Neutral Citation Number: [2015] EWHC 2884 (Ch)

Case No: HC03C00446

IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION

Rolls Building
Royal Courts of Justice
Fetter Lane, London, EC4A 1NL

Date: 14/10/2015

Before:

MR JUSTICE HENDERSON

- -

Between:

(1) SIX CONTINENTS LIMITED **(2) SIX CONTINENTS OVERSEAS HOLDINGS LIMITED**	**Claimants**
- and -	
(1) THE COMMISSIONERS OF INLAND REVENUE **(2) THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS**	**Defendants**

- -

Mr Jonathan Bremner (instructed by **Joseph Hage Aaronson LLP**) for the Claimants
Mr Rupert Baldry QC and Mr Oliver Conolly (instructed by **the General Counsel and Solicitor for HMRC**) for the Defendants

Hearing date: 20 July 2015

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Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

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MR JUSTICE HENDERSON

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Introduction

1. This is an application for summary judgment, or alternatively for an interim payment, brought by the second claimant Six Continents Overseas Holdings Limited ("Six Continents") against the Defendants ("HMRC" or "the Revenue").

2. Six Continents is enrolled as a member of the Controlled Foreign Company ("CFC") and Dividend Group Litigation Order ("GLO"), but the CFC component of its claim was settled in 2012, and the claim in its present form relates only to certain dividends paid to Six Continents in the accounting periods ending 30 September 1993, 1996 and 1997 respectively ("the Dividends") by its wholly-owned Dutch subsidiary, Six Continents International Holdings BV ("SCIH"). More specifically, Six Continents seeks to recover corporation tax under Case V of Schedule D which it says was levied on the Dividends in breach of EU law, together with compound interest from the dates when the tax was paid until judgment. The claim relies on the Woolwich and mistake-based restitutionary causes of action in English law, as they have been developed and applied in the context of the Franked Investment Income ("FII") group litigation over the last decade so as to provide the test claimants in that group litigation with an effective remedy for recovering tax which the Court of Justice of the European Union ("the ECJ") has held to be unlawfully levied.

3. Six Continents is not, as it happens, enrolled in the FII GLO, but HMRC no longer argue that this disentitles Six Continents from relying on the principles established in the FII group litigation in relation to the Dividends, or that it gives rise to any kind of procedural impediment. An argument to this effect was considered and rejected by Sir Andrew Park on an earlier application for an interim payment in the present case in 2009: see Six Continents Ltd and others v HMRC [2009] EWHC 1822 (Ch) at [11] to [15]. Nor is any point now taken by the Revenue about the jurisdiction of the High Court, rather than the Tax Chamber of the First-tier Tribunal, to entertain the claim, given that Six Continents' appeals to the Tribunal for the three relevant accounting periods have long since been finally determined and the years in question are therefore now "closed".

4. This judgment assumes familiarity with the complex history of the FII group litigation, including in particular the decisions of the ECJ upon the first and second references, the English liability proceedings in the High Court, Court of Appeal and Supreme Court, and the lengthy quantification trial in which I handed down judgment on 18 December 2014: see Test Claimants in the FII Group Litigation v Revenue and Customs Commissioners [2014] EWHC 4302 (Ch), [2015] STC 1471 ("FII (High Court) II"). In general, I will without further explanation use the same definitions, abbreviations, and so forth as I have adopted in earlier cases in the series.

5. At the hearing of the application on 20 July 2015 Six Continents was represented by Mr Jonathan Bremner, while Mr Rupert Baldry QC leading Mr Oliver Conolly appeared for HMRC. I am grateful to counsel on both sides for their clear and concise submissions.

Background

6. There is no dispute about the factual background, which is conveniently summarised in Mr Bremner's skeleton argument upon which the following account is largely based.

7. Six Continents was incorporated in England and Wales in 1991. In March 1992, it changed its name to Bass Overseas Holdings Limited, and in August 2001 it acquired its present name. Together with its immediate UK parent, Six Continents Limited, it is a member of the InterContinental Hotels Group of companies ("the IHG Group"). The IHG Group operates in the international hotel business across nearly one hundred countries. In the UK, the IHG Group is a successor to the Bass Plc group.

8. Between 1989 and 1991, the Bass Plc group expanded into the international hotel business with the acquisition of the Holiday Inn Group. Six Continents (under its then name of Bass Overseas Holdings Limited) was the UK holding company for this international group. It was arranged that SCIH (then known as Bass International Holdings BV) would hold the non-UK interests.

9. At the material times, dividend income of a UK-resident parent company (such as Six Continents) from subsidiaries resident outside the UK (such as SCIH), including those resident in other EU Member States, was subject to UK corporation tax under Case V of Schedule D. In contrast, dividend income received by a UK parent company from its UK-resident subsidiaries was exempt from corporation tax: section 208 of ICTA 1988.This was the basic feature of the UK corporate taxation regime which (as the ECJ held in the FII group litigation) led to Six Continents being subjected to discriminatory treatment in comparison to a UK-resident parent company with UK-resident subsidiaries.

10. During the three accounting periods which I have mentioned, Six Continents received the Dividends from SCIH. The source of the Dividends was a mixture of SCIH's own profits and dividends received from its Dutch-resident subsidiaries, Holiday Inns International BV and Bass Continental Finance NV. It is agreed that all of the relevant profits were of either Dutch or Belgian origin.

11. The Belgian profits were those of a Belgian coordination centre, which was a branch of Holiday Inns International BV. For the nature of Belgian coordination centres, and the computation of the appropriate tax credit at the Belgian nominal rate of tax on their distributed profits, see FII (High Court) II at [82] to [90]. There is now no dispute between the parties about how the income of the Belgian coordination centre in the present case should be treated.

12. The claim form was issued on 3 February 2003, and the claim in its present form is set out in the fourth amended particulars of claim dated 7 December 2012. Six Continents seeks to recover the unlawfully levied Case V tax which was paid in respect of the Dividends. By May 2009, Six Continents' advisers considered that it was bound to succeed on this part of its claim, and that it would therefore obtain judgment for a substantial sum of money against HMRC. Accordingly, on 11 May 2009, Six

Continents issued an application for an interim payment in relation to that part of its claim. The application was granted by Sir Andrew Park, who by his order dated 22 July 2009 ordered HMRC to pay Six Continents the aggregate amount of approximately £13.55 million.

13. Following the judgment of the Court of Appeal in FII (CA) in February 2010, which referred the question of the lawfulness of the Case V charge to the ECJ , and also reversed my conclusions on limitation in FII (High Court) I, Six Continents voluntarily repaid to HMRC the entire interim payment together with compound interest between the date of payment and the date of repayment.

14. In May 2012, the Supreme Court reversed the Court of Appeal's judgment on various limitation issues and concluded that for claims issued before 8 September 2003 (which therefore included Six Continents' claims) a claimant could rely upon the extended limitation period in section 32(1)(c) of the Limitation Act 1980. The impact of this reversal in the present case is in fact relatively limited, because only the first of the Dividends (in 1993) was paid more than six years before the issue of the claim form, and the amount claimed in relation to that dividend is only £177,366.37 (together with interest).

15. More importantly for present purposes, on 13 November 2012 the ECJ handed down its judgment on the second reference in FII (ECJ) II. In broad outline, it held that the Case V charge infringed EU law and was therefore unlawful, but that the UK system for taxing foreign dividends might have been lawful if it had provided (at least) for a credit at the relevant foreign nominal rate ("FNR") of tax. I have subsequently done my best to interpret and apply the ruling of the ECJ, both in relation to portfolio dividends (in Portfolio Dividends (No 2), The Prudential Assurance Co v HMRC, [2013] EWHC 3249 (Ch), [2014] STC 1236), and in relation to dividends received from subsidiaries (in FII (High Court) II).

16. In the light of the judgments of the Supreme Court and of the ECJ on the second reference, on 13 May 2013 Six Continents issued an application for an interim payment in the amount of £12,870,000. In effect, this application sought to reinstate the original 2009 interim payment ordered by Sir Andrew Park, upon the same terms as it had been granted. The application pre-dated the entry into force (with effect from 26 June 2013) of the restriction now contained in section 234 of the Finance Act 2013 on interim remedies against HMRC relating to a tax matter.

17. HMRC responded to the application in letters of 1 August and 25 September 2013, setting out a number of objections and a number of points upon which they required further information and evidence. These requests were answered on 28 October 2013. Six Continents then formed the view that HMRC had no reasonable grounds upon which to resist the application, and on 13 September 2013 the application notice was amended so as to apply, in the alternative, for summary judgment. This has now become its primary application.

18. The hearing of the applications was then postponed until after delivery of the judgments in Portfolio Dividends (No 2) and FII (High Court) II. After the handing down of those judgments, a case management conference took place on 30 January 2015, following which the present hearing was listed. Meanwhile, the parties exchanged further evidence to take account of the rulings in those two cases and to re-compute the claim

accordingly. Discussions on various points continued between the parties, and gave rise to further witness statements on each side in July 2015. No objection was taken to the admission of any of this evidence.

19. Finally, I should mention that on 16 June 2015 Six Continents issued and served, on a protective basis, a further application notice seeking summary judgment (or, in the alternative, an interim payment) on the same basis as the original application of May 2013. This step was taken to meet a technical objection previously taken by HMRC, that the original application was premature because it had been issued before service by HMRC of their defence on 25 October 2013. In my view the objection would have had no merit, had it been pursued, because CPR 24.4(2) merely provides that if a claimant applies for summary judgment before the defendant against whom the application is made has filed a defence, "that defendant need not file a defence before the hearing". However, the issue of the further application put the matter beyond any possibility of doubt.

The Law

(1) Summary Judgment

20. CPR 24.2 provides that:

> "The court may give summary judgment against a … defendant on the whole of a claim or on a particular issue if –
>
> "(a) it considers that –
>
> …
>
> (ii) that defendant has no real prospect of successfully defending the claim or issue; and
>
> (b) there is no other compelling reason why the case or issue should be disposed of at a trial."

21. The principles that the court should apply in deciding whether a defendant has no real prospect of successfully defending the claim are well known, and have been set out in a number of recent cases. Both sides referred me to the summary adopted by Popplewell J in F G Wilson (Engineering) Ltd v John Holt & Co (Liverpool) Ltd [2012] EWHC 2477 (Comm), [2013] 1 All ER (Comm) 223, at [20], from which I cite the following extracts (omitting the references to authority):

> "(1) the court must consider whether the defendant has a "realistic" as opposed to a "fanciful" prospect of success…;
>
> (2) a "realistic" defence is one that carries some degree of conviction. This means a defence that is more than merely arguable…;

> (3) in reaching its conclusion the court must not conduct a "mini-trial"…;
>
> (4) this does not mean that the court must take at face value and without analysis everything that a defendant says in his statements before the court…
>
> (5) however, in reaching its conclusion, the court must take into account not only the evidence actually placed before it on the application for summary judgment, but also the evidence that can reasonably be expected to be available at trial…
>
> (6) although a case may turn out at trial not to be really complicated, it does not follow that it should be decided without the fuller investigation into the facts at trial than is possible or permissible on summary judgment. Thus the court should hesitate about making a final decision without a trial, even where there is no obvious conflict of fact at the time of the application, where reasonable grounds exist for believing that a fuller investigation into the facts of the case would add to or alter the evidence available to a trial judge and so affect the outcome of the case…;
>
> (7) on the other hand it is not uncommon for an application under Part 24 to give rise to a short point of law or construction and, if the court is satisfied that it has before it all the evidence necessary for the proper determination of the question and that the parties have had an adequate opportunity to address it in argument, it should grasp the nettle and decide it. The reason is quite simple: if the respondent's case is bad in law, he will in truth have no real prospect of succeeding on his claim or successfully defending the claim against him, as the case may be…"

(2) Interim payment

22. CPR 25.7(1) provides that the court may make an order for an interim payment if:

> "(c) it is satisfied that, if the claim went to trial, the claimant would obtain judgment for a substantial amount of money (other than costs) against the defendant from whom he is seeking an order for an interim payment…"

By virtue of rule 25.7(4), "[t]he court must not order an interim payment of more than a reasonable proportion of the likely amount of the final judgment."

23. The approach to be followed by the court on an application under rule 25.7(1)(c) has been authoritatively considered by the Court of Appeal, when dismissing an appeal brought by the Revenue from an interim payment awarded by Sir Andrew Park to the GKN Group, which was a non-test claimant in the FII GLO: see Revenue and Customs Commissioners v GKN Group [2012] EWCA Civ 57, [2012] STC 953. The leading judgment was delivered by Aikens LJ, who at [32] identified three points of

construction which arise from rule 25.7(1)(c): first, what is meant by "…[*the court*] is satisfied that…"; secondly, what is meant by "…if the claim went to trial the claimant would obtain judgment for…"; and, thirdly, what is meant by "…a substantial amount of money…"?

24. Aikens LJ continued:

> "33. On the first point, it is obvious that the claimant seeking the interim payment has the burden of satisfying the court that the necessary conditions have been fulfilled for it to consider exercising the power to grant an interim payment order. An interim payment order is one that is obtained in civil proceedings. Whatever conditions have to be satisfied must be to the usual *standard* of proof in civil proceedings unless there is an express indication in a statute or rule of court to the contrary. Here there is none. Therefore the claimant has to satisfy the court that the requisite conditions have been fulfilled to the civil standard, which is upon the balance of probabilities…
>
> …
>
> 36. That leads on to the next and more important question: of what does the claimant have to satisfy the court? To which the answer is: that if the claim went to trial, the claimant would obtain judgment for a substantial amount of money from this defendant. Considering the wording without reference to any authority, it seems to me that the first thing the judge considering the interim payment application under para (c) has to do is to put himself in the hypothetical position of being the trial judge and then pose the question: would I be satisfied (to the civil standard) on the material before me that this claimant would obtain judgment for a substantial amount of money from this defendant?
>
> …
>
> 38. The second point is what precisely is meant by the court being satisfied that, if the claim went to trial, the claimant "would obtain judgment for a substantial amount of money"? In my view this means that the court must be satisfied that if the claim were to go to trial then, on the material before the judge at the time of the application for an interim payment, the claimant would actually succeed in his claim and furthermore that, as a result, he would actually obtain a substantial amount of money. The court has to be so satisfied on a balance of probabilities. The only difference between the exercise on the application for an interim payment and the actual trial is that the judge considering the application is looking at what would happen if there were to be a trial on the material he has before him, whereas a trial judge will have heard all the evidence that

> has been led at the trial, then will have decided what facts have been proved and so whether the claimant has, in fact, succeeded… the Court must be satisfied (to the standard of a balance of probabilities) that the claimant *would* in fact succeed on his claim and that he *would* in fact obtain a substantial amount of money. It is not enough if the court were to be satisfied (to the standard of a balance of probabilities) that it was "likely" that the claimant would obtain judgment or that it was "likely" that he would obtain a substantial amount of money.
>
> 39. Next there is the question of what is meant by "a substantial amount of money". In my view that phrase means a substantial, as opposed to a negligible, amount of money. However, that judgment has to be made in the context of the total claim made…"

25. In Heidelberg Graphic Equipment Ltd v Revenue and Customs Commissioners [2009] EWHC 870 (Ch), [2009] STC 2334, I held at [16] that the notional trial posited by the rule has to be regarded as taking place in the state of the law which obtains at the date when the application for an interim payment is made. I said:

> "Anything else would, in my view, involve a wholly unrealistic and speculative exercise in crystal ball gazing, which would involve not only the court taking a view as to how long the matter would take to come to trial, but also as to what might or might not happen to various appeals on questions of law during the interim period. That is not to say that the existence of an appeal should be totally disregarded, but as a matter of general principle I think the focus has to be on the law as it is at the date of the application, rather than at the probable time of a hypothetical future trial of the action."

26. I also stressed, at [28], that an order for an interim payment is not irreversible. If the party against whom the order is made eventually succeeds at trial, the interim payment will be repayable, together with interest. In each of the Heidelberg case, the interim payment orders made in the FII group litigation, and the interim payment order made by Sir Andrew Park in the present case in 2009, this obligation has been fortified by an undertaking given by the parent company of the UK group. There is no dispute that such an undertaking should also be given on the present application, if I make an order for an interim payment rather than summary judgment.

Summary judgment or interim payment?

27. Unsurprisingly, Six Continents' preference would be to obtain an order for summary judgment. Not only would this obviate the need for a trial, but (subject to any appeal) the order would have the benefit of finality. Six Continents therefore submits that HMRC have no real prospect of successfully defending the claim, and that there is no other compelling reason why the case should go to trial.

28. HMRC submit, however, that the application for summary judgment is misconceived, for two main reasons. First, the claim is necessarily founded to a large extent on complex issues of law for which permission to appeal to the Court of Appeal has been granted following the judgment in FII (High Court) II. Until the Revenue's appeals on those issues have been determined, it cannot be said that HMRC have no real prospect of successfully defending the claim. Secondly, the present claim also raises important issues which were not directly determined in FII (High Court) II but which are of a broadly similar nature, and must at this stage be regarded as offering a realistic (as opposed to fanciful) prospect of success.

29. In support of these submissions, Mr Baldry QC points out that the test for the grant of permission to appeal in CPR 52.3(6)(a), namely that "the appeal would have a real prospect of success", is exactly the same test as that which the courts apply when considering claims for summary judgment under rule 24.2(a)(i). As the notes in the White Book, volume 1, point out at paragraph 52.3.7 (p 1882):

> "The rationale is the same. If a claim or defence has no real prospect of success, the court will prevent the litigant from pursuing it. Likewise if an appeal has no real prospect of success, the court will prevent the litigant from pursuing it."

30. The relevant issues under appeal in FII (High Court) II, with permission which I granted at a hearing to deal with consequential matters on 30 January 2015, include whether I erred in law:

    (a) in my approach to "mixed" dividend streams, holding that where necessary a weighted average of the FNRs of the jurisdictions where the income had been subject to tax should be applied, following the system of section 821 of ICTA 1988;

    (b) in my approach to the Dutch participation exemption, and the gains realised on the sale of Henri Wintermans (see FII (High Court) II at [75] to [81]);

    (c) in holding that the defence of change of position to the mistake-based claims had not been made out, and that HMRC were anyway precluded from relying on the defence under EU law;

    (d) in my approach to HMRC's "actual benefit" argument in respect of the mistake claims (see FII (High Court) II at [416] to [430]); and

    (e) in holding that interest ought to be compound, and dismissing the Revenue's argument that the test claimants were only entitled to simple interest under section 35A of the Senior Courts Act 1981.

31. Consistently with the grant of permission to appeal on these issues, submits Mr Baldry, there must be a real prospect that the final determination of the FII litigation will give rise to a materially different outcome than under FII (High Court) II. In those circumstances, if summary judgment were now granted, HMRC would be compelled to pay out on a claim which might subsequently be found to have been excessive. Six Continents recognises that there is a potential problem here, because it

says in paragraph 23 of its skeleton argument that the Revenue's position can be protected by being granted permission to appeal so as to guard against a change in the law. But, says Mr Baldry, this amounts to an acknowledgment that HMRC have a real prospect of successfully defending the claim. He adds that it would in any event be inconsistent with the scheme of the GLO procedure that multiple appeals should be made to the Court of Appeal, pending the outcome of the test claims chosen to test the issues in dispute.

32. Turning now to issues raised by the present claim which were not directly determined in FII (High Court) II, Mr Baldry submits that they include:

(a) the appropriate FNR to apply to dividends paid by Dutch mixer companies which have blended dividends some of which have and some of which have not been subject to tax within the EU;

(b) the question whether revaluation adjustments made by a Dutch company which benefits from the participation exemption are profits subject to tax for the purposes of the test laid down in FII (High Court) II;

(c) the question whether gains on a liquidation received by such a Dutch company are likewise profits subject to tax for the purposes of the same test; and

(d) the question whether a dividend paid by SCIH out of a return of share premium accounts engages and breaches the EU law rights of Six Continents.

33. More generally, Mr Baldry submits that summary judgment is inappropriate, even if it is not ruled out in principle. The present case raises issues about whether the Dutch FNR should be applied to underlying profits in respect of which a credit is claimed. There are complex questions of fact and foreign law, which are not suitable for determination by way of summary judgment. Furthermore, because the claimant is not enrolled in the FII GLO, any factual findings made in the test claim in FII (High Court) II are not binding on the parties to the present application.

34. By contrast, the Revenue accept that, subject to the three substantive issues which I will discuss later in this judgment, and on the basis of the law as it now stands, Six Continents is entitled to an interim payment in respect of part of its claim. That part is quantified by the Revenue in the sum of £1,564,722.88, which together with compound interest comes to £4,076,516. This sum: (a) is calculated on the basis that the parts of the Dividends sourced from revaluation adjustments, participation exemption profits on a liquidation, and the return of share premium, are not subject to tax in the Netherlands under the law as it now stands; (b) includes interest on a compound basis; (c) ignores the change of position defence; and (d) accepts that (in accordance with FII (High Court) II) the gain on the sale of shares in a subsidiary of SCIH, BIF NV, was subject to tax in the Netherlands. The Revenue make no concessions in respect of any of these issues, save for the purposes of an interim payment, so they would in due course seek a repayment, and/or an adjustment of any amount awarded, to the extent that they may succeed on their appeal in the quantification proceedings.

35. In my judgment, Six Continents had no real answer to the main thrust of the Revenue's submissions on the inappropriateness of summary judgment in the present

case. As will appear from my discussion of the substantive issues, I am satisfied that they turn to a significant extent on questions of law which are either already under appeal in the quantification proceedings, or are sufficiently similar that their ultimate resolution is likely to be heavily influenced by the outcome of the existing appeals. Mr Bremner submitted that this might be a good reason for me to grasp the nettle now, and decide the similar issues, so that any appeals from my decision could (if the Court of Appeal agreed) be consolidated with the appeal in FII (High Court) II, which I was told has been fixed for hearing over ten days in June 2016. From a case management perspective, there might be some attraction in this suggestion; but it seems to me to ignore the basic point that I could only grant summary judgment if I were satisfied that the Revenue had no realistic prospect of successfully defending the claim. In the present state of the law, and with the appeals for which I have granted permission still pending, I do not feel able to reach that conclusion.

36. I also agree with the Revenue that there is at least one further reason why the present case needs to go to trial. Although Six Continents' case depends heavily on evidence of Dutch tax law, that evidence has not been presented in a satisfactory manner. The general rule is that, in an English court, foreign law is a matter of fact which must be pleaded and (subject to limited exceptions) must be proved by expert evidence: see Dicey, Morris & Collins, The Conflict of Laws, 15th edition, vol 1, Rule 25(1) and the commentary on that rule in chapter 9. In the present case, however, the relevant Dutch law has not been pleaded, and no expert evidence has been adduced in accordance with CPR Part 35. Instead, Six Continents relies on three witness statements (two of them very short) of Roger Brands, who is a tax partner with Deloitte in the Netherlands and in that capacity has provided tax services to the IHG Group since October 1999. Mr Brands holds university degrees in Business Economics and Tax Law, and is a member of the Dutch Association of Tax Lawyers. I have no reason to doubt that he is fully qualified to give evidence about Dutch corporate tax law, and the Revenue indeed appear content to accept his evidence as far as it goes. But the fact remains that his evidence has not been adduced as expert evidence in accordance with CPR Part 35, and there may also be a question whether he has the necessary independence to be a suitable expert witness. That apart, some of the principles of Dutch tax law which he states are set out in fairly general terms, and Mr Baldry made it clear that there are aspects of his evidence which he would like to have the opportunity to test and clarify in cross-examination. For all these reasons, I do not consider that the court could at this stage rely on Mr Brands' evidence with sufficient confidence to justify giving summary judgment on the claim.

37. It follows, since the principle of making an interim payment order in relation to part of the claim is not disputed by the Revenue, that the real issue is to what extent I can be satisfied that, if the claim went to trial, Six Continents would obtain judgment against HMRC. For that purpose, it is common ground that I should apply the law as it now stands, while having regard to the pending appeal in the quantification proceedings.

The substantive issues

(1) Revaluation adjustments

38. These are adjustments to pre-tax commercial (or accounting) profits, which in general prevent the recognition for tax purposes of revaluations (upwards or downwards) of

capital assets before they are disposed of. Substantial amounts of the Dividends paid in 1996 and 1997 were derived from upwards adjustments of this nature. The issue is whether Six Continents is entitled to a credit at the Dutch standard rate of corporation tax (being the relevant FNR) for so much of the Dividends as was derived from the adjustments.

39. The general principle for which HMRC contend, as set out in paragraph 3 of their grounds of appeal in FII (High Court) II, is that "where the income in question has not been made liable to tax in the foreign country, because it is exempt, the UK is not required to provide any credit in respect of that income". In such a case, they submit, there is no risk of economic double taxation in respect of the same income in the Netherlands and the UK, and there is accordingly no discriminatory treatment which engages EU law and needs to be remedied.

40. In this connection, Mr Baldry referred me to FII (ECJ) II where the Court described the underlying circumstances which engage EU law in the following way:

> "37. It should be recalled that, in the context of tax rules, such as those at issue in the main proceedings, which seek to prevent the economic double taxation of distributed profits, the situation of a corporate shareholder receiving foreign-sourced dividends is comparable to that of a corporate shareholder receiving nationally-sourced dividends in so far as, in each case, the profits made are, in principle, liable to be subject to a series of charges to tax…
>
> 38. That being so, articles 49 FEU and 63 FEU require a member state which has a system for preventing economic double taxation as regards dividends paid to residents by resident companies to afford equivalent treatment to dividends paid to residents by non-resident companies…"

41. Before considering this argument, I need to say a little more about the nature of the adjustments and their tax treatment in the Netherlands. Mr Colin Garwood, who is the head of tax for the IHG Group and a chartered accountant with thirty years' experience in the field of corporation tax, describes the revaluations which HMRC seek to exclude as:

> "…no more than a standard adjustment for tax one would expect in the UK and I anticipate most jurisdictions to limit the circumstances in which revaluations of assets in advance of disposal are recognised for tax purposes."

42. He goes on to explain that adjustments of this type "are entirely in keeping with accounting standards to ensure that assets are carried at a fair value". Downward revaluations are normally required where the value of the asset is thought to have fallen below its original cost on a permanent basis ("permanent diminution"). Such a write down will normally be made through profit and loss account, and if the asset later recovers some value the write down will be partially written back, again through profit and loss account. He continues :

> "The write down (and likewise the write back) are reversed from the accounting profits to establish the taxable profits. This creates corresponding differences between the book value of the asset for accounting purposes ("the carrying amount") and for tax purposes ("the tax base") which in principle requires deferred tax accounting as commented on in paragraph 20 of International Accounting Standard 12."

43. Mr Garwood concludes, in paragraph 31 of his fourth statement:

> "I can see no reason why this standard type of timing adjustment should be removed from the accounting profits for the computation of double tax credits and we have not followed this approach in our computations. The amounts HMRC are suggesting should be segregated were part of the accounting profits distributed in a given dividend and would have properly been taken into account in establishing the rate of underlying tax paid under the UK system at the time with respect to that dividend."

44. The tax treatment of the adjustments in the Netherlands is explained by Mr Brands in his evidence. Resident companies (such as SCIH) are subject to taxation on their worldwide income. The basis for the amount of tax due is known as "the taxable amount". The Dutch corporate income tax system requires the taxable amount to be computed in accordance with prevailing legislation and principles, and the resulting taxable profit is then subjected to tax at the standard rate (which in the three relevant years was 35%). He continues (in paragraph 7 of his first statement):

> "The taxable amount is the taxable profit less losses available for loss relief from prior years or by carry back from later years. Taxable profit is defined as income less deductible expenses and allowances. Generally, no distinction is made between trading income and capital gains."

45. In the next section of his first statement, Mr Brands describes the Dutch participation exemption and the revaluations with which I am now concerned. It is convenient to set out this passage in full, because the two topics are related:

> "9. The Dutch corporate income tax system contained a limited number of exemptions, most notably (and of most relevance to the Dutch IHG companies) the participation exemption system for qualifying share investments in subsidiaries. In the case of a qualifying share investment (which was the case with the Dutch IHG subsidiaries) dividends and capital gains/losses from domestic and foreign participations are exempt from taxation.

> Basically this meant that all results (positive and negative) coming from qualifying investments are excluded from the taxable amount. This was a full exemption and also applies to certain operational expenses that specifically relate to the activity of having qualifying share investments in subsidiaries.
>
> 10. One important exception is the liquidation loss incurred when liquidating a subsidiary. If certain provisions were met, a liquidation loss was tax deductible (at the normal prevailing Dutch tax rates).
>
> 11. Related to the participation exemption is the valuation method of subsidiaries on the balance sheet. For Dutch tax purposes subsidiaries qualifying for the participation exemption are valued at cost price. This means that annual revaluations are excluded from the fiscal profit/loss as any movements in the value of a subsidiary will be taken into account upon the sale of that subsidiary (the sale of a subsidiary is the assumed realisation moment by default and not liquidation). Any result would then be exempt from taxation due to the participation exemption."

46. Later in his first statement, Mr Brands says that all the adjustments now in issue were for interests in subsidiaries, and comments:

> "Revaluation results – positive and negative – are eliminated (exempt) for Dutch tax purposes and therefore impact the effective tax rate in a positive or negative way."

47. I can now return to the Revenue's argument outlined above. As the law now stands, the argument is in my judgment most unlikely to succeed at trial. On the basis of Mr Brands' evidence in its present form, it seems reasonably clear to me that the relevant adjustments formed part of Six Continents' accounting profits and as such fell within the basic charge to Dutch corporation tax on Six Continents' worldwide income. The adjustments were then excluded from the taxable amount, with the result that the tax base was correspondingly narrowed and the effective rate of tax was reduced. There appears to be no doubt about the exclusion, although it is unclear to me whether it follows from application of a general principle of Dutch tax law, or rests on the narrower basis that recognition of the adjustments for tax purposes would be incompatible with the underlying participation exemption for the shareholdings of Six Continents in the subsidiaries which paid the Dividends.

48. I find confirmation that this is the right way to analyse the position in Mr Brands' comment, quoted above, that the effect of eliminating revaluation results is to "impact the effective tax rate in a positive or negative way". This language is apt to describe a situation where the tax base is narrowed by the application of a relief or an exemption so that a meaningful contrast can then be drawn between the nominal and effective rates of tax applicable to the relevant income. The language would not be apt if, as Mr

Baldry appeared at times to submit, the adjustments were a mere "tax nothing" which did not even fall within the prima facie scope of the charge to Dutch corporation tax.

49. So viewed, the exclusion of the adjustments also falls squarely within the reasoning of the Court in FII (ECJ) II which led it to conclude that a tax credit at the FNR would have been needed in order to achieve equivalence between the exemption system for domestic dividends and the imputation system for foreign dividends which the UK then operated. Thus, the Court said at paragraph 46:

> "Second, exemption from tax of dividends paid by a resident company and application to dividends paid by a non-resident company of an imputation method which… takes account of the effective level of taxation of the profits in the state of origin also cease to be equivalent if the profits of the resident company which pays dividends are subject in the member state of residence to an effective level of taxation lower than the nominal rate of tax which is applicable there."

The Court added, in paragraph 49, that:

> "The effective level of taxation may be lower than the nominal rate of tax by reason, in particular, of reliefs reducing the tax base."

50. I am also satisfied that nothing turns, in the present context, on the distinction (which is anyway difficult to formulate with any precision) between reliefs and exemptions from tax. What matters is that the receipts in question fall within the general scope of the charge to tax, not the particular machinery by which they are then excluded from the charge. The words "in particular" in paragraph 49 of the Court's judgment in FII (ECJ) II show that the reference to "reliefs" reducing the tax base was not intended to be exhaustive. I would only add that, in giving guidance which was intended to apply to the differing tax systems in force in Member States throughout the European Union, it seems to me inconceivable that the ECJ could have intended anything to turn, at a general level, on the various legislative techniques which may be used to reduce the relevant tax base.

51. I am equally satisfied that the Revenue cannot find any assistance in paragraph 37 of the judgment of the Court, quoted at [40] above. That part of the judgment was directed to an earlier stage in the analysis, namely whether the situation of a corporate shareholder receiving foreign dividends is comparable to that of a corporate shareholder receiving domestic dividends. In the context of the FII Group litigation, that question was conclusively answered in the test claimants' favour in FII (ECJ) I.

52. For these reasons, I consider that the conditions for ordering an interim payment in relation to this component of the Dividends are satisfied. On the material now before me, I think that Six Continents would succeed at trial on its claim to be entitled to a credit at the FNR on the Dividends in so far as they were sourced from distributable profits arising from the revaluations. I do not merely think it likely that Six Continents would obtain judgment for this part of its claim.

(2) Exempt profits

53. I can deal with this issue briefly, because it raises essentially the same point as the revaluation adjustments. The sum in contention arose from the liquidation of a subsidiary of SCIH, and formed part of the accounting profits of SCIH for 1995. It was then included in the third of the Dividends which SCIH paid to Six Continents in 1997. The sterling equivalent of the sum was a little over £1million.

54. The Revenue submit that no tax credit is due in respect of this part of the dividend, because the profits from which it was paid were exempt from Dutch corporation tax by reason of the participation exemption. The answer to this submission is in my judgment the same as before. The profits derived from the liquidation of the subsidiary were in principle within the charge to Dutch corporation tax, although they were excluded from the taxable amount by virtue of the participation exemption. This is therefore another example of an exemption which narrowed the tax base and reduced the effective rate of Dutch tax. As such, it falls squarely within the reasoning of the ECJ in FII (ECJ) II , and a credit at the Dutch nominal rate of corporation tax is needed in order to remedy the unlawful impact of the Case V charge on the dividend in the UK.

55. Both sides are, I think, agreed that this issue is in principle indistinguishable from the Henri Wintermans sale which I considered in FII (High Court) II at [75] to [77]. In considering the question, I was handicapped by the absence of any evidence about the nature of the relevant exemption under Dutch law. I nevertheless concluded, with some hesitation, that it was preferable to regard the capital gain arising from the sale as a receipt which prima facie formed part of the taxable profits of BAT Nederland BV and was in principle subject to tax at the nominal rate, even though the effect of the exemption was to narrow the tax base by removing it from charge. Now that I have the benefit of Mr Brands' evidence, which for present purposes the Revenue are prepared to accept, I see no reason to depart from the view which I formed in FII (High Court) II and I respectfully decline the Revenue's invitation not to follow my earlier conclusion.

56. I am accordingly satisfied that an interim payment should also be made in respect of this part of the 1997 Dividends.

(3) Share premium account gains

57. The third, and last, substantive issue concerns dividends sourced from the share premium account in a Dutch subsidiary of SCIH. The evidence shows that the whole of the second, and part of the third, Dividends paid by SCIH in 1997 had their source in the share premium account. The sterling equivalent of the sums in issue was approximately £1.07 million.

58. Mr Brands' evidence in relation to dividends paid out of share premium reserve is that the reserve is considered a separate equity item, which was not liable to taxation on either income or capital when it was first contributed. A distribution out of share premium was likewise treated as a non-deductible equity movement for corporate income tax purposes, although it was considered a dividend liable to withholding tax unless certain requirements were met. Mr Brands continues (in his first statement):

> "27. From the perspective of the current HMRC questions, the distribution out of share premium does not relate to income liable to corporate income tax, as the contribution and the distribution are both considered non-deductible/taxable for corporate income tax purposes.
>
> 28. From a Dutch corporate income tax perspective a dividend paid out of share premium is considered not relevant for the purposes of computing Dutch taxes on profits as the dividend is considered a non taxable/deductible equity movement. Considering the fact that the dividend is not related to any income gained, there is no link with corporate income tax whatsoever."

59. On the basis of this evidence, as it now stands, Six Continents accepts that the share premium account cannot be regarded as liable in principle to Dutch corporation tax, and no assistance can therefore be gained from the reasoning in FII (High Court) II. Instead, Six Continents advances a different argument. It says that the Case V charge on this part of the Dividends breached their rights of free movement of capital and establishment, in spite of the fact that the underlying dividend was not subject to tax in the Netherlands. It says that the dividends paid from share premium account are a return of capital made by a non-UK resident company, but if such a return of capital had been made by a UK-resident company, it would not have been taxable. Such differential treatment would, it is said, be a clear breach of the relevant EU freedoms, and since the relevant parts of the dividends have been subjected to the Case V charge the appropriate remedy is again to allow a tax credit at the Dutch nominal rate of corporation tax.

60. HMRC's answer to this argument is that the analogy is faulty, because the return of capital was made (by way of dividend) to SCIH by an underlying Dutch subsidiary, whereas the dividends paid by SCIH to Six Continents were not a return of capital at all. The UK was therefore entitled to charge tax on those dividends, subject to providing a tax credit to the extent that the dividends were sourced from profits which were subject to tax. As the evidence makes clear, the share premium was not in any sense subject to tax, so no credit is due.

61. In my view there is much force in the Revenue's counter-arguments on this point, and my provisional conclusion is that this part of the claim should not succeed at trial. It follows that the conditions for an interim payment are not met.

Conclusion

62. My overall conclusion therefore is that the claim for an interim payment succeeds, save in relation to those parts of the 1997 Dividends which were sourced from share premium account. According to a helpful quantification table produced by Mr Bremner, the full amount of the claim on this basis would be £18,685,563. If this figure is correct, it is then common ground that (as in the original order made by Sir Andrew Park) it should be reduced by 15%, and rounded to the nearest £10,000, so as to give the appropriate figure for an interim payment. A number of points of detail on quantification were still under discussion at the time of the hearing in July, but in the

light of this judgment I hope the parties will now be able to reach agreement on the sum to be awarded by way of interim payment, and I will make an order accordingly.

63. The parties should also consider what further directions it is appropriate to give at this stage for trial of the claim.