Tolley's

Tax Digest

Issue 81 • July 2009

Containing practical, expert guidance on:

- The definition of a "Transaction in Securities"
- The "*bona fide* commercial" test
- The four Circumstances
- What is tax avoidance?
- Clearances
- Appeals to the new unified Tribunals

Transactions in Securities

Pete Miller
CTA (Fellow)
Partner, Powrie Appleby LLP

Tolley's Tax Digest

To subscribe call
0845 370 1234

LexisNexis® Tolley

www.lexisnexis.co.uk

Tax Digest Issue 81 Cover.pmd 1 22/07/2009, 12:01

Contents

Introduction 1
History and scope 2
Background 2.1
History 2.2
Scope of legislation 2.3
Application to capital gain avoidance 2.4
Interaction with other taxes 2.5
Current legislative references 2.6
Interpretation 3
Structure 4
Counteraction 4.1
Conditions 4.2
Escape clause 4.3
The conditions: 'tax advantage' 5
What is a 'tax advantage' 5.1
Avoidance or reduction of a charge to tax 5.2
Relief or increased relief from tax 5.3
The conditions: 'in consequence of' 6
The conditions: 'transactions in securities' 7
'Transaction in securities' 7.1
Company liquidation 7.2
Payment of a dividend 7.3
The circumstances 8
Circumstance A (TA 1988 s 704A/ITA 2007 s 686 8.1
Abnormal amount by way of dividend 8.2
Circumstance C (TA 1988 s 704C/ITA 2007 s 688 8.3
Circumstance D (TA 1988 s 704D/ITA 2007 s 689 8.4
Circumstance E (TA 1988 s 704E/ITA 2007 s 690 8.5
Escape clauses 9
Bona fide commercial reasons 9.1
Ordinary cause of making and managing investments 9.2
Tax avoidance motive 9.3
Whose intentions 9.4
Clearances 10
Form and content of the application 10.1
Disclosure 10.2
Meaning of a clearance 10.3
Administration of clearances 10.4
Timing 10.5
Urgent applications 10.6
Refusal of clearance 10.7
Information powers 11
Counteraction 12
New Tribunal system 12.1
Preliminary notification 12.2
The statutory notification 12.3
Submission to the Tribunal 12.4
Formal notice of counteraction 12.5
Appeals 13
Internal review 13.1
Appeal to the First-Tier Tribunal (Tax Chamber) 13.2
Appeal to the Upper Tribunal (Finance and Tax Chamber) 13.3
Appeal to the Court of Appeal and the House of Lords (or Supreme Court) 13.4
Scotland and Northern Ireland 13.5
The future of the legislation 14

Author

Pete Miller

Pete Miller is a partner with Powrie Appleby, a specialist tax firm based in Leicester but with a nationwide reach. He has more than 21 years experience in tax, having started with the Inland Revenue in 1988. After training as an inspector, Pete spent some years in Policy Division, advising Ministers on Capital Allowances policy and on the taxation of the film industry, with particular reference to ensuring that the UK was a favourable location for making big budget movies. Pete then moved on to take up a role in Technical Division (Company Distributions). Here Pete was part of a team responsible for the Revenue's technical analyses of corporate distributions, a role that included being responsible for demerger clearances and for some of the major corporate reconstruction projects of the period.

Since leaving the Revenue in 1997, Pete worked for 11 years in 'Big 4' firms and specialised in a number of areas, including reorganisations and reconstructions, the substantial shareholdings exemption, and the taxation of M&A transactions and of intangible assets.

Pete is a regular contributor to books and journals, including *Taxation*, *The Tax Journal* and *Simon's Direct Tax Service* (he is a member of the Editorial Boards of *The Tax Journal* and *Simon's*). He is co-author, with George Hardy, of *Taxation of Company Reorganisations* (Tottel Publishing, 2nd edition, January 2009).

Tolley's Tax Digest is produced and published by LexisNexis.

Views expressed in this Digest are the author's and are not necessarily those of the author's firm or of the publisher.

No responsibility for loss occasioned to any person acting or refraining from action as a result of the material in this Digest can be accepted by the author or publishers.

© Reed Elsevier (UK) Ltd 2009

Crown copyright material is reproduced with the permission of the Controller of HMSO and the Queen's Printer for Scotland. Any European material in this work which has been reproduced from EUR-lex, the official European Communities legislation website, is European Communities copyright.

LexisNexis, a Division of Reed Elsevier (UK) Ltd, Halsbury House, 35 Chancery Lane, London WC2A 1EL

Telephone: 020 7400 2500 Fax: 020 7400 2842

Printed and bound in Great Britain by Hobbs the Printers Ltd, Totton, Hampshire

1 Introduction

This *Tax Digest* covers the Transactions in Securities legislation, which many readers no doubt still call 'Section 703'. Within the next year, that title will become out-of-date: already, there are a series of income tax specific provisions in the Income Tax Act 2007, and the corporation tax regime is being rewritten into what will become Corporation Tax Act 2010.

Nevertheless, the legislation has been with us for nearly 50 years, now, having been enacted originally in FA 1960. And it remains as relevant as ever, with tax rates on gains being materially lower than the rates on income.

2 History and scope

2.1 Background

One of the most important things to remember about this legislation is that it was enacted five years before the capital gains tax legislation that we are now very familiar with, and two years before the first attempt at taxing short-term gains, in 1962. So a great deal of the tax avoidance schemes that existed at that time were geared towards turning income profits, taxable at rates up to 98% in some cases, into capital gains that were not taxable at all.

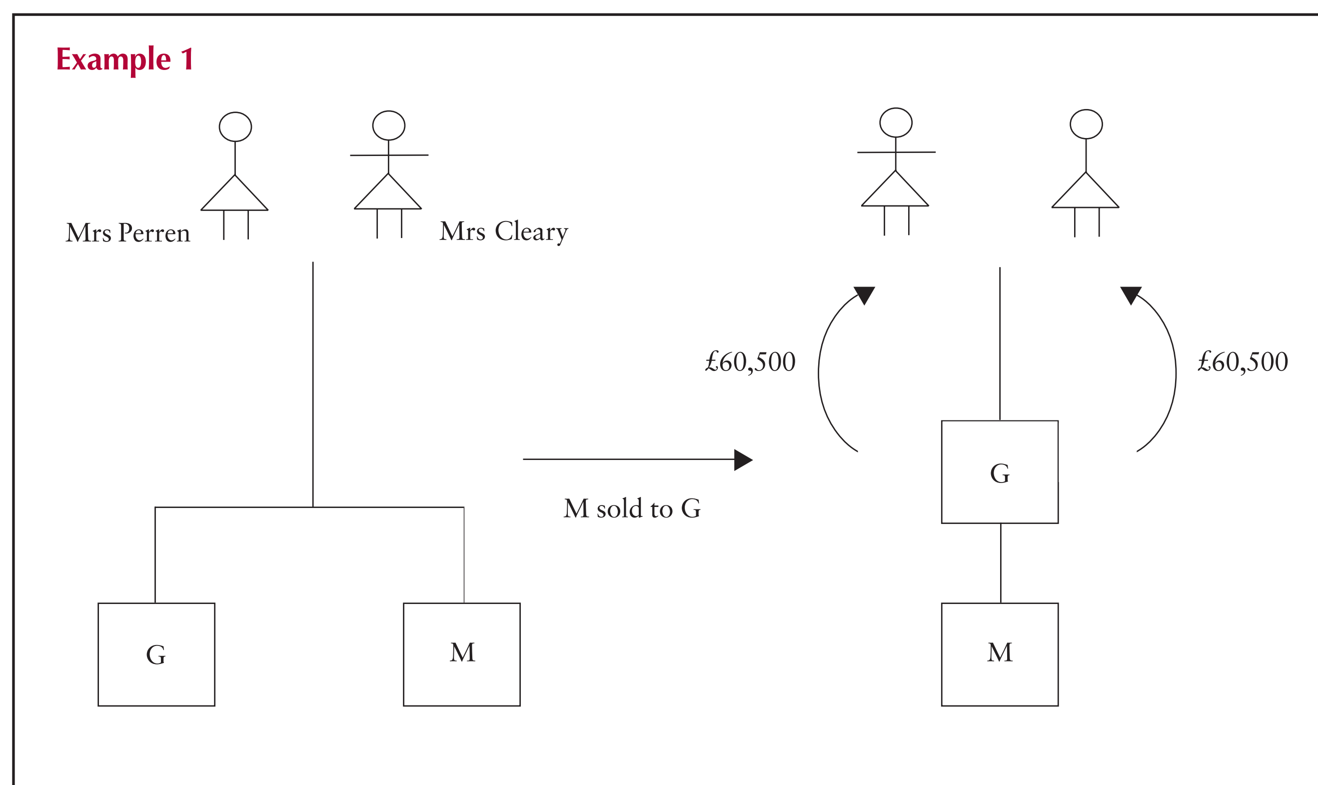
Examples 1 and **2** are just two examples of avoidance schemes that were practised prior to the enactment of this legislation in 1960, and which it was designed to stop.

Example 1: *CIR v Cleary* 44 TC 399

Mrs Cleary and her sister, Mrs Perren, each owned 50% of the shares in each of G Ltd and M Ltd. G Ltd had accumulated distributable profits in excess of £180,000. If those profits had actually been paid out as dividends to the sisters, the amounts paid out would have been liable to both income tax and to surtax.

Instead, M Ltd was sold to G Ltd for £121,000, each sister receiving £60,500. (See **Example 1 diagram**.)

Absent the provisions for taxing certain transactions in securities as if the relevant consideration had been distributed as a dividend, the sisters would have received the £60,500 each as a capital gain and there would have been no tax to pay.



The impact of the 1960 legislation is that the sisters were caught by Circumstance D (see below) and the £60,500 was taxed on each of them as if it had been received as a dividend.

Example 2: *CIR v Greenberg* 47 TC 240

L Greenberg Ltd was owned by Mr Greenberg and his son, Henry. The company was very profitable and in 1958 it was considered likely that the company would make at least £20,000 profits over the next five years. As in the *Cleary* case, dividends would have been taxed at very high rates, so the Greenbergs entered into a forward stripping arrangement, instead.

First, the Greenbergs subscribed for £100 of new preferred shares in the company, carrying preferred dividends amounting to £20,000 over the five years. The shares were then sold to Finsbury Securities Ltd., a company of share dealers, for £20,100. The intention was that the Greenbergs would have a £20,000 tax-free capital gain. Finsbury Securities would receive £20,000 preferred dividends over the five years and, as share dealers, they would also be able to claim tax deductions for both the cost of the shares of £20,100 and the loss in value of £20,000.

In the event, Finsbury Securities did not get the deduction they anticipated. This was denied under earlier legislation, although it would almost certainly have been denied under Circumstance B of the transactions in securities rules (see below).

And the tax position for the Greenbergs was also caught, this time by Circumstance C of the new rules.

2.2 History

During the 1950s Parliament enacted a number of statutory provisions that were aimed at specific tax avoidance devices, such as bond-washing. However, there was still a constant stream of tax mitigation schemes, as can be seen from the examples throughout this *Tax Digest*. Many of these, such as bond-washing and dividend strips, were based on converting income chargeable to income tax into capital receipts not chargeable to tax at all, as there was no capital gains tax until 1965. Eventually, very general anti-avoidance legislation was introduced as FA 1960 s 28, effective from 6 April 1960. The legislation remains largely unchanged in effect to the present day.

The legislation is still relevant, nearly 40 years after its enactment, as capital gains tax rates have often, as now, been lower than tax rates on income. At the time of writing, for example, for individuals, the main capital gains tax rate is 18%, whereas the income tax rate can be up to 40%. For companies, many chargeable gains are exempt (under the substantial shareholdings exemption, for example), while the main rate for corporate profits is 28%.

2.3 Scope of the legislation

Despite the reasons for enacting this legislation, it was never restricted to a specific type of transaction, such as bond-washing or dividend and asset stripping transactions. This would have defeated the object, as stated in the Budget Resolution: 'it will give [HMRC] protection against devices (outside the immediate dividend-stripping and bond-washing fields) which might be adopted in connection with stocks, shares and securities'.

There is judicial approval of this position, too, in a number of cases. For example, in *IRC v Parker* 43 TC 392, Lord Wilberforce said:

> 'I do not find it possible to discern in this Act any indication that it was the purpose of the Legislature to limit it to any specific kind of tax avoidance. The scheme and drafting … is far too general to admit of the suggested restriction, and I do not think that interpretation should seek to narrow this generality.'

And in *IRC v Joiner* 50 TC 449 he said:

> '… we must continue to give "transactions in securities" and "transactions relating to securities" the widest meaning: we can neither confine these expressions to the instances given in [TA 1988 s 709(2) or ITA 2007 s 713], nor can we deduce from that enumeration any limitation upon their scope.'

2.4 Application to capital gains avoidance

The legislation was enacted in 1960, five years before the enactment of capital gains tax. It has never been amended to refer to capital gains tax and it has generally been accepted that it cannot apply to avoidance of capital gains tax, *per se*. This is explicit in the rewritten income tax form and its definition of an 'income tax advantage'. However, the corporation tax version only refers to a 'corporation tax advantage', with no exclusion for the avoidance of corporation tax on chargeable gains. Most commentators nevertheless agree that the history of the legislation means that TA 1988 s 703 does not apply to the avoidance of corporation tax on chargeable gains, although HMRC has never been willing to confirm that the scope of TA 1988 s 703 has been limited in this way.

Tax Digest Issue 81 Text.pmd 2 22/07/2009, 12:00

2.5 Interaction with other taxes

The strict technical position is that counteraction can be taken even if the transaction has given rise to a liability to tax under non-income tax provisions, such as capital gains tax, inheritance tax and so on. However, HMRC (and, previously, the Inland Revenue) has frequently stated that counteraction is normally only taken in respect of any tax advantage not caught by the other legislation (see, for example, HMRC's Company Taxation Manual CTM36810). In fact, at CTM 36860, HMRC's view is that 'Where any legislation other than CGT legislation applies to transactions with the general scope of ICTA88/S703 - S709 then ICTA88/S703 applies only to any tax advantage which remains after the other legislation has been invoked'. This is technically incorrect but makes the point well enough.

This approach has received judicial approval on a number of occasions. In *Williams and ors v IRC* [1980] STC 535, assessments to surtax had been made on the taxpayers on an apportionment of a company's income, but there was also a tax advantage via loans from the company. The courts held that HMRC was entitled to take counteraction under TA 1988 s 703 in respect of the loans, on the understanding that if the counteraction succeeded the surtax assessments would be cancelled.

Similarly, the extent of possible counteraction is not restricted by any other tax paid (except income tax). In *IRC v Garvin* [1981] STC 344, the taxpayer had paid capital gains tax on a sale of shares, but HMRC discovered that the sale was part of a series of transactions and sought to take counteraction under TA 1988 s 703. HMRC said that credit would be given by concession against the tax charged under TA 1988 s 703. The House of Lords allowed the taxpayer's appeal on other grounds but their Lordships were unhappy that double taxation was only avoided by concession.

2.6 Interaction with self-assessment

Counteraction under the anti-avoidance provisions requires a notice to be issued by the Board of HMRC. As a result, liability (or potential liability) under the provisions cannot be a matter for self-assessment. This was confirmed in *Tax Bulletin 46*, which states explicitly that there is no requirement to self-assess liabilities under this legislation. Taxpayers are invited, however, to mention on their return any correspondence with HMRC about the provisions.

By the same token, the normal self-assessment time limits do not apply to the anti-avoidance provisions, which have their own longer time limits for seeking information from taxpayers and for counteraction.

2.7 Current legislative references

The legislation applicable to individuals is at ITA 2007 Ch 1 Part 13, ss 682-713 and has effect for all transactions in securities that represent income tax avoidance and take place after 5 April 2007, regardless of when the tax advantage accrues.

The legislation applicable to corporation tax is at TA 1988 Ch 1 Part 17, ss 703-709.

There is a Corporation Tax Bill to be enacted, probably for 1 April 2010. The modern form of this legislation is at Part 18, ss 733-754, of that Bill.

For the purposes of this *Tax Digest*, where the statute is quoted, the wording of ITA 2007 is generally used. This legislation is in the more recent 'modernised' statutory form, with shorter and clearer wording, and is also used in the new Corporation Tax Bill. The author believes that the new wording of this complex legislation has not changed the meaning of the rules in any way.

3 Interpretation

The general approach to these provisions is to interpret the words of the legislation as widely as possible. In the legislation itself, for example, it is clear that certain specific concepts are to be given a wide interpretation. Thus the definition of 'transaction in securities' in TA 1988 s 709(2) / ITA 2007 s 713 is worded extremely widely. The term includes 'transactions of whatever description relating to securities' and, in particular, the purchase, sale or exchange of securities, the issuing or securing the issue of new securities, applying or subscribing for new securities or altering or securing the alteration of the rights attached to securities.

The courts have also considered it necessary to interpret the provisions widely, in order that they might be effective as anti-avoidance rules. In *IRC v Greenberg* 47 TC 240 Lord Reid said:

> '…on the face of it any single act done by one person alone is a transaction in securities if it is one "relating to securities". This is a vague phrase, but I do not see how to stop short of giving to it a very wide meaning.'

And:

> '…if the courts find it impossible to give very wide meanings to general phrases the only alternative may be for Parliament to do as some other countries

Tax Digest Issue 81 Text.pmd 3 22/07/2009, 12:00

have done and introduce legislation of a more sweeping character.'

Lord Wilberforce, in *IRC v Joiner* 50 TC 499, noted that these rules require:

> '… a different method of interpretation from that traditionally used in taxing Acts … the scheme of [these provisions], introducing as they did a wide and general attack on tax avoidance, required that expressions which might otherwise have been cut down in the interest of precision were to be given the wide meaning evidently intended …'

This principle of a wide interpretation of anti-avoidance legislation is now well established as necessary to give effect to the intention of Parliament, and is routinely applied across a wide range of other anti-avoidance provisions.

4 Structure

The legislation gives HMRC the power to unwind or counteract a tax advantage, if that tax advantage arose as a result of tax avoidance arrangements where the necessary, widely-drawn conditions are satisfied. However, there is an 'escape clause', so that HMRC cannot challenge *bona fide* commercial transactions with no tax avoidance motive.

4.1 Counteraction

HMRC has the power to counteract tax advantages under these provisions by making appropriate adjustments. The possible adjustments are specified (in TA 1988 s 703(3) / ITA 2007 s 698(4)) as:

- an assessment;
- nullifying a right to repayment;
- requiring the return of a repayment already made;
- the computation or recomputation of profits or gains; and
- the computation or recomputation of a liability to tax.

The administration of the counteraction process is discussed below.

For income tax purposes only, ITA 2007 s 699 imposes a limit to the amount of the counteraction which may be taken in the Circumstances in ITA 2007 ss 689 and 690. The charge must not exceed the amount of tax for which the person concerned would be liable if he received a qualifying distribution equal to the amount or value of the consideration mentioned in those Circumstances on the same date as he received that consideration.

4.2 Conditions

A person is liable to counteraction by HMRC under these provisions if three conditions are satisfied:

- a person must be in a position to obtain, or must have obtained, a tax advantage (TA 1988 s 703(1) / ITA 2007 s 684(1));
- the tax advantage must be obtained or obtainable by that person in consequence of:
  - a transaction in securities (TA 1988 s 703(1)(*b*) / ITA 2007 s 684(1)(*b*)(i));
  - the combined effect of two or more transactions in securities (TA 1988 s 703(1) / ITA 2007 s 684(1)(*b*)(ii)); or
  - the combined effect of one or more transactions in securities and the liquidation of a company (TA 1988 s 703(2) / ITA 2007 s 684(3)); and
- one of the 4 (Circumstance B was repealed by FA 2008) prescribed Circumstances (in TA 1988 ss 704A-704E / ITA 2007 ss 686-690) must be present (TA 1988 s 703(1)(*a*) / ITA 2007 s 684(1)(*a*) and (2)). (Circumstance B was repealed by FA 2008.)

We will look in more detail at the meaning of a 'tax advantage', the meaning of 'in consequence of' and what a 'transaction in securities' is, for the purposes of this legislation.

4.3 Escape clause

Even where all three conditions are satisfied, HMRC may not take counteraction if the taxpayer can show that the transaction or transactions were carried out either:

(i) for bona fide commercial reasons; or

(ii) in the ordinary course of making or managing investments;

and in either case that none of the transactions had as their main object or one of their main objects to enable tax advantages to be obtained. This provision is frequently known as the 'escape clause' and we will be looking at this in more detail below.

Tax Digest Issue 81 Text.pmd 4 22/07/2009, 12:00

5 The conditions: 'tax advantage'

5.1 What is a 'tax advantage'

Since 2007, there have been two definitions, one for income tax (ITA 2007 s 683, Meaning of 'income tax advantage') and one for corporation tax (TA 1988 s 709(1), Meaning of 'corporation tax advantage' and other expressions).

Both definitions have the same three parts:

- a relief or increased relief from tax, which can include tax credits;
- a repayment or increased repayment of tax;
- the avoidance or reduction of a charge to tax or the avoidance of an assessment or a possible assessment to tax, whether the avoidance or reduction is effected by receipts accruing in such a way that the recipient does not pay or bear tax on them or obtains a deduction in calculating profits or gains.

5.2 Avoidance or reduction of a charge to tax

One ingredient frequently seen in these cases is that the transaction that was carried out is much more complex than the alternative higher-tax transaction that HMRC might be suggesting is the proper comparator. So for many years it was thought that, for there to be a tax advantage, there must also be an alternative, usually simpler, transaction that would have achieved a similar result but with a higher tax bill.

For example, in *Cleary v IRC* 44 TC 399, a sale of shares from one private company to another was the 'more complex' arrangement, compared to the simple payment of a dividend. And in *IRC v Parker* 43 TC 396, instead of a dividend there was the capitalisation of reserves followed by the redemption of that capital. In the House of Lords, Lord Wilberforce said of the definition of tax advantage that it:

> 'presupposes a situation in which an assessment to tax, or increased tax, either is made or may possibly be made, that the taxpayer is in a position to resist the assessment by saying that the way in which he received what it is sought to tax prevents him from being taxed on it, and that the Crown is in a position to reply that if he had received what it is sought to tax in another way he would have had to bear tax. In other words, there must be a contrast as regards the "receipts" between the actual case where these accrue in a non-taxable way with a possible accruer in a taxable way, and unless this contrast exists the existence of the advantage is not established.'

It is also considered that the reference to 'receipts accruing in such a way that the recipient does not pay or bear tax on them' is not restricted to cash receipts but includes acquisitions of property. Thus HMRC believes that assets distributed in the liquidation of a company, where the liquidation is part of a scheme involving a transaction in securities, may give rise to a tax advantage (Company Taxation Manual CTM36850).

5.3 Relief or increased relief from tax

The view that there must always be a comparative transaction carrying a higher tax burden is not universally true, following the decision in *IRC v Universities Superannuation Scheme Ltd* [1997] STC 1 (**Example 3**), where the planning turned what would have been an exempt capital gain into an income distribution with a payment of the tax credit to the tax exempt body.

Example 3: *IRC v Universities Superannuation Scheme Ltd* [1997] STC 1

USS, a charity, invested large sums of money in a property development project, part of which was in the form of shares in TSH, the company carrying out the development. USS had a put option whereby it could require S, the majority shareholder of TSH, to buy the shares for a sum that represented 7.5% of the profits of the development. When the option was exercised, the amount payable would have been £3,517,000.

S suggested, instead, that the TSH shares held by USS should be repurchased by TSH for £2,662,750 (see **Example 3** diagram). For tax purposes, most of this sum was treated as a distribution (under TA 1988 s 209(2)(*b*)) and, as an exempt fund, USS was able to claim a payment of the associated tax credit (under rules that have since been repealed). The tax credit was £854,250, which meant that USS's total receipt was £3,517,000.

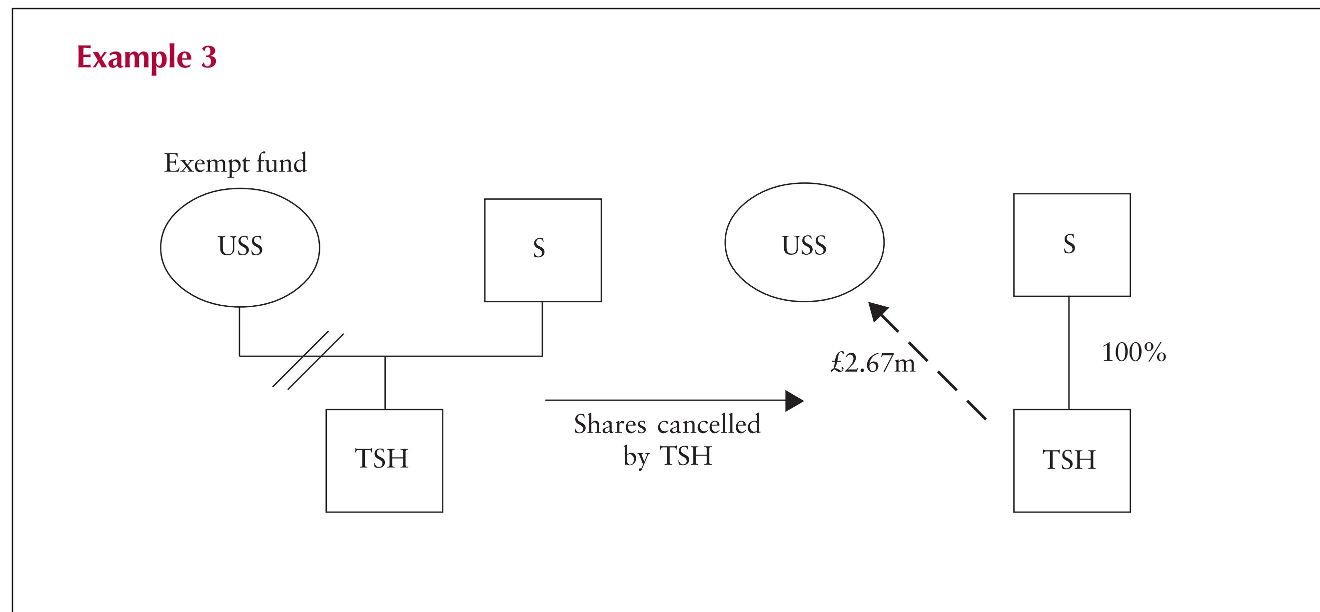
So, economically the transaction still left TSH as a wholly-owned subsidiary of S, but £854,250 of the consideration was effectively funded from the Exchequer.

Not surprisingly, HMRC refused the repayment and invoked TA 1988 s 703.

HMRC had long held the view that, where a person (eg a charity or a pension fund) is entitled to exemption from tax, and is therefore entitled to

Tax Digest Issue 81 Text.pmd 5 22/07/2009, 12:00

Example 3



repayment of tax deducted at source or to payment of a tax credit attached to a distribution, that person has obtained relief from tax which can give rise to a tax advantage capable of being counteracted, where the necessary Circumstances are present.

USS contended, *inter alia*, that a tax advantage could not arise because there was no way in which the receipts could have accrued in a taxable form, so there was no contrast with an alternative transaction carrying a higher tax burden, as required by the definition of a tax advantage. But the High Court said that the definition of a tax advantage did not require such a contrast or comparison when considering the grant of relief, as opposed to the avoidance of an assessment. Where the grant of a relief is concerned, the comparison is, in effect, with a different transaction that does not result in the relief being or becoming available and so does not result in the payment or repayment of tax from the Exchequer, regardless of the fact that the body concerned is exempt from tax on either transaction. In the USS case, the comparison would have been between a direct sale of the shares to the other shareholder and a share repurchase that generated a right to a payment of a tax credit. In neither case would USS have had to pay tax on the transaction.

The court also noted that the meaning of 'relief' in this context had to be given a wide meaning, as was appropriate for anti-avoidance legislation. So, for example, a 'relief' cannot be distinguished from an 'exemption'.

So we have two approaches. For the reduction of a charge to tax or of an assessment, there must always be a comparison between the transaction carried out and an alternative transaction, which is usually also simpler, which carries a higher tax burden. Conversely, for the purposes of a relief or exemption from tax, or a payment or repayment, the comparison is between a transaction where relief, etc. is due and one where it is not, even if neither would result in a charge to tax.

As a result of the USS case, and to put the matter beyond doubt, FA 1997 provided that references to relief and a repayment of tax include a tax credit and a payment in respect of a tax credit as regards distributions made after 7 October 1996, irrespective of the chargeable period concerned. (Note that, for transactions entered into on or after 1 April 2008, this provision has now been repealed for corporation tax purposes as companies can no longer obtain a tax advantage by obtaining a payable tax credit).

6 The conditions: 'in consequence of'

Very few cases have considered in detail the question of whether a tax advantage has arisen 'in consequence of' a transaction in securities.

On one level, in order for a company to be able, for example, to sell shares or to receive a dividend, it must have acquired those shares in the first place. Whether the acquisition was by subscription, by purchase or by barter (eg a share-for-share exchange), this initial

Tax Digest Issue 81 Text.pmd 6 22/07/2009, 12:00

acquisition is usually going to be a transaction in securities. But is that transaction in securities one to which the anti-avoidance legislation can apply? That is, does the subsequent tax advantage arise in consequence of it? In general terms, the answer must be that it does not, unless it is itself part of the tax avoiding arrangements.

Indirect authority for this position is found in *Laird Group plc v IRC* [2003] STC 1349 where the company acquired a new subsidiary for normal commercial reasons. The subsidiary was able to pay a dividend in circumstances that gave rise to a tax advantage and Laird had been aware of this at the time of the purchase. However, the Tribunal held *inter alia* that the dividends were not paid *in consequence of* the original acquisition of the subsidiary.

In *IRC v Garvin* [1981] STC 344 there was a complex series of transactions and the House of Lords considered the similar words 'in consequence of a transaction whereby' as they appear in Circumstance C (TA 1988 s 704C / ITA 2007 s 688). Lord Russell of Killowen said that:

> 'to treat the word [whereby] as introducing the concept that all that is required is that the transaction should be a *causa sine qua non* of the subsequent abnormal dividend goes in my opinion too far.'

Although the context is slightly different, it is further indirect judicial authority for the proposition that just because the legislation cannot apply if a person does not own shares does not mean that the initial acquisition of those shares is a transaction in securities *in consequence of* which a tax advantage arises. Indeed, in many cases the original acquisition of shares will have been for wholly commercial reasons, often years before there was any question of carrying out any tax planning.

In general, therefore, the phrase 'in consequence of' should normally be taken to mean that both the tax advantage and the transaction in securities must be part of the arrangements that HMRC might find offensive.

7 The conditions: 'transactions in securities'

As we have already seen, counteraction under the anti-avoidance legislation can only be taken against a taxpayer if he is in a position to obtain or has obtained a tax advantage *in consequence of*:

- a transaction in securities (TA 1988 s 703(1)(*b*) / ITA 2007 s 684(1)(*b*)(i));
- the combined effect of two or more transactions in securities (TA 1988 s 703(1) / ITA 2007 s 684(1)(*b*)(ii)); or
- the combined effect of one or more transactions in securities and the liquidation of a company (TA 1988 s 703(2) / ITA 2007 s 684(3)).

7.1 'Transaction in securities'

So what actually is a 'transaction in securities'? As we have already seen, the expression 'transaction in securities' has a very wide definition in TA 1988 s 709(2) / ITA 2007 s 713, which includes 'transactions, of whatever description, relating to securities, and in particular:

(a) the purchase, sale or exchange of securities;

(b) issuing or securing the issue of new securities;

(c) applying or subscribing for new securities; and

(d) altering or securing the alteration of the rights attached to securities'.

'Securities' for these purposes includes shares and stock, and an interest of a member of a company that is not limited by shares.

The examples in the legislation are not exhaustive, which is why the list is introduced with the word 'includes'. Various combinations of events and actions have been considered to fall within the definition, even though a layman might not consider them to be transactions in securities. For example, in *CIR v Greenberg* 47 TC 240 (see **Example 2**), it was decided that a dividend followed by a payment of the same amount as an instalment of capital together constituted a transaction in securities (even though the courts declined to decide whether the dividends alone were transactions in securities). And in *Williams v IRC* 54 TC 257 it was held that loans by a company to individuals who subsequently acquired the company were transactions in securities, even though the loans were not securities in the normal sense of the word.

7.2 Company liquidation

It was clear when the legislation was introduced that Parliament did not consider that a liquidation was a transaction in securities. The Attorney-General at the time said that a 'liquidation is not a transaction in securities any more than the payment of a dividend on shares'. However, it soon became clear that, if a liquidation were not a transaction in securities, there was a potential lacuna in the legislation. The 1962 addition of the words 'the combined effect of the transaction or transactions and the liquidation of a company' (ITA 2007 s 684(3) and TA 1988 s 703(2))

Tax Digest Issue 81 Text.pmd 7 22/07/2009, 12:00

indicate that the draftsman also did not consider that a liquidation was a transaction in securities. That said, this wording does not declare a liquidation to be a transaction in securities for the purposes of this legislation, so in fact it is arguably completely pointless!

HMRC's practice was not to apply the legislation to an ordinary liquidation, with no other elements. But there have been exceptions, as in **Example 4**.

Example 4: *CIR v Joiner* (50 TC 449)

A company was put into liquidation and the assets were distributed to the shareholders according to an agreement made between them before the liquidation. The trade was transferred to a new company and other assets were distributed to the shareholders, as capital receipts.

A tax advantage therefore accrued to the shareholders, as they had managed to extract assets from the company in capital form, while leaving the trade in a company. Their defence was that the tax advantage arose only from the liquidation, which was not a transaction in securities.

The courts decided that the pre-liquidation shareholders' agreement was a transaction in securities as it varied the rights of the shareholders in respect of their shareholdings, so the tax advantage arose as a result of the combined effect of the shareholders' agreement – a transaction in securities – and the liquidation of the company, and was squarely within the terms of TA 1988 s 703(2).

Notably, the courts declined to decide whether the liquidation *per se* was a transaction in securities. However, we might also see this decision as an example of the courts taking a wide view of the correct interpretation of this anti-avoidance legislation.

7.3 Payment of a dividend

As noted above, the Attorney-General in 1960 said that a 'liquidation is not a transaction in securities any more than the payment of dividend on shares'. But, once again, such a statement in Parliament does not necessarily make it so. The position was looked at in *Greenberg* (see **Example 2**). The issue here was that all the preliminary transactions in securities – the subscription for preferred share capital and the sale of those shares to the dealers – had taken place before 6 April 1960, when the new legislation came into force. However, the dividends were to be paid in tranches, as the profits were made and became distributable, so the only 'transactions' that occurred after 5 April 1960 were the dividends.

Fortunately for the Revenue, the payments of capital to the Greenbergs were also to be made in tranches, following the receipts of the dividends by the dealers. The courts decided that a dividend and the subsequent payment of an instalment of capital together constituted a transaction in securities. Again, we might see this as another example of the courts taking a wide view of the interpretation of this legislation. But the court stopped short of deciding whether a dividend *per se* was a transaction in securities.

Nevertheless, many people clearly took the view that a dividend was a transaction in securities, purportedly following *Greenberg*. For example, the TA 1988 s 706 Tribunal's judgment in *Marwood Homes No 3 v IRC* [1999] STC (SCD) 44 explicitly states that all parties agreed that the dividends were transaction in securities.

The position was finally resolved in *Laird Group plc v IRC* 75 TC 399. The company acquired all the share capital of S Ltd, a UK company carrying on a similar trade, and arranged that S Ltd paid a dividend of £3 million to Laird. Due to the operation of the now repealed and unlamented ACT regime, this allowed Laird to claim a repayment of corporation tax. HMRC contended, *inter alia*, that the tax advantage arose from the dividend, which was a transaction in securities. The House of Lords decided that there was no material difference between a distribution of profits in a liquidation and a distribution by way of dividend, as in either case this merely gave effect to the rights attached to the shares. Neither form of distribution was a 'transaction relating to securities'. Their Lordships asked rhetorically why a distribution to shareholders by a company that is still active and continuing to trade or carry on business should be a transaction in securities while a distribution to shareholders by a company that is being wound up is not? In other words, why should the intended continued activity of the company determine whether distributions in respect of shares should be a transaction in securities? The House of Lords felt that there was no reason for a difference and, therefore, upheld the company's view that a dividend is not a transaction in securities.

8 The Circumstances

As we have already seen, counteraction can only be taken under ITA 2007 s 698 or TA 1988 s 703 where a tax advantage is obtained in one of the four Circumstances set out in ITA 2007 ss 686-690 / TA 1988

Tax Digest Issue 81 Text.pmd 8 22/07/2009, 12:00

s 704 paragraphs A–E (for corporation tax purposes generally, and for income tax purposes before 6 April 2007). Circumstance B (TA 1988 s 704B / ITA 2007 s 687) was repealed by FA 2008 and is not considered further.

If there is an appeal against counteraction, the onus is on HMRC to show that one of these Circumstances is present and that the tax advantage arises in consequence of the transactions concerned.

8.1 Circumstance A (TA 1988 s 704A / ITA 2007 s 686)

Circumstance A is satisfied where a person receives an abnormal amount by way of dividend (see below) where the receipt is in connection with:

- the purchase of securities followed by the sale of the same or other securities;
- the sale of securities followed by the purchase of the same or other securities;
- the distribution, transfer or realisation of assets of a company;
- the application of such assets in discharge of liabilities

where the amount of the abnormal dividend is taken into account for

- exemption from income tax or corporation tax;
- setting off losses;
- obtaining relief for interest on a qualifying loan (income tax only);
- giving of group relief (corporation tax only); or
- the application of franked investment income in computing shadow ACT (corporation tax only).

A reference to a dividend includes other qualifying distributions and interest.

As noted previously, the wording of TA 1988 s 704A is rather more convoluted. The simpler rewritten version gives the same result in a clearer fashion with no change in meaning or effect.

8.1.1 Targets of Circumstance A

This paragraph was aimed at dividend stripping operations where a taxpayer receives an abnormal dividend. For example, an exempt body, such as a pension fund, might buy a security *cum dividend* and sell it *ex dividend*, incurring a small capital loss but obtaining a substantial payment of tax credit relating to the dividend. However, since such bodies are no longer entitled to payment of tax credits, Circumstance A is generally not invoked in such situations. However, we have had to consider it occasionally in other situations (see **Examples 5** and **6**).

Example 5: On-shoring foreign profits

Imagine a UK company with a profitable off-shore subsidiary, perhaps somewhere inoffensive, like the Isle of Man. Over time, profits have accumulated in the subsidiary but, under the rules applicable until 1 April 2009 (the new regime for the taxation of foreign profits), paying a dividend to the UK would have carried a tax bill under what was then Case V of Schedule D.

One way round the issue was to make the subsidiary UK resident for tax purposes, so that the profits could then be paid tax-free between UK companies, under TA 1988 s 208 re-enacted as CTA 2009 s 1285 (and repealed by FA 2009). So the Isle of Man directors would be replaced with UK resident directors. This would be sufficient to make the company UK tax resident by virtue of central management and control and effective management, under the terms of most of the UK's Double Tax Treaties.

The changing of the company's directors is not a transaction in securities. However, there was a period when there was major uncertainty about whether the subsequent dividend would be a transaction in securities. This was between the Court of Appeal and House of Lords decisions in *Laird Group v CIR*, as the Court of Appeal had found for the Revenue that a dividend was a transaction in securities, which would have been sufficient to bring the otherwise exempt dividend within the scope of the legislation. In the event, as we have seen, the House of Lords decided that a dividend *per se* was not a transaction in securities and this planning was a very useful tool.

Under the new rules for the taxation of foreign profits, it will usually now be possible to pay the dividend to the UK tax-free without the need for any planning.

Example 6: On-shoring foreign profits

Imagine the same situation as **Example 5**, but where the profits arose off-shore through a transaction in securities. For example, a client of mine had a Dutch holding company for its Eastern European operations. Those companies were sold

Tax Digest Issue 81 Text.pmd 9 22/07/2009, 12:00

at a large gain, leaving material profits in the Dutch company that would have been taxable if paid to the UK parent.

We looked at making the Dutch subsidiary UK resident for tax purposes, as in **Example** 5, and paying the profits tax-free to the UK parent, under TA 1988 s 208. However, the concern was that the distributable profits themselves arose from a transaction in securities – the sale of the Eastern European subsidiaries – and we were worried that HMRC would challenge the planning on the basis of a nexus between that transaction in securities and the subsequent dividend of the profits arising on the transaction, so as to bring the whole thing within the scope of the transactions in securities legislation.

Again, the new rules for the taxation of foreign profits will usually mean that such planning is unnecessary.

Note that neither of the examples mentioned above got as far as consideration of whether the dividend would have been abnormal in amount.

8.1.2 Abnormal amount by way of dividend

A dividend is abnormal for the purposes of Circumstance A if the appropriate authority is satisfied that it satisfies either of two conditions; the excessive return condition or the excessive accrual condition. The appropriate authority is either (from 6 April 2007) an HMRC officer or (from 1 April 2009) the First-tier Tribunal.

In the case of *IRC v Trustees of the Sema Group Pension Scheme* [2002] STC 276, it was decided that also determined that the amount to be taken into account in deciding whether the dividend was abnormal was the distribution only, and not the sum of the distribution and the tax credit. This is on the basis that 'distributions' are defined by TA 1988 s 209 without reference to the tax credit. This decision overturned an earlier decision on this point in *IRC v Universities Superannuation Scheme Ltd* [1997] STC 1, see **Example** 3).

A dividend is abnormal for the purpose of the excessive return condition if it substantially exceeds a normal return on the consideration given for the securities by the recipient company. The legislation requires that the length of time the securities have been held by that company (and not, for example, by any related parties, fellow group companies and the like), and that previous dividends or qualifying distributions, should be taken into account. If the securities were derived from other securities acquired previously, the dividend will be abnormal if it substantially exceeds the consideration given for the earlier acquisition. If the consideration given for the securities was in excess of market value, or if no consideration was provided, they are treated as having been acquired at market value.

For the purpose of the excessive accrual condition, a dividend at a fixed rate is abnormal if it substantially exceeds the amount which would have been received if it had accrued from day to day over the time the securities were held. But a dividend is not treated as abnormal if the taxpayer does not sell (or acquire an option to sell) any of the securities concerned or any similar securities within six months of their acquisition. Similar securities means securities giving the same rights as to capital and interest against the same persons, regardless of the form in which they are held or the way in which they can be transferred.

A dividend is not abnormal just because it arises in unusual circumstances. This is demonstrated in the *Sema Group Pension Scheme* case, where a qualifying distribution that arose from a share buy-back was held not to be abnormal simply because the transaction was unusual. The case involved the shares of a listed company being bought back at a price set by the company itself. In essence, the court held that the qualifying distribution was offered on the same terms to all shareholders, so the return could not be said to be abnormal within its own context.

8.2 Circumstance C (TA 1988 s 704C / ITA 2007 s 688)

This circumstance applies where a person (A) receives, in a form not taxable as income, a consideration representing:

(a) assets of a company available for distribution by way of dividend (or would be available apart from anything done by the company);

(b) future receipts of a company; or

(c) the value of trading stock of a company.

The consideration must be received in consequence of a transaction under which another person (B) subsequently receives an abnormal dividend (or before 1 April 2008, became entitled to a deduction under Circumstance B, now repealed).

The assets in (a) above do not include assets which represent a return of sums paid on the issue of securities, even if the law of the relevant country requires such assets to be available for distribution.

Tax Digest Issue 81 Text.pmd 10 22/07/2009, 12:00

The significance of these elements of the consideration will be considered with Circumstance D.

8.2.1 Target of Circumstance C

Circumstance C is intended to apply to the vendor of shares where the purchaser is within Circumstance A (or B before its repeal). If we look at the *Greenberg* case (**Example 2**), the brokers, Finsbury Securities, received the abnormal amount by way of dividend, and were caught by a precursor to Circumstance B, as dealers in shares. But the Greenbergs themselves were caught under Circumstance C. They had received tax-free (ie capital) consideration for the sale of the shares and that consideration represented the distributable reserves of the company.

Once again, we no longer see the transactions that this Circumstance was originally aimed at. But we still have to consider it in other situations, such as in **Example 7**.

Example 7: International reorganisations

One area where I have often been consulted is in the field of international reorganisations. In these cases, the planning related to the cost of repatriating foreign profits to the ultimate parent, which was often in the US, where the profits had to pass through a UK sub-holding company. Typically, a US group would have its EU subsidiaries held under a UK sub-holding company. The problem was getting the profits out of the EU subsidiaries without having to pay UK tax on the way back to the US ultimate parent.

One approach was to reorganise the group, so that the EU subsidiaries were transferred to a sub-holding company resident in a jurisdiction with a participation exemption or favourable Double Tax Treaties, that allowed the dividends to be paid tax-free through to the US parent. The UK sub-holding company would therefore sell the subsidiaries to the new sub-holding company and that transaction would generally be free of UK corporation tax on chargeable gains because of the UK's substantial shareholdings exemption for trading groups (TCGA 1992 Sch 7AC).

The concern here was that the UK sub-holding company would therefore receive tax-free consideration for the disposal, which is likely to represent in part the undistributed profits of the EU subsidiaries, and the new sub-holding company subsequently receives a dividend that might be challenged by HMRC as being abnormal in amount.

The general argument we used here was about the relative complexity of the transactions. That is, it is as simple to sell the EU subsidiaries and then pay a dividend as it is to pay the dividend first, then transfer the subsidiaries. So the tax efficient transaction is not more complex than the comparator, which means that it would have been more difficult for HMRC to challenge the transactions as being motivated by tax avoidance.

8.2.2 'in consequence of'

It is important to note that this phrase is used differently in Circumstance C than in the main charging provision in TA 1988 s 703(1) / ITA 2007 s 684(1). For the tax advantage to be obtained in consequence of transactions, it is only necessary that the advantage would not have been obtained if the transactions had not been carried out. But for the specific requirement in Circumstance C, that the taxpayer receives a consideration in consequence of a transaction whereby specified events subsequently take place, it is necessary for HMRC to be able to show that there was a causal connection between the transaction and the subsequent events. This distinction was drawn in the case of *IRC v Garvin* [1981] STC 344.

8.3 Circumstance D (TA 1988 s 704D / ITA 2007 s 689)

Circumstance D applies where a person receives consideration (in money or money's worth) on which he does not pay or bear income tax, in connection with the distribution, transfer or realisation of assets of a relevant company (see below) or the application of such assets in discharge of liabilities. The consideration must:

(a) be or represent the value of assets available for distribution by the company (or would be so available but for anything done by the company);

(b) be received in respect of future receipts of the company; or

(c) be or represent the value of trading stock of the company.

The term 'assets' does not include assets which represent a return of sums paid on the issue of securities, even if the law of the relevant company requires such assets to be available for distribution.

Part of these definitions are repeated from those in Circumstance C.

8.3.1 Target of Circumstance D

It has been established that Circumstance D catches a variety of transactions which would not be considered as dividend stripping or stock stripping. The most

Tax Digest Issue 81 Text.pmd 11 22/07/2009, 12:00

obvious example of the effect of Circumstance D is in the *Cleary* case (**Example 1**). But we also see it used a lot by HMRC in cases involving management buy-outs or buy-ins, where some of the original shareholders also retain a stake (**Example 8**).

Example 8: Private equity transactions

Mr Simon owns 100% of the shares of 59th Street Ltd., a successful trading company, which is now worth £20 million. As the business is expanding, he realises that he needs substantial external financing to fund the expansion. Garfunkel Enterprises, a private equity firm, agrees to provide funds. The deal is structured so that Garfunkel Enterprises sets up a new company, Simon & Garfunkel Ltd., with £90,000 equity and a £10 million debt. Simon & Garfunkel Ltd. then buys 59th Street Ltd. for £20 million, paying £5 million cash, issuing Mr Simon with £10,000 share capital, so that he owns 10% of Simon & Garfunkel Ltd., and issuing him £12.9 million in loan notes, to be paid off over ten years. (See **Example 8** diagram.)

Superficially, Mr Simon is selling his company for a total consideration of £18 million in cash and loan notes and 10% of the equity of Simon & Garfunkel Ltd. So one would expect this to be a purely capital gains transaction with tax payable at 18% on the gain.

HMRC see this transaction as structurally similar to the transaction in the *Cleary* case (Example 1), with proceeds being received free of income tax. In effect, since the proceeds received by Mr Simon that are taxable at 18%, compared to the 25% rate for a dividend distribution, Circumstance D may be in point.

In the example given, the most likely outcome is that HMRC would agree that this is a transaction carried out for *bona fide* reasons and not for the avoidance of tax, and no counteraction would be considered.

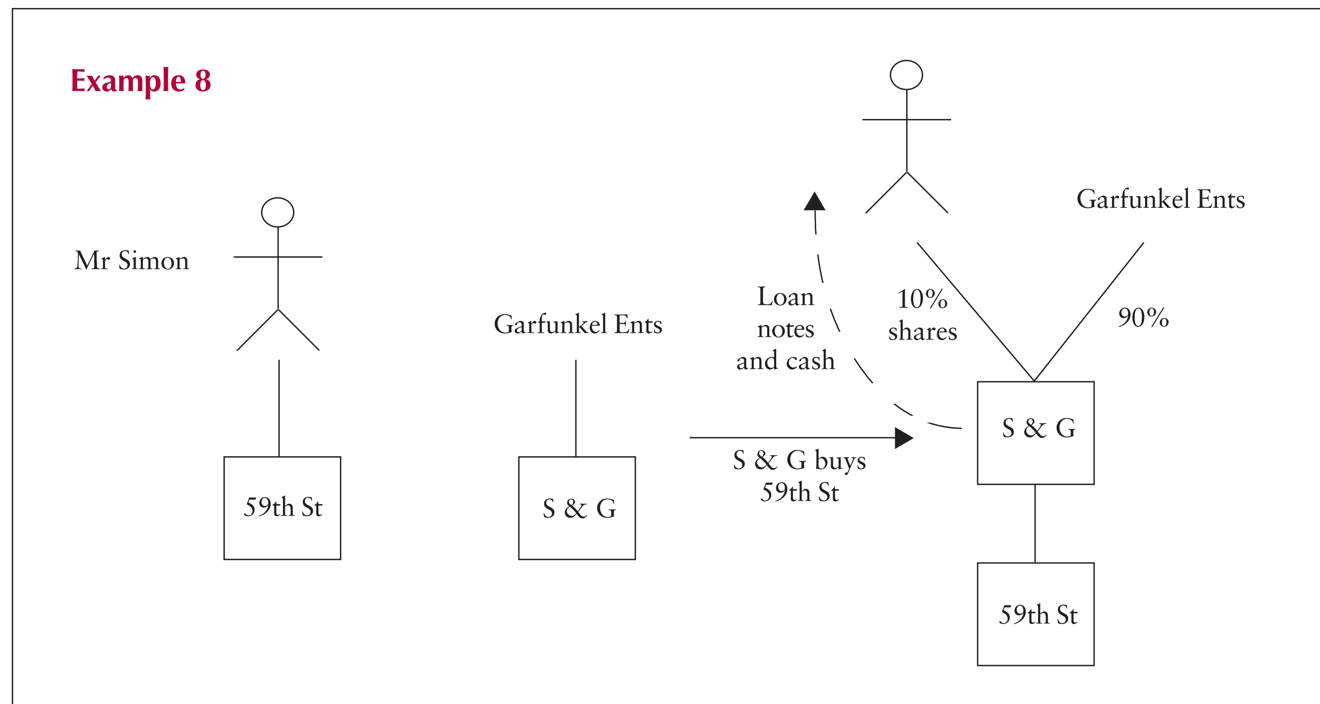
Alternative scenario

Suppose, instead, that the deal is structured to give Mr Simon 60% of the equity of Simon & Garfunkel Ltd., together with cash and loan notes to the value of £8 million. This looks much more like a *Cleary* transaction, as Mr Simon retains control of the business but has nevertheless received consideration of £8 million free of income tax. In a case like this, it is more likely that clearance would be refused, because of the similarities to the *Cleary* case.

In practice, since the Transactions in Securities legislation is to prevent the receipt of distributable profits in a tax-free form, HMRC can only consider counteraction if and to the extent that 59th Street Ltd. has reserves available for distribution (see below).

Practical issues

In practice, HMRC does not generally take issue with transactions where a person materially



reduces his stake, such as Mr Simon reducing his stake from 100% to only 10%. But HMRC does look closely at transactions where the person retains control or where the stake is not materially reduced, which is why the alternative scenario might cause a problem, as Mr Simon retains control of the company. And in **Example 10**, we will see a secondary buy-out, where Mr Simon holds 10% of the new buy-out company, as well as receiving cash, so HMRC might challenge this transaction as being too like the *Cleary* case.

In determining whether a person retains a similar stake, or retains control, HMRC will also look at shareholdings of other family members and connected parties. So if Mr Simon had sold 59th Street Ltd. to his daughter, Carly, and retained an equity stake, HMRC might have challenged the transaction on *Cleary* principles, as the company effectively remains under the control of the Simon family.

There is no clear answer to the issues raised here and HMRC will review every case on its merits.

We have also had to consider Circumstance D in cases of international group reorganisations (**Example 9**).

Example 9: Irish reorganisation

A US group had a UK trading subsidiary. They decided to start business in Ireland, too, and set up an Irish company under the UK subsidiary to carry out this business. A number of years later, the Irish business was extremely profitable but there was significant tax leakage on repatriation of the profits through the UK company. Nor was there any longer a commercial need to have the Irish company held through the UK. So the US parent decided to set up an Irish holding company to acquire the Irish trader from the UK company. Under the new structure, the Irish profits could be paid directly to the US parent with minimal tax leakage. (See **Example 9** diagram.)

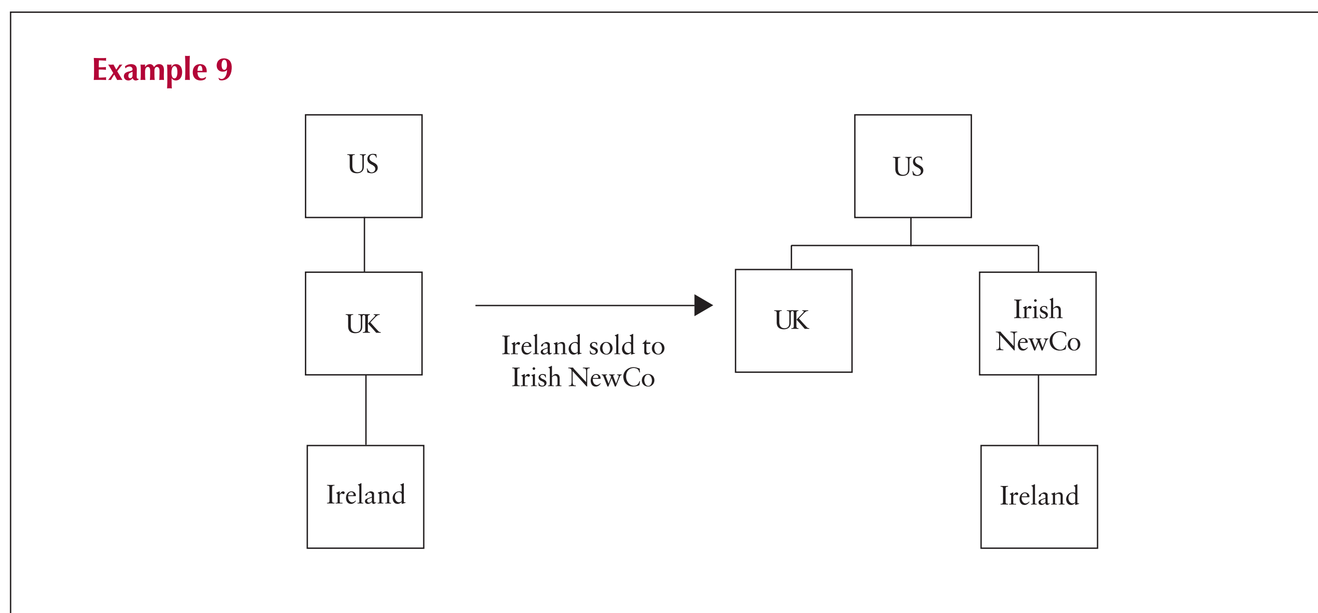
Since this was a trading group, the UK company would not suffer any corporation tax on the transaction, due to the substantial shareholdings exemption. So the transaction again looks very much like a *Cleary* transaction, with a person (the US parent) effectively selling a company it owned indirectly to another company it owned, for a tax-free consideration.

In the event, a clearance application (see below) was made and HMRC was satisfied that the transaction was to be carried out for *bona fide* commercial reasons and that there was no intention to avoid tax.

8.3.2 Relevant company

The definition of a relevant company (TA 1988 s 704D / ITA 2007 s 691) is in some respects similar to that of a close company but it is important to recognise the points of difference. However, the same tests of control in TA 1988 s 416 apply. A relevant company is:

(a) one under the control of not more than five persons;



(b) any other company (including those whose shares are traded on the Alternative Investment Market – Revenue Budget Press Release dated 28 November 1995 ('Cancellation of tax advantages from certain transactions in securities')) other than those whose shares (other than debenture stock, preferred shares or preferred stock) are listed in the Official List of the Stock Exchange and dealt in on the Stock Exchange regularly or from time to time.

However, a company is not a relevant company if it is controlled by one or more companies which are not relevant companies.

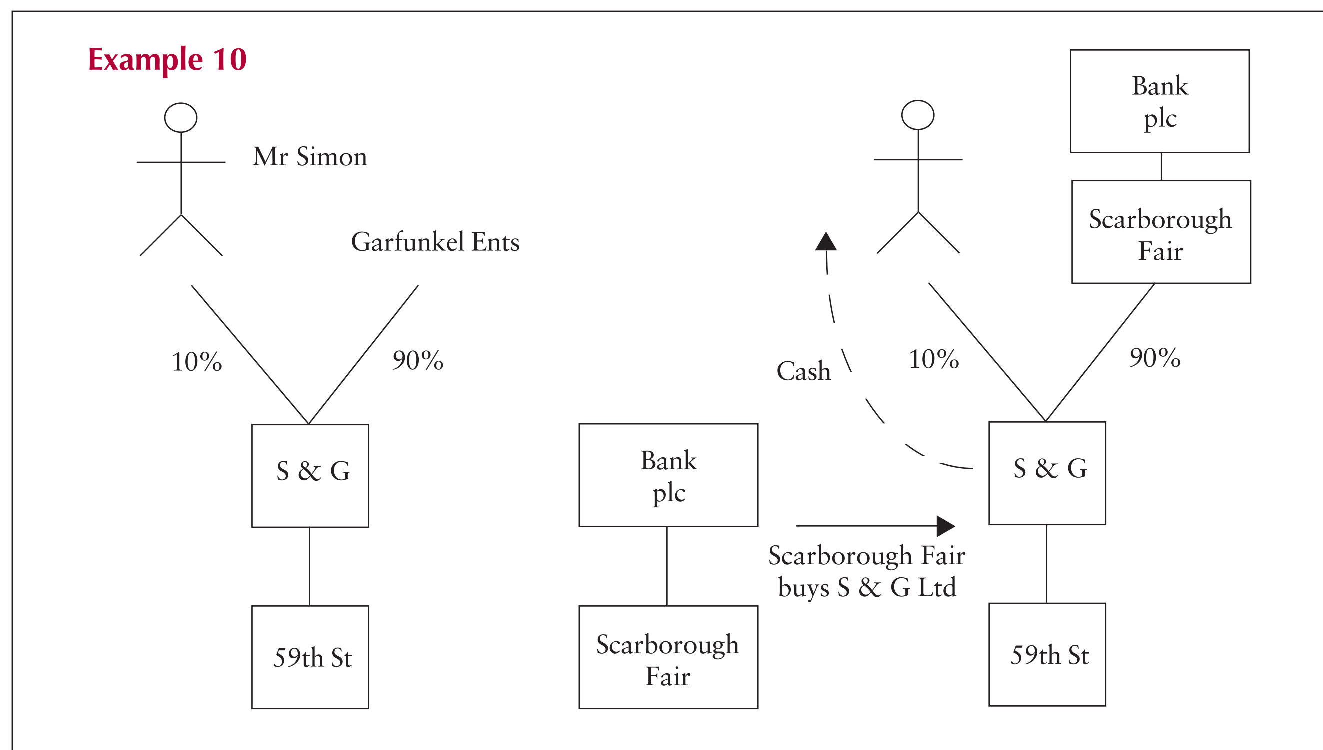
It is an open question whether the requirement that the company be listed on the London Stock Exchange is susceptible to challenge as being contrary to the EC Treaty and the rights to freedom of establishment and to the free movement of capital. That is, this provision may be seen as unjustifiably discriminating against companies listed on the exchanges of other EU Member States, and in favour of companies listed on the UK Stock Exchange. Such discrimination, if it cannot be shown to be both justified and proportionate, could be held to be a breach of the EC Treaty and hence unlawful.

In *IRC v Garvin* [1981] STC 344 it was held that the company must be a relevant company at the date of the relevant distribution of profits. This may be advantageous to taxpayers in private equity transactions where the private equity investor is a subsidiary of a UK listed group, such as the major clearing banks. In a number of cases, HMRC has conceded that transactions in securities involving such investors cannot be caught by this legislation, as the company being transferred is controlled by a listed company, so that Circumstance D cannot apply.

Example 10: Listed company investment

The Simon & Garfunkel group (see **Example 8**) has been trading successfully for some time following the private equity investment. So Garfunkel Enterprises, the private equity firm which holds 90% of the equity, decides to sell its investment. The buyer is a UK listed bank, which structures the purchase as a secondary buy-out, through a newly-incorporated company, Scarborough Fair Ltd. As in **Example 8**, Scarborough Fair Ltd. puts in a small amount of equity and a lot of debt. It then buys Garfunkel Enterprises' Simon & Garfunkel shares for cash and pays Mr Simon in cash and equity, so that he now has 10% of the equity of Scarborough Fair Ltd. (See **Example 10** diagram.)

Once again, this looks like a *Cleary* transaction from Mr Simon's perspective. He held 10% of Simon & Garfunkel Ltd. before and he holds 10% of Scarborough Fair Ltd. afterwards. However, as a result of the secondary buy-out, all the companies are subsidiaries of a UK listed group and therefore



cannot be relevant companies. So Circumstances D and E (see below) cannot apply and no counteraction should be possible.

8.3.3 Consideration

In most cases, the consideration will be recognisably a payment of a tax-free sum or the receipt of assets (money's worth). But this is not a *sine qua non* for the legislation to apply. In *Williams v IRC* [1980] STC 53 the taxpayers were the shareholders of a property company, K Ltd, which had made a substantial profit. Following a complex sequence of transactions, including a distribution of profits by K to a new parent company, a third company made interest-free loans to the shareholders of the original company. It was held that the loans had been received by the taxpayers in connection with the distribution of the profits by K Ltd, demonstrating that the loans were themselves to be considered as "consideration" for the purposes of this legislation.

8.3.4 In connection with

Circumstance D only applies if consideration is received free of tax in connection with the distribution of profits of a relevant company. The phrase 'in connection with' is satisfied by a less definite causal link than the phrase 'in consequence of' in TA 1988 s 703(1) / ITA 2007 s 684(3) or in Circumstance C: it involves a relationship between things one of which is bound up with or involved in or having to do with another.

There are a number of examples throughout the jurisprudence in this area. In *Anysz v IRC* [1978] STC 296 a scheme was effected to extract a development profit from a property company, K Ltd. The scheme included the exchange by the taxpayers of their shares in K Ltd for shares in an investment company, P Ltd and a dividend from K Ltd to P Ltd. The Special Commissioners found that the purpose of the share exchange was to enable K Ltd to be stripped of its assets by the subsequent dividend, so the receipt by the taxpayers of the shares in P Ltd was 'in connection with' the payment of the dividend by K Ltd to P Ltd and accordingly Circumstance D applied.

Similarly, In *Williams v IRC* (see **8.3.3** above), it was held that the loans had been received by the taxpayers in connection with the distribution of the profits by K Ltd.

8.3.5 In connection with the distribution of profits / assets

The wording in TA 1988 s 704D refers to the 'distribution, transfer or realisation of profits' of a company. In the *Cleary* case (**Example 1**), the taxpayers argued that Circumstance D only applied if the transfer of assets diminished the company's assets available for distribution. Otherwise, the transfer of assets was not 'in connection with the distribution of … profits'. The House of Lords preferred to read the phrase as meaning 'In connection with the distribution, transfer or realisation, including application in discharge of liabilities, of profits, income, reserves or other assets of a company', using the expanded meanings of 'distribution' and of 'profits', in TA 1988 s 709.

The simplified wording of the new legislation reflects this reading and makes it clear that Circumstance D does not require that there be a reduction of the company's distributable assets to be in point. Indeed, many people read Circumstance D as being targeted at planning, as in *Cleary*, that is specifically intended to avoid receiving distributable assets as such.

8.3.6 Assets available for distribution

Since the consideration for the sale of the shares of a company will usually come from a purchaser, it is clearly not necessary that the consideration giving rise to a tax advantage should come directly from the company itself. All that is necessary is that the consideration can be shown to represent reserves or assets of the company.

Nor does the statute concern itself with the identity of the company whose reserves are represented by the consideration. In *Cleary*, as we have seen, it was the transferee (purchaser) company that had reserves and it was those reserves that were held to have been represented by the consideration paid to Miss Cleary and her sister. In other cases, particularly in the private equity arena, HMRC has pointed to the reserves of the transferred company as the company whose reserves are represented by the consideration received by the shareholders, even though the consideration is provided by the new company, which typically has no reserves at the time of the transactions.

It is also clear from the judgment in *Addy v IRC* [1975] STC 601 that capital distributions are not excluded from counteraction under Circumstance D. In that case a company reconstruction was followed by the distribution of revenue and capital reserves in the liquidation of the original company.

8.3.7 But for anything done by the company

The requirement that the consideration represents assets available for distribution can be helpful, in that this generally means that the anti-avoidance legislation cannot be invoked in respect of a company that has no distributable reserves at the time of a relevant transaction in securities, perhaps through being loss-making, or because reserves have already been distributed up to shareholders. In such cases, cash consideration cannot represent distributable reserves.

Tax Digest Issue 81 Text.pmd 15 22/07/2009, 12:00

However, it was necessary to ensure that Circumstances C and D could not be circumvented by reducing a company's reserves, so that the tax-free consideration cannot not 'represent' reserves. For example, in *IRC v Parker* 43 TC 396, a company made a bonus issue of debentures which some years later were redeemed. The House of Lords held that the redemption of the debentures was a transaction in securities and a distribution of profit and that there was a tax advantage because, but for something done by the company (ie the bonus issue), the consideration could have been received by way of dividend.

HMRC has also invoked this proviso in circumstances where the reduction of reserves has not itself been a taxable transaction (**Example 11**).

Example 11: Pension contribution

A company made a large payment to the director's pension fund, so that the company claimed a tax deduction, but the pension fund did not bear tax on the receipt. Subsequently, the company was to be subject to a management buy-out, and one of the purchasers was the director concerned.

Clearance under TA 1988 s 707 was refused, in part because an element of the consideration was considered by the inspector to represent an amount that would have represented the distributable reserves of the company, but for the fact that that amount had been contributed to the pension fund.

Generally, HMRC does not object where the reserves have been reduced by a taxable transaction, such as the payment of a dividend to the shareholders.

What is less clear is HMRC's attitude where a deduction is not available, perhaps because the contribution is to an EBT, rather than an approved pension fund. There is still a reduction of the reserves available for distribution but, absent the tax deduction, HMRC might not find this so offensive.

8.3.8 In respect of future receipts

Generally speaking, where a transaction generates cash consideration, this is held to potentially represent the reserves of the company – as above – or the trading stock – below. Where the consideration is in the form of deferred cash, such as loan notes or redeemable shares, HMRC take the view that these are consideration in respect of future receipts of the company. Strictly, the legislation would appear to permit counteraction at the time the loan notes, etc, are issued. However, in these cases, HMRC has frequently stated in correspondence that counteraction will only be considered at the time the securities are redeemed, and any counteraction would be by reference to the distributable reserves of the company at that time. This would be consistent with the premise that the legislation is aimed at transactions that generate cash representing a company's reserves, not merely its receipts.

Example 8 revisited

If we return to the Mr Simon example, he received £13 million in loan notes on the first buy-out. HMRC might have effectively reserved judgment on the application of the Transactions in Securities legislation to this part of the consideration, and chosen to look at the reserves available for distribution at the time the loan notes were redeemed.

Conversely, immediate counteraction might be considered where the securities are convertible to cash in the short term. In particular, this is likely to apply where the instruments are short-dated loan notes, redeemable shortly after issue. HMRC has been known to take a similar view of bank-guarantees of loan notes, too, as the bank guarantee means that the loan notes can be effectively be converted to cash in the short term, by using them as security for personal loans. In HMRC's view this looks like a receipt of consideration in money's worth.

In practical terms, if the later redemption of loan notes or shares is part of a later shareholder exit from the company, HMRC will very often decide against counteraction.

8.3.9 Is or represents the value of trading stock

This form of consideration is exemplified in *CIR v Wiggins* (**Example 12**).

Example 12: *CIR v Wiggins* 53 TC 639

The company's trade was that of picture framers and, having bought a batch of old pictures for the frames, it was discovered that one of the pictures was an extremely valuable Poussin, potentially worth £130,000. Had the picture been sold as part of the trade, income tax would have been due at a high rate. Instead, there was a reconstruction and the trade was transferred from the original company, Wiggins, to a new company.

Tax Digest Issue 81 Text.pmd 16 22/07/2009, 12:00

Wiggins was then sold for £44,447, with the painting, to a third-party purchaser as a capital transaction. It was held that this was a tax avoidance scheme and that Circumstance D applied, as the consideration received by the shareholders represented the trading stock of the company that was sold.

The reason for the discrepancy between the value of the painting and the disposal proceeds of the company is the very high rates of tax involved. Essentially, if the company had sold the painting for £130,000, the company would have paid tax on the trading profit and a distribution of the remaining proceeds would have been subject to both income tax and surtax. So the lower price for the 'tax-free' sale of the company itself was based on a sharing of the overall tax benefits.

Unfortunately for the shareholders, the counteraction was based on the £44,447 received, so that they paid both income tax and surtax, having already given up the bulk of the proceeds on the basis of the anticipated tax savings. So this case demonstrates something of a double whammy for the taxpayers.

Transactions to which this provision applies are generally rare (perhaps due to the deterrent effect?)

8.4 Circumstance E (TA 1988 s 704E / ITA 2007 s 690)

Circumstance E applies where a person receives non-taxable consideration:

- which consists of any share capital or security issued by a relevant company;
- which represents the value of assets available for distribution by such a company;
- which is in connection with the transfer directly or indirectly of assets of a relevant company to another relevant company or in connection with any transaction in securities in which two or more relevant companies are concerned.

'Share' includes stock and any interest of a member in a company. 'Assets available for distribution' means assets of the company available for distribution by way of dividend (or which would be available but for something done by the company) or trading stock of the company. 'Relevant company' has the same meaning as for Circumstance D (TA 1988 s 704D / ITA 2007 s 691).

Other definitions have already been looked at in connection with Circumstance D.

If the share capital is not redeemable, counteraction can only be taken if and when the share capital is repaid, whether in a winding up or otherwise. In such a case, any distribution in a winding up will be treated as repayment of share capital to which the Transactions in Securities legislation might apply as a result of Circumstance E.

8.4.1 Target of Circumstance E

Circumstance E will apply to transactions whereby the tax-free consideration received is in the form of shares or securities, or other similar interests in a company. There is a high degree of overlap with Circumstance D (indeed, it is hard to conceive of a transaction within Circumstance E that would not also fall into Circumstance D).

Circumstance E will therefore catch a reorganisation of a family company where the trade and/or assets of one company are exchanged for shares or securities in another such company which results in the accumulated reserves of the first company being represented by capital of the other company.

There is a vital difference in the timing of counteraction between the two Circumstances, however. Under Circumstance E counteraction is deferred where the consideration is in the form of non-redeemable shares until such time as the shares are repaid. In such a case the taxpayer is entitled to have the counteraction deferred even if Circumstance D could apply.

8.4.2 Interaction with Circumstance D

Where, in a particular case, the circumstances of the transactions in securities fall within both Circumstance D and Circumstance E, Circumstance E will take precedence and HMRC cannot have a second bite of the cherry. This is particularly relevant where the consideration received by the taxpayer consists of non-redeemable share capital: HMRC cannot prevent liability being deferred under Circumstance E by relying on Circumstance D alone or as an alternative to Circumstance E. The specific and particular circumstances described in Circumstance E restrict the more general description in Circumstance D and the two Circumstances are not to be regarded as distinct alternatives.

This was decided in *IRC v Williams* (54 TC 257). In the Court of Appeal Bridge LJ said that it was 'perfectly clear' that the intention of Parliament was that Circumstance E had priority over Circumstance D in such cases, as otherwise TA 1988 s 704E(2) / ITA 2007 s 690(5) would be 'totally ineffective'. (However, in that case the issue of interest-free loans was held to be tax-free consideration for further transactions in securities to which Circumstance D applied, so HMRC's counteraction was deemed to be effective (see **8.3.3**).)

Tax Digest Issue 81 Text.pmd 17 22/07/2009, 12:00

9 Escape clauses

Even if a tax advantage is obtained in one of the Circumstances set out in TA 1988 ss 704A-704D / ITA 2007 ss 686-690 ITA, HMRC cannot take counteraction if the taxpayer can show:

(*a*) that the transaction or transactions concerned were carried out either for *bona fide* commercial reasons or in the ordinary course of making or managing investments; and

(*b*) that none of them had as their main objects, or one of their main objects, to enable tax advantages to be obtained.

These 'escape clauses' are at TA 1988 s 703(1) / ITA 2007 s 685. On an appeal against counteraction, it is for HMRC to show that a tax advantage has been obtained in one of the prescribed Circumstances. However, the onus is on the taxpayer to establish the availability of the escape clause.

It is also important to note that these are separate tests and it is entirely possible that transactions are carried out for *bona fide* commercial reasons or in the ordinary course of making or managing investments, while also having tax avoidance as a main object, as in *IRC v Trustees of the Sema Group Pension Scheme* (see **Example 17**).

9.1 *Bona fide* commercial reasons

The basic premise is that *bona fide* commercial transactions should not be susceptible to counteraction, so long as those transactions were not entered into for tax-avoidance reasons. This is clear from a reading of the Standing Committee debates on FA 1960 s 28. The question of what is a *bona fide* commercial reason has been considered a number of times by the courts, although each case is decided on its own merits and views have changed as taxpayers and their advisers become more sophisticated. **Examples 13** and **14** are cases where a *bona fide* commercial reason was accepted for the transactions. They are useful cases but, perhaps because business people and their advisors are nowadays more sophisticated and better informed about tax, if these cases were to be heard today, I suspect that the Tribunals or courts would concentrate on the tax saving and find that there was a tax avoidance motive.

Example 13: *IRC v Brebner* 43 TC 705

The taxpayer and five others were the main shareholders in a public company trading as coal merchants. A takeover bid was made for all the shares of the company at a price of 40*s* 6*d*, well in excess of the then market price of 25*s* per share. The taxpayer and five principal shareholders formed a group to oppose the take-over bid for two reasons. They had interests in fishing companies which bought coal on favourable terms from the company. Further, the bidder intended to liquidate the company and the appellants did not wish to see employees lose their jobs. Eventually, in February 1959 the group offered to acquire the shares of the other shareholders at 45*s* per share, an offer which most shareholders accepted.

To finance the purchase £108,000 was borrowed from a bank on a joint and several undertaking by the group and on condition of early repayment. It was intended from the outset that cash should be extracted from the company to pay off the bank loan though that consideration did not affect the price offered. The company's share capital was therefore increased, partly from the revenue reserve, and the increased share capital was then reduced by a capital (hence tax-free) repayment.

On appeal against counteraction, the main contention of the taxpayer was that the transactions were entered into for *bona fide* commercial reasons and did not have as one of their main objects the avoidance of tax. The Revenue contended that the extraction of cash had the gaining of a tax advantage as its main object. The courts found for the taxpayer. In a seminal speech, Lord Upjohn, in the House of Lords, said:

'My Lords, I would only conclude my judgment by saying, when the question of carrying out a genuine commercial transaction, as this was, is considered, the fact that there are two ways of carrying it out—one by paying the maximum amount of tax, the other by paying no, or much less, tax—it would be quite wrong as a *necessary* consequence to draw the inference that in adopting the latter course one of the main objects is, for the purposes of the section, avoidance of tax. No commercial man in his senses is going to carry out commercial transactions except upon the footing of paying the smallest amount of tax involved. The question whether in fact one of the main objects was to avoid tax is one for the Special Commissioners to decide upon a consideration of all the relevant evidence before them and the proper inferences to be drawn from that evidence.'

He further stated that whether a main object is to obtain a tax advantage is a subjective matter of the intention of the parties. This is often the intention of the taxpayers, but it suffices if it is the intention of those in control of carrying out the relevant transaction.

Tax Digest Issue 81 Text.pmd 18 22/07/2009, 12:00

Example 14: *Clark v IRC* [1978] STC 614

One of the shareholders of a private investment company, Robin Clark, also ran a commercial farm. The opportunity arose to purchase a neighbouring farm which could be run profitably with the taxpayer's own. In order to finance the transaction, he sold his 50% of the company to another family company (similar to the *Cleary* transaction).

The Special Commissioners found that there were good commercial reasons for acquiring the farm; it followed that the sale of the shares was also carried out for *bona fide* commercial reasons but that those reasons were too remote from the activities of the company to qualify for the escape clause.

The High Court overturned this decision on the basis that the Special Commissioners had misdirected themselves in law and that the commercial reasons for the transactions did not need to be connected with the taxpayer's interest in companies concerned in or affected by the transaction. The High Court did not have a problem with the Special Commissioners' finding of fact, that the transaction was carried out for *bona fide* commercial reasons, only with the finding in law, which was inconsistent with the finding of fact. The legislation did not concern itself with whose commercial reasons were in point, only with the existence of *bona fide* commercial reasons at all.

In the ordinary course of making or managing investments

The Special Commissioners were also required to look at the similar transactions carried out by Colin Clark, Robin's brother. Colin sold his shares as he didn't want to be stuck with 50% if Robin had sold his 50%, and also because selling the shares together might achieve a better price. Colin had no specific need for the funds and would not have sold had Robin not been selling his shares.

The Special Commissioners held that the sale of Colin's shares to another family company was done in the ordinary course of making and managing investments, which is the alternative requirement to the *bona fide* commercial reason, so that the escape clause applied to Colin, too, and the Revenue's counteraction was not valid. In effect, while the circumstances were unusual, he was protecting the value of his investment in the best way possible, by realising the investment and reinvesting the proceeds.

In similar contexts, it has been accepted that retention of family control of a private company and its business can be a *bona fide* commercial reason (*IRC v Goodwin, IRC v Baggley* [1975] STC 173, CA, [1976] STC 28). The courts accepted that the prosperity of a business could depend in part on the very fact that it was an old established family business and continued as such under family control and management, both in the context of company–customer relationships and of the employer–employee relationship. Where such reasons for the transaction were found by the Special Commissioners to be *bona fide* commercial, it was not open to the courts to overturn the finding of fact: the Special Commissioners could not be said to have acted in a manner which no body of commissioners, properly instructed in the law, would have done. Where the Special Commissioners find that the objects of transactions are *bona fide* commercial and that the obtaining of a tax advantage was not a main object, the reasons for the transactions are essentially questions of fact for the Special Commissioners to determine and there is no justification for interfering with their determination unless it is one which they could not reasonably have made.

It is also clear that a *bona fide* commercial reason for a transaction does not imply that the transaction itself has to be obviously commercial, as we see from the *Trevor Lloyd* case (**Example 15**).

Example 15: *Trevor G Lloyd v HMRC* (SPC 00672)

Mr Lloyd sold his 38.2% holding in a private trading company to a company that he owned jointly with his wife and a family trust. The commercial reason he gave was that this was part of a scheme to ensure that the other two (unrelated) directors of the trading company would each hold one third of the shares of the trading company.

HMRC argued that there were simpler commercial ways to achieve that end result, so the transaction could not have been carried out for *bona fide* commercial reasons. The Special Commissioner said that his first question was 'whether the Transaction was carried out for *bona fide* commercial reasons; it is not whether it was a *bona fide* commercial transaction, which is more objective ... The fact that it seems to me today that the Transaction was unnecessary does not mean that the Appellant did not believe that it was, or that [the other directors] did not regard it as a step showing that the ultimate end was being pursued. Accordingly I find that the Transaction was carried out for *bona fide* commercial reasons'.

9.2 Ordinary course of making and managing investments

This is the alternative escape clause from counteraction under the anti-avoidance legislation, although it is not incompatible with the *bona fide* commercial reason clause. Nor is it restricted to investment businesses. We have already seen its application in *Clark v IRC* (**Example 14**).

Conversely, in *IRC v Wiggins* (**Example 12**), the sale of the picture-framing company was described by the Special Commissioners as not having been in the ordinary course of making and managing investments, as 'none of the Appellants was ordinarily concerned in making or managing investments'.

In *IRC v Universities Superannuation Scheme* (**Example 3**), USS realised an investment in shares by agreeing that the shares should be cancelled, rather than sold, so that, in effect, part of the price of the transaction was met by the Exchequer. USS contended that TA 1988 s 703 could not apply as the transaction was in the ordinary course of making or managing investments. The Special Commissioner said 'USS took the transaction out of the ordinary course of making or managing investments and substituted a transaction which was in my judgment not ordinary. On the evidence before me I find that the second transaction … was not carried out for *bona fide* commercial reasons or in the normal course of making and managing investments'. As we have see, USS also argued that they could not be subject to counteraction under TA 1988 s 703, as they were in any case an exempt fund, so no tax was being avoided. But the courts held that the arrangements whereby part of the transaction consideration was funded by the Exchequer amounted to tax avoidance.

9.2.1 Conclusions

There are a number of broad themes arising from the decided cases about *bona fide* commercial reasons and the ordinary course of making or managing investments.

- Just because a transaction or series of transactions generates a tax advantage, does not of itself mean that the tax advantage was a main purpose of carrying out the transactions (*Brebner*).
- There is no rule that requires a connection between the commercial reason for the transaction(s) and the activity of the company whose shares or securities are being transacted in (*Clark*).
- A *bona fide* commercial reason for carrying out a transaction is distinct from the question of whether a transaction is itself commercial (*Trevor Lloyd*).
- There is no escape for transactions in the ordinary course of making or managing investments where the parties concerned do not habitually make or manage investments (*Wiggins*).
- But this escape clause may apply, even for unusual circumstances, so long as the transaction is itself ordinary (*cf. Colin Clark* and *USS*).

9.3 Tax avoidance motive

The test here is that that none of the transactions in securities have as their main objects, or one of their main objects, to enable tax advantages to be obtained. So it is not just about tax avoidance being the only reason for entering into the transactions, the test is also about whether tax avoidance was the one of the major motives behind the transactions, as opposed to being wholly ancillary.

The question of whether there is a tax avoidance motive behind the transactions is theoretically separate from that of whether the transactions were for commercial reasons or in the ordinary course of making and managing investments. Indeed, in many of the cases described above, the taxpayers won on the latter ground but lost on the former.

We are fortunate in having some cases with identical or nearly identical facts that can be contrasted to show this test in operation (**Examples 16** and **17**).

Example 16: *Marwood Homes Ltd*

Marwood Homes, a member of a group of companies, was making heavy losses. In addition the group wished to consolidate the building and maintenance division, of which Marwood Homes formed part. A series of transactions was carried out and, in due course, the Inland Revenue challenged these and raised counteraction notices. The Special Commissioners noted that the tax advantage was very much in the mind of those who decided to undertake the transaction but that it would be wrong as a necessary consequence to draw the inference that one of the main objects of the transactions had been to obtain that tax advantage (following *Brebner*). The Commissioners found a decision to be very finely balanced indeed but concluded on balance that it was not the subjective intention of those in control of Marwood Homes that a main object of the acquisition by Marwood Homes of the four subsidiaries was to enable a tax advantage to be obtained (reported in *Marwood Homes v CIR (No 1)* 1997 SCD 37).

Tax Digest Issue 81 Text.pmd 20 22/07/2009, 12:00

The Inland Revenue required the case to be reheard by the Tribunal constituted under TA 1988 s 706 (now abolished). On the re-hearing by the Tribunal, reported in *Marwood Homes v CIR (No 3)* 1999 SCD 44, new evidence was produced, including a note of a meeting convened to discuss a letter to be sent to the Inland Revenue requesting a clearance under TA 1988 s 707. The note stated that much of the meeting was spent 'beefing-up' the commercial rationale for the transactions. The Tribunal decided that this meant that the transactions had a main purpose of avoiding tax, effectively because they inferred that there was not originally an adequate commercial reason for the transactions. In their decision, the Tribunal stated that:

'If one or more of the specified transactions can be explained as having its main objective (or one of its main objectives) the obtaining of a tax advantage, the obtaining of that tax advantage may disqualify the transactions … from the *bona fide* commercial limb of the escape clause.'

The Tribunal held that the transactions were only rational if the tax advantage was taken into account, and the obtaining of that advantage was the main reason, if not the only reason, for the transactions in question. The company was not entitled to the protection of the escape clause.

The key point in this case is that the evidence seen on re-hearing the case clearly demonstrated that the commercial *bona fides* for the transactions were secondary to the desire to reduce the tax burden on the Marwood Homes group, so that the escape clause was not available.

The *Marwood Homes* case is also an important demonstration of the need to take proper care in correspondence between advisers and clients. Meeting notes in the terms described in the evidence in *Marwood Homes* can clearly be prejudicial in legal hearings, even if what was actually meant was something far more innocent. Given HMRC's powers to require information (see below), it must be assumed that every document relating to a transaction, except those covered by legal professional; privilege, may be seen by an inspector considering counter-action.

Example 17: The *Lewis and Sema Group* cases

In *Lewis (Trustee of Redrow Staff Pension Scheme) v IRC* [1999] STC (SCD) 349 and the very similar case of *IRC v Trustees of the Sema Group Pension Scheme* [2003] STC 95, the trustees of exempt pension schemes took advantage of an offer by the company to buy back its own shares. In both cases the transactions represented in large part a distribution (TA 1988 s 209(2)(*b*)) and the trustees claimed and received a tax credit in respect of those distributions. Subsequently, HMRC claimed that a tax advantage had been obtained by the sale of the trustees' shares to the companies instead of selling them on the open market.

In *Lewis*, the Special Commissioners accepted the claim by the trustees that the purchase was made in the ordinary course of making and managing investments. There was a requirement to reduce the pension fund's holding to 5% in order that the company could be floated, and the trustees did not wish to incur the costs and extra work which would have been involved if they had sold their shares in the course of the flotation. Although the trustees were aware of the tax benefit, this was not a main object of the sale of the shares, it was merely 'the cherry on the cake'.

In contrast, in *Sema Group*, the trustees decided to accept the buy back offer at a price below what they had paid, because a material part of the consideration would be treated as a distribution and the associated tax credit payable to the exempt fund would give the trustees an aggregate profit on the investment. While the Special Commissioners again found that the trustees were acting in the ordinary course of managing investments, they also found one of their main objects of the sales had been to enable tax advantages to be obtained, so the Revenue's counteraction was valid.

The key implication in these decisions is that the escape clause is not available if the transaction would not have been carried out if there were no tax advantage.

Many of the published decisions, such as the original *Marwood Homes* decision, have made it clear that taxpayers are entitled to take tax into account in their decision-making, without such considerations necessarily tainting the transactions with a tax avoidance motive. Indeed, commercially it would be remiss of the directors of a company not to take tax into account in making their decisions. As we have seen in *IRC v Brebner*, it was noted that the legislation requires a distinction between the purpose of a transaction and its effect. Thus, just because the effect is a reduced tax burden it is not open to HMRC to necessarily infer that this was the purpose of the transaction. As Lord Pearce, in the House of Lords, said:

Tax Digest Issue 81 Text.pmd 21 22/07/2009, 12:00

> 'Admittedly, an object of the carrying out of the broad scheme by way of the resolutions was a tax advantage. But that which had to be ascertained was the object (not the effect) of each interrelated transaction in its actual context, and not the isolated object of each part regardless of the others.'

9.3.1 Conclusions

Overall, there are no hard and fast rules in this area, and each case must be viewed on its own merits.

As noted in **Example 17**, the *Sema Group* case, when contrasted with *Lewis*, suggests that tax is a main motive for a transaction if the transaction would not have taken place without the tax advantage. This may be an extreme statement of the position. It is perhaps fairer to say that the escape clause may still be available in finely balanced cases, such as *Marwood Homes No. 1*, perhaps, where a positive tax outcome helps to tip the balance towards carrying out a transaction, or carrying it out in a particular way. But where a transaction would clearly not have been carried out, as in *Sema Group*, where the outcome would have been commercially unfavourable without the payable tax credit, then it is more likely that HMRC will challenge the application of the escape clause and, perhaps, more likely that a Tribunal or court will agree.

Finally, *Brebner* tells us (and HMRC) very clearly that purpose and effect must not be confused. Just because there is a tax advantage does not automatically mean that that advantage is a main purpose of the transaction(s).

9.4 Whose intention?

While individuals might have commercial purposes or might wish to avoid tax, it is a trite point that a company does not have a mind and cannot have a purpose of its own. This point was clarified in *Brebner*, where Lord Pearce said that:

> 'The "object" which has to be considered is a subjective matter of intention. It cannot be narrowed down to a mere object of a company, divorced from the directors who govern its policy or the shareholders who are concerned in and vote in favour of the resolutions … the company, as such, and apart from these, cannot form an intention.'

In *IRC v Addy* [1975] STC 601, another case involving a liquidation, Mrs Addy argued that she could not have had a tax avoidance motive, as she was not party to the decision to liquidate and took no part in the operations of the business, being only a minority shareholder. Mr Justice Goff in the High Court found this to be of no relevance, 'because what has to be applied is a subjective test of the intention of those in control'. He went on to suggest that 'those in control' might also include the professional advisers who had dreamed up the scheme. This theme was approved of by the Section 706 Tribunal in *Marwood Homes*, where the decision included the statement that the intention to be looked at is that of '… those who governed the policy of the company in the area where the transaction or transactions in question fall. This may involve looking at the intention of the directors, or the shareholders or, where appropriate, the professional advisers'.

This latter point causes some concern in that, if the advisers of a company are 'governing the policy of the company' in any area, it may be that they are acting as more than mere advisers and may be shadow directors. This should not be the case (and may even contravene company law), and perhaps a better formulation is that in some cases a company's policy is directed by the directors or shareholders but under the guidance of the advisers.

To reiterate, two principles are established by these decisions. First, as a company cannot have an intention, it is necessary to look at the intention of those making policy for the company, usually the directors or the shareholders. Second, ignorance of the scheme is not a defence for such as minority shareholders. If the intention of the scheme is to avoid tax, then the anti-avoidance provisions can apply, even if individual shareholders have no such intention (this is similar to decisions based on the *Ramsay* doctrine, too).

10 Clearances

Given the concerns of Parliament in 1960, the legislation was enacted with the facility for taxpayers ascertain in advance whether the HMRC is satisfied that no counteraction is required. This facility for 'clearance' is now found at TA 1988 s 707 / ITA 2007 s 701.

10.1 Form and content of the application

The application must be in writing (which includes email or fax, see below) and must give full details of the transactions to be carried out. Statement of Practice 13/1980 has some helpful information about the form and information required in any clearance application.

As a practical point, it is vital that the initial clearance application is complete in all material respects in order to avoid HMRC asking for further information, thus restarting the 30-day clock (see **10.5**). Equally important

Tax Digest Issue 81 Text.pmd 22 22/07/2009, 12:00

is clarity in the clearance application. The best letters are those that tell the story clearly, concisely and logically, so the inspector has all the information required to grant a clearance without further ado. A badly-written letter invites queries and therefore creates delay.

While clearance applications should be comprehensive, it is frequently the case that the final details are not decided until relatively late in the process. In such a case, it is preferable to make a clearance application earlier rather than later, also making a point of detailing the area(s) where decisions are yet to be finalised, together with the likely outcome. If the final decisions are materially different from what was originally advised to HMRC, a supplementary letter may be required to get final sign-off. Strictly, such a letter is a new application for clearance, but in circumstances like this the inspector will usually expedite the clearance on the basis that there are only minor differences to consider.

Although the legislation refers to transactions carried out by the applicant, it is important that the application includes details of any associated transactions carried out by others which might affect the relevance of the anti-avoidance provisions.

The application should as far as possible keep separate the transactions in securities (which should be listed in numbered paragraphs), the background information and evidence of *bona fide* commercial reasons or of the factors which indicate that the transactions will be carried out in the ordinary course of making and managing investments.

10.2 Disclosure

Should an application later be found not to have fully disclosed all the relevant facts, TA 1988 s 707(2) / ITA 2007 s 702(4) provide that inadequate disclosure makes any clearance void.

The importance of this was highlighted in the Special Commissioner's decision in the capital gains case of *Harding v HMRC* SpC 608. Mr Harding had applied for and been granted a pre-transaction clearance. But the clearance application had failed to mention the crucial aspects of the transaction that made it attractive for tax planning purposes. As the Special Commissioner said, the 'letter to the Revenue was, to be charitable, wholly inadequate for its purpose'.

This case emphasises that it is vital to give HMRC all relevant information when applying for a clearance, otherwise that clearance is void. At least if a clearance is refused, a transaction can be restructured to try and achieve a better result. But a transaction that has been carried out under an invalid clearance is irrevocable.

10.3 Meaning of a clearance

A clearance under TA 1988 s 707 / ITA 2007 s 702 states that HMRC is satisfied that no counteraction should be taken, given the facts and circumstances that have been disclosed. Where HMRC have given a clearance they are precluded from taking counteraction under TA 1988 s 703 / ITA 2007 s 698 in respect of the transactions notified in the clearance application. However, the clearance does not extend to arrangements which include the notified transactions along with other transactions not included in the application. Hence the importance of full disclosure of any associated transactions (see **10.1**).

Unlike clearances under, say, the capital gains reorganisation provisions (TCGA 1992 s 138, for example), such clearances do not specifically state that the Board is satisfied with the commercial reasons for the transaction, and so on. This can be helpful, as it allows applications for clearance to be made either on the basis that the transactions are carried out for *bona fide* commercial purposes and not to avoid tax – the more usual escape clause – but also where the taxpayer would like confirmation that the transactions do not technically fall into the provisions, perhaps because there is no transaction in securities, or none of the Circumstances is present.

10.4 Administration of clearances

Clearances are dealt with by the HMRC Clearance and Counteraction Team, which also deals with, *inter alia*, clearances under the following provisions:

(*a*) TA 1988 s 215 (demergers);

(*b*) TA 1988 s 225 (company purchase of own shares); and

(*c*) TCGA 1992 ss 138 and 139 (company reconstructions).

Most of the comments here will be relevant to clearance applications under other provisions, too, so should be taken as being of general use.

Applications for clearance under any of the relevant statutory provisions should be sent to:

Mohini Sawnhey
HM Revenue & Customs
Clearance & Counteraction Team
Anti-Avoidance Group (Intelligence)
1st Floor
22 Kingsway
LONDON
WC2N 6NR

Applications can be sent by e-mail to reconstructions@hmrc.gsi.gov.uk or by fax to 020 7438

Tax Digest Issue 81 Text.pmd 23 22/07/2009, 12:00

4409, as well as by post. However, only one method should be used to avoid confusion and double counting of applications.

If the transaction is market sensitive, it should be addressed to the Team Leader at the above address. You should telephone the Team Leader on 020 7438 6585 before you fax market-sensitive information. HMRC regards information that could affect the price of a stock market quoted company and information concerning the financial affairs of well-known individuals as sensitive in this context.

There is a great deal of helpful information available from the HMRC website about clearances, particularly:

- http://www.hmrc.gov.uk/cap/index.htm which explains about a number of areas where advice and clearances may be available;
- http://www.hmrc.gov.uk/pdfs/cop10.htm which contains a copy of Code of Practice 10. This Code of Practice tells about the different ways that HMRC will give information or advice, including clearances; and
- Statement of Practice 13 of 1980 (SP13/80) which is strictly about demerger clearances under TA 1988 s 215 but which has some helpful information about the form and information required in any clearance application. This can be found at http://www.hmrc.gov.uk/practitioners/sop.pdf which has all the Statements of Practice on one Acrobat document.

Practitioners and taxpayers should read this guidance carefully whenever they are making an application for clearance under any of the statutory provisions.

In general, HMRC will deal with simple applications as quickly as possible, usually within a few days of receipt, and there will be no separate acknowledgment of the application. HMRC will only issue a formal acknowledgement of an application if HMRC does not expect to deal with the application within a few days of receipt. This may happen if the Team is particularly busy or if the case is complex and requires more detailed thought. A letter of acknowledgement does not mean that HMRC is concerned about the application and wants to refuse clearance. It is just letting applicants know that their response may take a little time.

If you are enquiring about the progress of an application or making general enquiries, the contact number for Mohini Sawnhey, who deals with the administration of clearance applications, is 0207 438 8355.

10.5 Timing

The legislation gives HMRC the 30-days to give a substantive response to a clearance application, either be giving a decision or by requesting further information. If they request further information, the application technically lapses if that information is not supplied within 30 days. In practice, HMRC does not usually take this point and will reconsider the original application whenever the new information is received. After all, if it takes more than 30 days to supply the further information, the applicant can simply make a completely new application, including the further facts requested by the inspector. The decision must then be given within 30 days of HMRC receiving the information.

Given this timescale, it is important to consider clearance applications earlier rather than later when considering transaction timetables, to ensure that there is plenty of time to obtain clearance for a transaction before it is carried out. It is also important because it is not possible to rely on HMRC being willing to expedite a clearance for an imminent transaction, particularly at busy times when there are other clearance applications that may be getting close to the 30-day deadline.

If, exceptionally, HMRC fail to give a decision within 30 days of the application (or of the provision of further information) it should not be assumed that no counteraction can be taken. However, I am not aware of HMRC ever failing to give a substantive repose within the statutory 30 days.

Note that clearance applications can be made after the transaction has been carried out, as well as before, although one would generally assume that best practice would always be to seek clearance before carrying out a transaction.

10.6 Urgent applications

The most important thing about an urgent application is that it be clearly marked as urgent at the top of the front page of the letter. When clearance applications are initially received, they are allocated a reference number and passed to an inspector to deal with in date order. So no one will see a statement that the application is urgent at the end of the letter or hidden in the explanatory text until the inspector reads the letter in detail.

In my experience, the Clearance and Counteraction Team will always do its very best to comply with reasonable requests for urgent clearances, but it is also important to be aware of the other pressures on inspectors to process all applications within the 30-day time limit, particularly at busy times. So make sure your

Tax Digest Issue 81 Text.pmd 24 22/07/2009, 12:00

application really is urgent before taking this approach. If taxpayers or practitioners constantly demand quick turn-around times on what are essentially non-urgent cases, this is likely to be to the detriment of their relationship with the Clearance and Counteraction Team. This could make life very difficult for an adviser who regularly applies for clearance on behalf of clients.

Also, remember that inspectors are human too! There is nothing more annoying than being begged for an urgent clearance when it is clear that the transaction had been under consideration for some considerable time and the clearance application could and should have been made much earlier in the process.

10.7 Refusal of clearance

The legislation does not require HMRC to explain why an application for clearance has been denied. However, as a matter of practice, an applicant is always informed as to the area(s) of concern. This allows taxpayers to correspond with HMRC if clearance has been denied, in order to see if HMRC's concerns can be allayed. In practice, HMRC is usually willing to consider further comment or to opine on changes to the structure with a view to being able to grant clearance, whether on the originally proposed transaction or on a transaction that is less 'offensive'. Remember, however, as always, that HMRC's latitude is limited and also that their ability to respond swiftly is likely to depend upon how busy the inspectors are.

There is no formal route of appeal against a refusal of clearance by HMRC, in contrast to the procedure for demerger clearances (TA 1988 s 215) or capital gains (TCGA 1992 s 138 *et seq*); however, such a facility has been mooted in informal consultations with HMRC and the reaction was not entirely negative. As a practical matter the inspector will explain his or her concerns in the refusal letter and is likely to be willing to enter into further correspondence, or even discuss the case by telephone. As a result, it is frequently possible for taxpayers to amend transactions to remove the offending factors and to obtain the required clearance.

The refusal of a clearance does not automatically mean that counteraction will be taken, but it is not the practice of HMRC to refuse clearance unless, on the information available, they would expect to give serious consideration to taking counteraction if the transactions were to be carried out as described in the clearance application.

11 Information powers

HMRC have powers to require a taxpayer to provide information about transactions in securities, in order to determine whether these anti-avoidance provisions apply and that counteraction may be appropriate. The powers are at TA 1988 s 708 / ITA 2007 s 703 and the provision is at once both short and wide-ranging.

Where it appears to an HMRC officer that TA 1988 s 703 may apply to a company or that ITA 2007 s 684 may apply to a person, by reason of any transaction or transactions, that officer may issue a notice on that company or person requiring further specified information. That information must be in the possession of the company or person on whom it is served, and the information must be relevant to the question whether a counteraction notice should be served on that person.

The notice must also specify a period of time within which the information is to be provided, and that period cannot be less that 28 days for a company or 30 days for income tax purposes. The draft 2010 Corporation Tax Bill increases the minimum time limit to 30 days for companies, too.

Penalties may be imposed for failure to supply the required information, under TMA 1970 s 98.

This power to seek information is discretionary and must be used by HMRC reasonably, not misdirecting themselves as to the law, not taking into account irrelevant considerations nor failing to take into account relevant considerations. The exercise of this discretion by HMRC can be subject to judicial review if it amounts to an abuse of power.

The fact that enquiries are issued under this provision does not necessarily mean that counteraction will follow. Clearly it is possible that the information supplied may satisfy HMRC that there is no tax advantage which can be counteracted. However, if you or your clients receive such a notice, it is vital to ensure that the reasons for the transactions be explained fully and clearly in order to achieve a favourable outcome.

12 Counteraction

I am sure that we all fervently hope that none of our clients will be subject to counteraction under these provisions. However, it clearly happens occasionally, so it is important to be aware of the process and of your clients' rights and obligations throughout.

Tax Digest Issue 81 Text.pmd 25 22/07/2009, 12:00

The process of counteraction consists of a number of stages. Before all of these, of course, HMRC will have gathered the information required for making a decision about counteraction. They will either have used the powers discussed above, under TA 1988 s 708 / ITA 2007 s 703, or they will have got the information they need from a clearance application under TA 1988 s 707 / ITA 2007 s 701.

12.1 New Tribunal system

On 1 April 2009, the old system of General and Special Commissioners was replaced by the new two-tier unified tribunal system. This unified tribunal system also replaces the special tribunal (the 'TA 1988 s 706 / ITA 2007 s 704 Tribunal') established to consider certain cases under the Transactions in Securities legislation. In general terms, appeals that would have been heard by either the General or the Special Commissioners, or by the TA 1988 s 706 / ITA 2007 s 704 Tribunal, will now be heard by the Tax Chamber of the First-tier Tribunal. The detailed amendments to the legislation in TA 1988 Ch 1 Part 17 and ITA 2007 Ch 1 Part 13 are given in SI 2009/56. The primary legislation was changed by SI 2009/56, Schedule 2. See in particular paragraphs 150 et. seq. (regarding corporation tax) and paragraphs 456 et seq. (regarding income tax). The amended legislation is also now available on LexisNexis.

Although the primary legislation has been changed, HMRC has not yet issued any guidance as to how the new system will operate in the context of the Transactions in Securities legislation. I understand the matter is currently under review and that HMRC is aiming to release guidance later in 2009. For the moment, there is some useful information on the website of the Tribunals Service, at www.tribunals.gov.uk.

12.2 Preliminary notification

Once all the information has been gathered and a decision made that counteraction is probably required, HMRC must issue a notice under TA 1988 s 703(9) / ITA 2007 s 695. This is a preliminary notification that the person concerned is liable to counteraction and that a counteraction notice ought to be served.

This preliminary notification must detail the transaction or transactions concerned. However, there is no requirement to state which of the Circumstances is present or why HMRC considers that counteraction may be appropriate. In *Balen v IRC* [1977] STC 148 the Revenue notified the plaintiff that they had reason to believe that TA 1988 s 703 might apply in respect of certain specified transactions which they listed. The notification did not specify HMRC's reasons for their opinion. The plaintiff argued *inter alia* that the preliminary notification was null and void on the basis that natural justice dictates that a party against whom an allegation was made should have clear notice of the case he had to meet.

The court decided that the notification under TA 1988 s 703(9) was merely a triggering mechanism to put the taxpayer on notice that HMRC required an explanation. There was no reason why fairness should demand that HMRC should be compelled at the outset to do more than specify those transactions which had excited their interest or to tie themselves to making good a particular case when by statute they were not obliged to make any case at all. The notification followed literally the words of the statute and specified with sufficient precision the transactions in respect of which the taxpayer's contentions were invited, and was unobjectionable.

There is no formal appeal against a preliminary notification, so strictly the taxpayer must follow the prescribed statutory declaration procedure (see **12.3**). However, even at this late stage, it is to be hoped that the Clearance and Counteraction Team will be prepared to discuss their concerns about the transactions with the taxpayers, in order to reach an appropriate resolution.

12.3 The statutory declaration

TA 1988 s 703(9) / ITA 2007 s 696 requires the taxpayer to oppose the notification by a statutory declaration. I note in passing that there is no obvious policy reason why the statement of opposition to the preliminary notice should be by statutory declaration and this is one of the areas where some of us involved in simplification of anti-avoidance legislation would like to see a change.

The statutory declaration must 'state the facts and circumstances' whereby the taxpayer does not believe that they are liable to counteraction. It must be sent to the officer of HMRC who issued the preliminary notification, within 30 days of the issue of that notification.

If HMRC takes no further action, the person ceases to be liable to counteraction.

12.4 Submission to the Tribunal

If HMRC still wishes to proceed with a counteraction notice after receiving a statutory declaration from the affected person, the inspector is required to send to the Tax Chamber of the First-tier Tribunal a certificate to that effect, along with the statutory declaration. HMRC

Tax Digest Issue 81 Text.pmd 26 22/07/2009, 12:00

may also send a counter-statement, which one assumes will explain why they wish to proceed with the counteraction and why HMRC disagrees with the taxpayer's statutory declaration.

The function of the Tribunal in this respect is to take into account the declaration and the counter-statement and to determine whether there is a *prima facie* case for proceeding. If the Tribunal decides that there is no *prima facie* case for proceeding, HMRC cannot take counteraction.

HMRC has no right of appeal against the decision of the Tribunal. However, that decision only applies to the transactions that were the subject of that decision. HMRC is still entitled to consider counteraction in respect of arrangements which include some or all of the specified transactions if they also include one or more other transactions.

Strictly, the Tax Chamber has no authority to seek or consider information not in those documents, nor may the taxpayer or the Board address further arguments to them. This was challenged in *Wiseman v Borneman* 45 TC 540 as being contrary to natural justice and that the taxpayer should be given the opportunity to deal with the counter-statement or to address the Revenue's arguments. The House of Lords unanimously dismissed the taxpayer's appeals, on the ground that the procedure laid down by statute was not in all the circumstances unfair to the taxpayer. However, a majority of their Lordships indicated that in the proper circumstances the Tribunal had power, if it saw fit, to take appropriate steps to eliminate any unfairness in an exceptional case where material has been introduced of such a character that it would be unfair to decide upon it *ex parte*. That said, I am not aware of ever seeing this *obiter* tested in any later cases.

12.5 Formal notice of counteraction

Where a notification has been issued to a taxpayer and either he has not made a statutory declaration or the Tribunal has found a *prima facie* case for proceeding, the HMRC officer will issue a formal notice of counteraction specifying the adjustments which are to be made to counteract the tax advantage, under TA 1988 s 703(3) / ITA 2007 s 698. This notice must specify the adjustments to be made, which are limited to:

- an assessment;
- the nullifying of a right to repayment;
- the requiring of the return of a repayment already made; or
- the calculation or recalculation of profits or gains or liability to income tax or corporation tax.

Once again, there is no requirement for the notice to specify the Circumstance that applies or the grounds for HMRC's view that counteraction is required. Nor is there any obligation for HMRC to show the counter-statement to the taxpayer.

The HMRC officer will arrange for any necessary assessments or amendments to assessments to be made. No assessment may be made more than six years after the chargeable period (in the case of income tax, the year of assessment and in the case of corporation tax, the accounting period) to which the tax advantage relates.

Where counteraction is taken against an individual in Circumstance D or E, ITA 2007 s 699 limits the amount of tax which may be assessed. It is the amount of tax for which the individual would be liable if he received, on the date on which the vulnerable consideration was received, a qualifying distribution equal to the amount of the vulnerable consideration.

13 Appeals

When a notice of counteraction has been issued to a taxpayer, he has the right to appeal within 30 days, under TA 1988 s 705 / ITA 2007 s 705. The appeal may be on the grounds that TA 1988 s 703 / ITA 2007 s 684 does not apply to him in respect of the transaction or transactions in question, or that the proposed adjustments are inappropriate.

13.1 Internal review

However, since the counteraction notice is an appealable decision, the taxpayer is entitled to request HMRC to review the decision to issue the notice, or HMRC may of their own accord offer a review. This is under the new statutory internal review process detailed in TMA 1970 ss 49A-49I (also inserted by SI 2009/56).

If the taxpayer requests a review HMRC will then have 30 days to give their 'view' and a further 45 days to conduct the internal review and issue a decision on whether to uphold the counteraction notice. If HMRC offer a review of their own accord, they will just have the 45 days to conduct the review. The taxpayer would then have a further 30 days to notify an appeal against the counteraction notice to the Tax Chamber of the First-tier Tribunal.

Of course, if the individual or company concerned does not want an internal review, they can simply make the appeal directly to the First-tier Tribunal, within 30 days of the counteraction notice (see **12.5**).

Tax Digest Issue 81 Text.pmd 27 22/07/2009, 12:00

13.2 Appeal to the First-Tier Tribunal (Tax Chamber)

The procedure as regards an appeal is in general similar to that for an appeal against an assessment. The general principle is that the appeal will be heard by the Tax Chamber of the First-tier Tribunal. There is scope in certain circumstances for appeals to be transferred directly to the Upper Tribunal, but this is not discussed in detail here, as it is assumed that almost all appeals against counteraction notices will be dealt with by the First-tier Tribunal. If you are involved in a case where it is suggested that the appeal should be heard by the Upper Tribunal, you are advised to seek advice from a tax litigation specialist (as, indeed, you should in any appeal to either Tribunal).

Appeals to the First-tier Tribunal are categorised according to their complexity. The categories are 'default paper', 'basic', 'standard' or 'complex'. A full discussion of these categories is beyond the scope of this *Tax Digest* but readers might like to read the booklet *Making an Appeal*, available at http://www.tribunals.gov.uk/tax/Documents/MakinganappealWEB.pdf. Default paper hearings usually do not require a hearing, and an appeal against a counteraction notice is unlikely to fall into this category. Basic cases only require an informal hearing and, again, an appeal against a counteraction notice is unlikely to fall into this category. So appeals against counteraction notices are most likely to be categorised as standard or complex.

As noted above, HMRC will not have previously been required to share any of its concerns with the taxpayer. The exact level of disclosure by HMRC will depend on the category to which the case is allocated. As most cases involving Transactions in Securities will fall in the 'Standard' or 'Complex' categories, the taxpayer will be provided with a Statement of Case setting out HMRC's case. The taxpayer will then be able to file a 'reply' addressing the issues raised in this.

On an appeal, the Tax Chamber has the power to affirm, vary or cancel the counteraction notice under TA 1988 s 703(3) / ITA 2007 s 698 or to affirm, vary or cancel any assessment made in accordance with that notice. However, appealing against the notice does not affect the validity of anything done in consequence of that notice pending determination of the appeal. So it is necessary to make a separate appeal against any assessment which may have been made as part of the counteraction.

There is no appeal from a determination by the Tax Chamber on a question of fact, only on a point of law.

Under the old system, there was a facility to have the case re-heard by the special tribunal (convened under TA 1988 s 706 / ITA 2007 s 704), if either party was dissatisfied with the decision of the Special Commissioners. However, this facility has been withdrawn. This is not entirely a surprise as there was consultation on this point a few years ago, and the facility for a complete re-hearing of a case seems to have been used only two or three times since the enactment of this legislation in 1960.

13.3 Appeal to the Upper Tribunal (Finance and Tax Chamber)

After a determination by the Tax Chamber of the First-tier Tribunal, the taxpayer or HMRC officer may declare dissatisfaction with the determination on a point of law. They may, within 56 days of the determination, request leave to appeal to the Upper Tribunal. If permission is not given by the First-tier Tribunal, a request for leave to appeal can be made to the Upper Tribunal within one month of the First-tier Tribunal refusing permission to appeal.

While appeals to the Upper Tribunal are pending, tax must be paid in accordance with the determination of the Tax Chamber of the First-tier Tribunal. If the amount payable is reduced by the order of the Upper Tribunal, the tax, and interest determined by the Tribunal, must be repaid. If the amount due is increased, HMRC must issue a notice of the further amounts to be paid. Payment is then due within 30 days of the date the notice is issued.

13.4 Appeal to the Court of Appeal and the House of Lords (or Supreme Court)

Appeals against a decision of the Upper Tribunal lie to the Court of Appeal, with permission from the Upper Tribunal or the Court of Appeal. Similarly, appeals to the House of Lords require the permission of the Court of Appeal or of the House of Lords Appellate Committee. The income tax legislation (at ITA 2007 s 710) refers to the Supreme Court, which will replace the Appellate Committee of the House of Lords as the highest court of appeal, probably from October 2009. However the jurisdiction of the House of Lords is maintained until this happens.

13.5 Scotland and Northern Ireland

The new unified tribunals system applies to the whole of the UK. However the (English) Court of Appeal usually only hears appeals on English matters. The legislation requires the Upper Tribunal to determine which of the Court of Appeal in England and Wales, Court of Session in Scotland or Court of Appeal in Northern Ireland is the most 'appropriate' to hear the appeal and to send the appeal there. Appeals from any of these courts go to the House of Lords (or Supreme Court once established).

Tax Digest Issue 81 Text.pmd 28 22/07/2009, 12:00

14 The future of the legislation

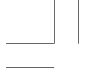
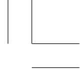
The Government and HMRC remain committed to eradicating what they see as tax avoidance. It seems likely, therefore, that these provisions will remain in force for some time to come, particularly as the rates of tax on gains remain lower than those on income. However, there are some areas where some change is likely.

First, as we saw above, the UK tribunal system has undergone a major overhaul and the revised, two-tier tribunal system incorporates all the current tax tribunals, including the Special Commissioners. However, the right to have an appeal against a counteraction notice reheard by the successor to the TA 1988 s 706 / ITA 2007 s 704 Tribunal has not survived the change. It is also possible that other changes in the administration of this legislation will follow.

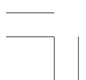
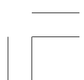
Secondly, with the rewrite of income tax legislation, there are now both income tax and corporation tax versions of the provisions. While they are almost identical in meaning (and in wording, once CTA 2010 becomes law), having two versions means that there is scope for divergence over time between the income tax and corporation tax versions.

Finally, HMRC has been consulting on anti-avoidance legislation more generally, with a view both to simplifying the legislation and to make it more 'fit for purpose'. Early consultation exercises suggested that this particular legislation divided opinions: some people think that it is well understood and that it does not require radical change, others that it is convoluted and out of date and something different is required. We understand that a Consultation Document may be issued during the summer of 2009.

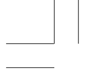
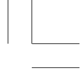
Tax Digest Issue 81 Text.pmd 29 22/07/2009, 12:00

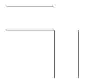
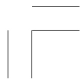
Notes

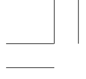
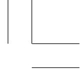
Tax Digest Issue 81 Text.pmd 30 22/07/2009, 12:00

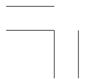
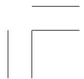
Notes

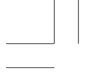
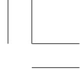
Tax Digest Issue 81 Text.pmd 31 22/07/2009, 12:00

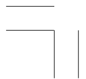
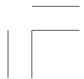
Notes

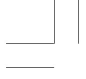
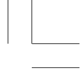
Tax Digest Issue 81 Text.pmd 32 22/07/2009, 12:00

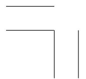
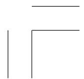
Notes

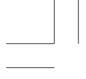
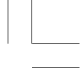
Tax Digest Issue 81 Text.pmd 33 22/07/2009, 12:00

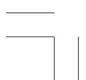
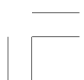
Notes

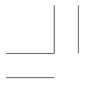
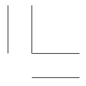
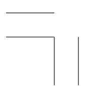
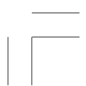
Tax Digest Issue 81 Text.pmd 34 22/07/2009, 12:00

Notes

Tax Digest Issue 81 Text.pmd 35 22/07/2009, 12:00

Tolley's Tax Digest

Three good reasons to subscribe:

1 **Expert guidance on all the key topics –** and we cover all the new hot topics, such as alignment of trusts, taxation of non-UK domiciliaries and foreign profits.
2 **Quality assured –** each digest is written by a leading practitioner to give you the best possible guidance. Authors include tax partners at leading firms, former Presidents of the CIOT and ATT (including John Whiting, Robert Jamieson and Andrew Hubbard), along with leading Tax Barristers and many more.
3 **Amazing value –** pay around £16 per digest if you subscribe (12 issues for £197) – a fraction of the cost of other publications – or order individual digests for only £40 each.

Back issues

Recent back issues of Tolley's Tax Digest are also available for £40 per copy.
Please contact LexisNexis Customer Services on:
tel: 0845 370 1234 fax: 020 8662 2012 email: customer.services@lexisnexis.co.uk

TTD Issue 50	–	The New Construction Industry Scheme	(December 2006)
TTD Issue 51	–	Employment-related Securities	(January 2007)
TTD Issue 52	–	Inheritance Tax Planning – Common Scenarios	(February 2007)
TTD Issue 53	–	Fiscal Share Valuation	(March 2007)
TTD Issue 54	–	Expatriate Tax	(April 2007)
TTD Issue 55	–	Property Taxes	(May 2007)
TTD Issue 56	–	HMRC Enquries and Investigations	(June 2007)
TTD Issue 57	–	VAT Schemes for a Registered Business	(July 2007)
TTD Issue 58	–	Finance Act 2007 – Practical Aspects	(August 2007)
TTD Issue 59	–	Incorporation, Disincorporation and Related Issues	(September 2007)
TTD Issue 60	–	Taxation of Non-resident Trusts	(October 2007)
TTD Issue 61	–	Capital Gains Tax Planning	(November 2007)
TTD Issue 62	–	Capital Allowances	(December 2007)
TTD Issue 63	–	Group Tax Planning	(January 2008)
TTD Issue 64	–	HMRC Powers	(February 2008)
TTD Issue 65	–	Loan Relationships	(March 2008)
TTD Issue 66	–	Employment Taxes: Latest Developments	(April 2008)
TTD Issue 67	–	The New Entrepreneurs' Relief	(May 2008)
TTD Issue 68	–	First Steps Abroad By An SME	(June 2008)
TTD Issue 69	–	The New Remittance Rules	(July 2008)
TTD Issue 70	–	Finance Act 2008 – Practical Aspects	(August 2008)
TTD Issue 71	–	Tax On Company Reorganisations	(September 2008)
TTD Issue 72	–	Inheritance Tax Planning Post FA 2008	(October 2008)
TTD Issue 73	–	Partnership Taxation	(November 2008)
TTD Issue 74	–	Substantial Shareholdings Exemption	(December 2008)
TTD Issue 75	–	Tax Relief on Research and Development Expenditure	(January 2009)
TTD Issue 76	–	Tax Implication Of Trusts	(February 2009)
TTD Issue 77	–	Completing Expenses and Benefits Returns	(March 2009)
TTD Issue 78	–	Private Residence Relief	(April 2009)
TTD Issue 79	–	Taxation Of Foreign Profits Review	(May 2009)
TTD Issue 80	–	Appeals to the Tax Tribunals	(June 2009)
TTD Issue 81	–	Transactions in Securities	(July 2009)

The next issue is on Finance Act 2009.

Get Tolley’s Tax Digest hot off the press!

By filling in and returning the attached order form, you will ensure immediate delivery of each new issue as soon as it is published.

Each month you will receive around 30 pages of practical, detailed guidance relating to a specific area of tax. A subscription to **Tolley’s Tax Digest** will provide you with all you need to know on the most important tax topics, such as taper relief, incorporation, the taxation of trusts, and tax planning on retirement. Written by well-known specialists in each area and edited by the **LexisNexis Tolley** editorial team, you can be sure that the information will be of the highest quality. Each Digest can be stored in a FREE BINDER, which will be sent to you when you first subscribe. Individual Digests can also be purchased for £40.

Price: £197.00 for 12 issues

Individual Digests can also be purchased for £40

Subscribe today and receive

Tolley’s Tax Digest delivered to your desk every month plus a FREE binder.

1 Order Details

Product Details	Unit Price	Total
Tolley’s Tax Digest ISSN 1 478 4653 Product code TTD	£197.00	
	Total amount due	£

Orders are subject to a charge of £5.45 p&p in the UK. Overseas customers will be charged at the current p&p rate for their delivery zone; please call +44 (0) 845 370 1234. VAT where applicable will be added. Prices are subject to change without notice.

Pay As You Go (PAYG)

Do you wish to receive this publication each time it is published? Please indicate your choice:

☐ Yes. I understand that I will continue to receive, until countermanded, future editions and will be invoiced for these when I receive them.

☐ No. I do not wish to receive future editions of these publications unless ordered.

There may be updated by supplements between editions, when purchasing the main work customers will be automatically sent the updating supplement on publication. All orders placed with us are subject to our standard terms and conditions of trade, available on request and on the invoice. Our products are intended to be general reference guides to the law and cannot be substitutes for legal advice.

2 Delivery Details *Required Fields

*Title ______

*First name ______

*Surname ______

*Job Title ______

*Phone ______

*Email address ______

Company name ______

Department ______

*Address ______

______

______

*Postcode ______

3 Your Payment Choice

- Account no. ☐☐☐☐☐☐☐☐
- ☐ Mastercard ☐ Amex ☐ Visa Exp. date ______

☐ Switch/Maestro/Delta Start date ______ Exp. date ______

Card no. ______ Issue no. ______

- Cheque payable to **LexisNexis** for £ ______

VAT reg. no. ______

4 Order Authorisation

Signature ______

Print name ______ **Date** ______

If you DO NOT wish to be kept informed by mail ☐ phone ☐ fax ☐ email ☐ of other LexisNexis Butterworths products and services, please tick the box.

☐ If you do NOT wish your contact details to be passed on to companies approved by LexisNexis, to keep you informed of their products and services, please tick the box. For details of our privacy policy please visit our website at: www.lexisnexis.co.uk/contact_us/privacypolicy.html

5 Return Your Order

- **Freepost** Marketing Department, LexisNexis, Freepost (6983), London WC2A 1BR
- **Phone** +44 (0)845 370 1234 • **Fax** +44 (0)20 7400 2570

30 Day Money Back Guarantee

Products can be returned for refund within 30 days according to the following conditions:

- All returns must be accompanied by the invoice and a valid authorisation code.
- No returns can be accepted after 30 days following date of invoice
- All goods returned must be in re-saleable condition

Please quote response code 5067

35 Chancery Lane, London WC2A 1EL
A division of Reed Elsevier (UK) Ltd
Registered office 1-3 Strand London WC2N 5JR
Registered in England number 2746621
VAT Registered No. GB 730 8595 20

LexisNexis and the Knowledge Burst logo are trademarks of Reed Elsevier Properties Inc.

ISSN 1478-4653

0109-069/SE/CE/0108