so its removal is irrelevant to the present appeal, where there is no other (competing) deeming provision at play.

112.Mr Goy submitted that the section 730 ICTA does not have the effect claimed by the Partnership. He contended that that provision operates to attribute the distribution to the owner of the shares – it does not affect the position of the purchaser/transferee. He cited *R v Dimsey* [2001] STC 1520, where Lord Scott (giving the leading speech with which the others of their Lordships agreed) construed the deeming provision in section 739(2) ICTA as referring only to the position of the transferor of assets, to whom the deeming provision attributed the income in question.

113.Lord Scott referred to the passage in *Marshall v Kerr* relied on in this appeal by the Partnership and said that the legislative history of section 739, the other provisions in Chapter III of Part XVII of ICTA, the comparison of section 739(2) with other tax avoidance provisions and the tax avoidance purpose of section 739, persuaded him that the court should not, in that case, treat as real the consequences that would follow from the deemed state of affairs if that deemed state of affairs were real (*ibid.* [40] and [41]).

114.Mr Goy submitted that the amendment of section 730(1) by the F(2)A 2005 removed the rule that had previously applied, that where income of a transferee was deemed to be income of the transferor it could not also be regarded as the income of the transferee. He accepted in argument that if section 730(1)(c) were in force for the period relevant to this appeal, then section 730 ICTA would indeed have the effect claimed for it by the Partnership. But he said that Parliament, in repealing section 730(1)(c) had clearly intended to introduce a possibility that income deemed to be the income of person A under section 730(1)(a) could also be the income of person B if it could otherwise be attributed to person B. HMRC had stated in a commentary on the Finance Bill 2005 that the amendment 'removes the non-application of any tax charge on the recipient of the actual distribution'.

115. Mr Goy referred us to [47] to [49 of *R v Dimsey*, where Lord Scott makes explicit reference to section 730 ICTA before its amendment by F(2)A 2005. He submitted that it was clear from what Lord Scott said that he regarded the omission of any words, such as those formerly found in section 730(1)(c), from section 739 made it 'very difficult, if not impossible, to argue that those words, or something similar' should be an implied addition to section 739. So here, the removal of section 730(1)(c) showed, in Mr Goy's submission, a clear Parliamentary intention that there should be no consequence from section 730 for the tax liability of persons other the person at whom the deeming provision is principally aimed (*ibid.* [50]).

116.In *R v Dimsey*, Lord Scott did not consider that 'the double taxation possibilities that the Revenue's case undoubtedly leaves theoretically open' carried much weight in considering the correct construction of section 739(2) ICTA (*ibid.* [58]). Mr Goy argued that we should not be dissuaded from the construction of section 730 for which HMRC contended by the theoretical possibility that it might (in other cases) lead to double taxation. He pointed out that it would not lead to Dickens (as seller of the dividend rights) being subject to tax on the dividend income (section 399, Income Tax (Trading and Other Income) Act 2005) and that in other cases the possibility of double taxation is more theoretical than real. He submitted that it was relevant that section 730 ICTA was designed to combat tax avoidance, so that it was likely that, as a practical matter, tax avoiders would not enter into transactions caught by section 730 if double taxation were possible – which it was not in this case.

117.Mr Goy countered Mr Thornhill's argument that section 730(1)(c) was intended only to prevent any other deeming provision having effect by submitting that, in that case, Parliament must have gone to the trouble of expressly precluding the income being treated as that of a third person, but, as regards the position of the actual recipient of the income, was prepared to leave matters to be dealt with as a matter of inference. He submitted that that was highly improbable and that we should interpret the word 'deemed' in section 730(1)(c) as meaning little more that 'treated' or considered'.

118.Mr Goy also prayed in aid his argument based on the '*Ramsay*' principle, that there was not here, as a matter of a purposive construction of section 730 ICTA, any sale or transfer of the right to receive any distributions payable in respect of the Helios shares, or, in other words, the transactions relied on by the Partnership in this case are not real transactions having commercial effect, but are both contrived and circular in nature. He submitted that we should assume that Parliament only intended section 730 ICTA to apply to real transactions having commercial effect.

Issue 3: *Discussion*

119. We accept Mr Goy's submissions and hold that section 730 ICTA does not have the effect for which the Partnership contends.

120. We point out the qualifications made by Peter Gibson J in the passage from *Marshall v Kerr* on which Mr Thornhill's argument rests. Peter Gibson J said that, in construing a deeming provision, the words must be taken to have their ordinary and natural meaning *consistent so far with the policy of the Act and the purposes of the provisions so far as such policy and purposes can be ascertained.* Those emphasised words must, in our judgment, be taken to be a qualification also to the general proposition stated by the judge that one must treat as real the consequences and incidents inevitably flowing from or accompanying the deemed state of affairs.

121. We consider that the policy and purposes of section 730 ICTA can be ascertained to be the prevention of tax avoidance by the transfer of the right to distributions from shares without the transfer of the shares themselves. What the Partnership has endeavoured to do in this case is to use that provision, intended to prevent tax avoidance, as an engine of tax avoidance. This seems to us to be so far from the evident purpose of section 730 that we can confidently apply the dictum from *Marshall v Kerr* in this case by holding that section 730 ICTA does not have the effect of relieving the Partnership from taxation on the Helios dividends.

122. However, our decision does not rest on this consideration alone. In accepting Mr Goy's submissions, we consider that the amendment of section 730 ICTA by the removal of the former section 730(1)(c) clearly had the effect for which he contended, namely that it removed the provision by which there was a prohibition on treating the distribution as the income of any person other than the owner of the shares. We regard Mr Thornhill's argument that the repeal of section 730(1)(c) had the effect only of allowing the income to be 'deemed' to be the income of another person (in addition to the owner of the shares) – as opposed to allowing it to be treated as the income of any other person – as being, with respect, far-fetched. We can discern no statutory purpose for an amendment having such a limited effect.

123. As already indicated, we also accept Mr Goy's argument based on the '*Ramsay*' principle. In the passage in this Decision headed 'the money flows' we have explained that the relevant transactions consisted of three interlocking circular money flows, with the result that the lenders (Schroders and SGHCI) lent funds and recovered them with interest, while retaining control over their funds in the meanwhile by security provisions. The other money introduced to these arrangements consisted of the contributions privately raised by the limited partners, which were all lost, because they were required to fund the costs of the scheme.

124. We regard it as wholly unrealistic in these circumstances to regard there as having been any real sale of the right to receive the Helios dividends by Dickens to the Partnership within the meaning of section 730(1) ICTA.

125. Since the hearing, we have noticed the judgment of the Supreme Court in *UBS AG v Commissioners for HMRC* and *DB Group Services (UK) Ltd v Commissioners for*

HMRC [2016] UKSC 13. In allowing the appeal of HMRC in that case, Lord Reed (with whom the others of their Lordships agreed) made some important comments of general application to the interpretation of provisions providing for exemption from tax. (Although section 730 ICTA is an anti-avoidance provision, the Partnership claims that it should be applied to provide it with an exemption from tax.)

126. Lord Reed said that the provision under review in that case (Chapter 2 of Part 7 of the Income Tax (Earnings and Pensions) Act 2003 ("ITEPA")) 'was introduced partly for the purpose of forestalling tax avoidance schemes' and that that 'self-evidently makes it difficult to attribute to Parliament an intention that it should apply to schemes which were carefully crafted to fall within its scope, purely for the purposes of tax avoidance' (*ibid.* [77]).

127. With regard to the application of section 423(2) ITEPA, Lord Reed also said that '[t]he context was one of real-world transactions having a business or commercial purpose. There is nothing in the background to suggest that Parliament intended that section 423(2) should also apply to transactions having no connection to the real world of business, where a restrictive condition was deliberately contrived with no business or commercial purpose but solely in order to take advantage of the exemption' (*ibid.* [78]).

128. In our judgment, these authoritative comments are of general application to the construction of tax legislation where (as in this appeal) avoidance of tax is sought to be achieved by the use of a provision apparently providing for a tax exemption, by its application to 'transactions having no connection to the real world of business' such as we find the transactions by which the Partnership arranged to receive the Helios dividends to have been.

129. For the reasons given, we hold that section 730 ICTA does not have the effect claimed by the Partnership, but should be interpreted in accordance with HMRC's submissions.

Issue 4: *On the basis that the Partnership was trading, were the fees in respect of tax advice paid to Mercury deductible in computing the profit/loss of the trade? The parties' submissions*

130. In his Skeleton Argument, Mr Thornhill submitted that the tax advisory fees paid to Mercury of £761,363 were wholly and exclusively incurred for the purposes of the Partnership's trade, and so were deductible in computing its profits. The comment was made that, as the Information Memorandum records, Mercury were the Partnership's tax advisers and that there was therefore nothing surprising or unusual in the Partnership making these payments to Mercury.

131. However, in argument, Mr Thornhill accepted that if the transactions by which the Partnership purchased the rights to the Helios dividends and received the dividends themselves were not transactions carried out in the course of the Partnership's trade of dealing in short-dated securities, then he conceded that the tax advisory fees paid to Mercury were not deductible as a trading expense.

132.Mr Goy also submitted that if the arrangements relating to the scheme dividends were not trading transactions entered into the course of the Partnership's trade of dealing in short-dated securities, then likewise fees paid to facilitate the payment of the dividends and the repayment of the debt due from the Partnership to Schroders are not properly to be treated as a deductible expense.

Issue 4: *Discussion*

133.We have decided that the transactions by which the Partnership acquired the rights to the Helios dividends from Dickens and subsequently received those dividends pursuant to those rights were not trading transactions at all – see: above [103] – our decision on Issue 2. It follows in our judgment, and as the parties apparently agree, that the fees of £761,363 paid to Mercury were not deductible for tax purposes as trading expenses.

Disposition

134.For the reasons given above, the appeal is dismissed.

135.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.

JOHN WALTERS QC
TRIBUNAL JUDGE

RELEASE DATE: 18 APRIL 2016