485. Lord Reid considered that the Special Commissioners "plainly meant" that Kilmorie would not have paid so large a sum to Opendy "but for their non-trading purpose of enabling the tax avoidance scheme to succeed". He noted that neither party was acting as a free agent in its own interest (as Opendy was a subsidiary of the devisers of the scheme and Kilmorie was a Downes family company) and "both had been procured to play their part in the scheme". He continued similarly to link the overinflated price with the tax avoidance scheme in saying that "the price was dictated by the scheme, and plainly had nothing to do with the market value of the rights sold". He also thought it quite obvious that none of the companies acted in their own interests; they just did what Mr Downes and the devisers of the scheme wanted. He said that if a trader only had commercial motives the Revenue cannot merely say that he has paid too much; he may have been foolish or he may have had what could fairly be regarded as a good commercial reason for paying too much but:

> "if it is proved that some non-commercial reason caused the trader to pay more than he otherwise would have done, then it seems to me quite clear that the payment can no longer be held to have been wholly and exclusively expended for the purposes of the trade. No authority is needed for so obvious a proposition."

486. Lord Reid is clear that it is only if there is "some non-commercial reason" which causes the overpayment that the payment fails the wholly and exclusively test. In the context of the findings of the Special Commissioners, which Lord Reid was considering, the non-commercial reason for the overpayment can only be the facilitation of the tax avoidance scheme.

487. He concluded by noting that the statutory provision could well be read as meaning that, if it could be shown that a part of the expenditure was in fact wholly and exclusively for trading purposes, then that part was deductible. But he did not have to decide that because the Revenue had agreed that in this case £2,250 of the £77,250 paid would be allowed as a deduction being the then market value of the rights.

488. Lord Morris based his decision on the tax avoidance motive (at 1609 B to D). He noted that Opendy only came into the story in order to facilitate the scheme and the amount of £77,250 had to be paid, not wholly and exclusively for the purpose of developing the Landywood Estate, but "mainly in furtherance of and in order to facilitate the scheme for avoiding liability to income tax". He noted that, as the agreement did have some value, the disallowance of the whole of the £19,240 "bore somewhat hardly". But he nevertheless considered that the appeal failed.

489. Lord Wilberforce said, at 1616 B to D, that what the Commissioners meant by the agreement being "an essential prerequisite" was that it was "a necessary step in the scheme" whereby the prospective profits were to be passed back (through Opendy) to the trustees. It was not being said that it was "necessary in any commercial sense". Once this was properly understood, the Commissioners' finding was fatal to the taxpayers' claim:

> "To have found that to agree to pay £77,250 for the benefit of an agreement which barely a week earlier had been assigned for £2,250 was a commercial purpose would have been simply perverse. After all, the directors of [the relevant company] had considered that, on March 30, 1962, £2,250 was a good price fully reflecting the value of the building agreement. The price Kilmorie paid was 34 times that good price."

490. Again, it is clear that Lord Wilberforce is referring to the lack of commerciality of the price in the context of justifying the Commissioners' finding that the payment was made with a tax avoidance purpose.

491. Lord Cross thought that the Special Commissioners could be criticised in so far as their language could suggest that the fact that one of the purposes for which a payment is made is not a trading purpose necessarily leads to the conclusion that the payment must be disallowed. He gave an example where a payment could be held to be for dual purposes but it was nevertheless allowable as a bona fide commercial transaction:

> "Suppose that a retailer is in the habit of buying certain articles from a wholesaler for £10 each which is a fair commercial price, that his son-in-law sets up in business as a wholesaler dealing in similar articles and that thenceforth the retailer deserts the other wholesaler and buys the articles from his son-in-law for £10 each. One of the purposes for which the retailer is entering into the transactions with his son-in-law is to help him in business but nevertheless the cost would be properly allowable because the transactions though entered into in a sense for a dual purpose are bona fide commercial transactions."

492. However, although the language used could be open to misunderstanding, he thought the Commissioners were correct in their conclusion. Continuing with his example he put another case where the retailer bought articles from his son-in-law for £15 which he could have bought from the wholesaler for £10. He said that:

> "each expense would not have been allowable - at all events to the extent of the extra £5 - because the purchases were not genuine commercial transactions but purchases at a fancy price entered into to benefit the vendor".

493. Lord Cross noted that the benefit of the agreement for which Kilmorie paid over £77,000 had been sold for £2,250 only a few days previously and Mr Downes himself had said in evidence that that was a fair price. So "£77,000 was in truth a fancy price fixed by Downes and [the designers of the scheme] for the purposes of the scheme" – in the same way as £15 was a fancy price in his second example.

494. He noted that the taxpayer stressed the fact that although Kilmorie had to pay £77,000 for the benefit of the agreement, it nevertheless derived a substantial profit from the transaction and also on the fact that the Special Commissioners found that the agreement "was an essential prerequisite to the carrying out by Kilmorie of the development of the estate." He said:

> "But these facts do not show that the price of £77,000 was a commercial price. It is, of course, true that Kilmorie could not develop the estate unless it acquired the benefit of the agreement from Opendy and that in order to acquire it had to pay £77,000. Further, it is true that the fact that a price paid is extravagant does not necessarily show that the purchase is not a genuine commercial transaction. A purchaser dealing at arm's length with a vendor may say to himself 'The price which he is asking is absurdly high but I cannot get him to take less and I believe that even at that price I can make a profit on the deal. So I will agree to pay what he is asking.' But Kilmorie was not dealing at arm's length with Opendy. It was controlled by Downes and it agreed to pay the £77,000 not because its directors other than Downes decided in the exercise of an independent judgment that it was worth Kilmorie's while to agree to pay that price but because the scheme provided for that price being paid. For these reasons I would dismiss the appeal by Kilmorie."

Scotts Atlantic

495. *Scotts Atlantic* concerned a scheme designed to enable the taxpayers to provide their directors and employees with benefits, which were not taxable at that time, whilst obtaining a tax deduction for the cost of the scheme. It was designed to circumvent the provisions of schedule 24 to the Finance Act 2003 which are aimed at preventing exactly that situation.

496. The Upper Tribunal decided that the transaction was not outside the scope of schedule 24 so that it applied to prevent there being any deduction which would otherwise be available. They went on, however, to consider the question of whether a deduction would be allowable under s 74 ICTA as, in effect, that was a pre-requisite to schedule 24 applying. On that issue, the taxpayer argued that the only purpose of the contributions was to provide benefits for employees through employee benefit trust arrangements. HMRC argued that there was another purpose, namely to secure a tax deduction. Not only was securing this tax deduction a purpose of the scheme (which was accepted) but it was also a purpose of the expenditure so that the contributions were not wholly and exclusively expended for the purposes of the trade.

497. The Upper Tribunal set out the principles of the "wholly and exclusively" test adopting the principles set out in *Vodafone* including the need to distinguish between object and effect. They noted, at [55], that the mere fact that a choice is influenced or dictated by the tax consequences does not necessarily mean that the choice involves a duality of purpose as regards the expense. In their view:

> "the words of Millett LJ [as regards the distinction between object and effect] are just as relevant and applicable where there is a choice as where there is not: in each case, the question is whether the payment is made exclusively for the purposes of the trade, and that is a question of fact for the FTT".

498. At [56], the Upper Tribunal continued to note that the taxpayer had two arguments that the findings made by the tribunal in its decision in favour of HMRC was wrong.

(1) The first argument was that the tribunal's conclusion, that a main purpose of the relevant expense was to reduce tax liabilities, is inconsistent with the principle, as stated by Romer LJ in *Bentleys, Stokes & Lowless v Beeson* [1952] 2 All ER 82 at 85, 33 TC 491 at 504 (and approved by the Court of Appeal in *Interfish Ltd v Revenue and Customs Comrs* [2014] EWCA Civ 876, [2015] STC 55) that:

> "if, in truth, the sole object is business promotion, the expenditure is not disqualified because the nature of the activity necessarily involves some other result, or the attainment or furtherance of some other objective, since the latter result or objective is necessarily inherent in the act."

The taxpayer noted that the tribunal had accepted the purpose of the expense was to benefit employees which was a business purpose. In the taxpayer's view, the fact that the employees' tax liability was reduced was merely an incidental effect and not a purpose.

(2) The second argument, at [57], was that, even if there was an element of duality of purpose, the expenditure would have been incurred even without a non-trading tax avoidance motive and, relying on *Kilmorie*, in such circumstances the expenditure remains deductible.

499. On the first issue, the Upper Tribunal considered precisely what the relevant finding of fact was that the tribunal had made. They noted, at [65] and [66], that a finding that there was an object of avoiding corporation tax would not be justified on the basis that the taxpayer had decided to incur expenditure for the purposes of its trade in a particular way. That would "confuse the object of the expenditure with the reasons for incurring it in the way in which it was in fact incurred", as they had noted at [55], and, at [66]:

> "A taxpayer is entitled to order its affairs in a way which incurs the least tax liability and the mere fact that a choice is influenced or dictated by the tax consequences does not necessarily mean that the choice involves a duality of purpose. It does not, therefore, necessarily follow that the adoption of the scheme … results in a duality of purpose (although it may do so as a matter of fact) unless this is one of those cases referred to by Lord Oliver in *MacKinlay v Arthur Young* … where the results (in the present case, the securing of deductions) are so inevitably and inextricably involved in particular activities (in the present case, the making of the contribution and the effecting of the scheme) that they cannot but be said to be a purpose of those activities."

500. However, the Upper Tribunal concluded that was not the basis for the tribunal's finding. They noted, at [59], the distinction the tribunal drew between a case where a taxpayer ordinarily pays salary, in which case the fact that it expects to secure a

deduction does not occasion any duality of purpose and, at [61], that where "the deliberate and all-pervading objective of achieving a corporation tax deduction makes it impossible to treat the corporation tax result sought for the contributions as the "ordinary, intended or realistically expected outcome" of making salary, bonus or equivalent payments. In their view, at [67], it was this last statement which essentially provided the basis for the tribunal's findings. The words "ordinary, intended or realistically expected outcome" were adopted as the yardstick by reference to which a result can be ignored as a separate object.

501. They were satisfied, at [70] to [73], that the tribunal had based its decision on a finding that they were entitled to make, that one of the purposes of the contributions (in contrast with the purpose of the method of expenditure) was to obtain a tax deduction which would not have been available if the contribution had been made by more conventional means, and that, in these particular circumstances, such purpose was not an incidental consequence of the expense. Whatever else, "the FTT did not conclude that because the tax benefit was a consequence of the contribution, it was a purpose of the expense."

502. They concluded by emphasising, at [73], that the important words in Romer LJ's comments in *Bentleys* are "if, in truth, the sole object is business promotion". In their view the principle is that "if such is the case, then an incidental effect does not as a matter of law disturb that conclusion". In this case, the tribunal did not find that there was a sole object but only that the companies had another object. In doing so, it recognised that an incidental consequence of a tax deduction did not mean that such a deduction was necessarily an object. They continued, at [74], that the point made in *Bentleys* was that expenditure is not disqualified:

> "*because* the nature of the activity necessarily involved some other result, in other words that the mere existence or knowledge of that result is not enough to give a dual purpose.
>
> But if the fact-finding tribunal concludes that its inquiry into the mind of the taxpayer revealed that the taxpayer actually had that other purpose as an object of the expenditure, then the fact that that result is a natural consequence of the expenditure will not cause that finding to be perverse."

503. It is clear, therefore, that the Upper Tribunal considered that the fact that a payment has tax consequences or that the way expenditure is incurred may result in a fiscal advantage does not necessarily result in the payment having a non-trading purpose. The question, as set out in *Vodafone*, must be assessed by reference to the particular object the taxpayer has in mind in making the relevant payment. If, on the subjective enquiry required, it is properly concluded that the taxpayer had in mind obtaining the tax benefit that results from the making of the payment, the fact that the obtaining of the tax benefit is a natural consequence of the payment does not affect that finding. In other words, there is no presumption that the natural consequence or effect of a payment is or is not the object of the payment.

504. On the second argument the Upper Tribunal noted, at [75], that the taxpayer argued (similarly to BNP in this case) that *Kilmorie* shows that if the cost of

something would have been £10 and its cost with tax benefit is also £10, then £10 remains deductible. This was said to follow both from the example in Lord Cross's speech about a retailer and also from the division between the allowable and unallowable elements of an expense incurred with a dual purpose espoused by Lord Wilberforce in his agreement with Roskill LJ ([1973] STC 330, [1973] 1 WLR 1180) and by Lord Simon in his speech.

505. They noted, however, at [76], that in that case none of their Lordships reached a conclusion that part of the payment should be allowed and part disallowed. The closest to that proposition were Lord Reid and Lord Cross:

> "Further the House was considering the case in which it was possible to divide and segregate the expense into parts incurred for one purpose and parts for another, and Roskill LJ's remarks in the Court of Appeal were also addressed to such a situation. That is quite different from saying that, if the whole of an expense had both a trading and a non-trading purpose, the existence of a trading purpose was sufficient to make the whole expense deductible. Such a result would seem to us to fly in the face of the statutory requirement that the purpose be 'exclusively' a trading one."

506. They continued, at [77], that they were "not deflected from this conclusion" by Lord Cross's example of a retailer who buys goods for £10 from his son-in-law rather than for the same price from his usual supplier as set out above. They noted that in that case Lord Cross did not consider that the fact that the retailer purchased from the son-in-law to help him in his business prevented a deduction:

> "But, whether the retailer buys for £10 from the previous wholesaler or his son-in-law he incurs the same expenditure, and, absent some particular factor, the object of that expenditure will almost certainly be found as a matter of fact to be to obtain the goods, even though the manner of the expenditure may be to benefit his son-in-law."

507. They then considered the other example given by Lord Cross where the retailer pays £15 to obtain the goods from his son-in-law when he could have paid £10 to his usual wholesaler. They said that in that case:

> "it will generally be an obvious deduction from the circumstances that as a matter of fact he must have had an additional object in incurring the expenditure and not merely a different object in the manner it was incurred. But neither conclusion follows as a matter of law, for the actual evidence before the tribunal may dictate or permit a different factual conclusion."

508. In *Drummond* the Court of Appeal rejected HMRC's argument that the whole of the price of £1.96 million paid by a taxpayer to acquire second-hand life assurance policies was not "consideration given wholly and exclusively" for the assets, within the meaning of the capital gains legislation, because the policies were purchased as part of a tax avoidance scheme to realise a loss on the policies. The Court of Appeal essentially agreed with Norris J in the High Court (*Drummond v Revenue and Customs Commissioners* [2008] STC 2707) who held (at [29] of his decision) that the

taxpayer "wanted to acquire the policies precisely because by doing so he thought he would obtain a tax advantage on their surrender" but he nevertheless "still gave consideration wholly and exclusively to acquire them."

Discussion

509. BNP submitted that in *Kilmorie* their Lordships (particularly Lords Reid, Cross and Wilberforce) did not consider the tax avoidance purpose to be determinative of the issue. Rather (with the exception of Lord Morris) they were focussed on the relationship between the amount expended and the value of what was acquired; the overpayment was the key to the issue. The corollary is that where, as here, the taxpayer pays a fair value to acquire a real asset, such as the right to a dividend, a tax deduction is available.

510. BNP argued that the factual basis of the decision in *Scotts Atlantic* is distinguishable from this case and the reasoning used in fact supports BNP's position. BNP noted that it was held in that case that the over-arching object of the payment was simply to get a deduction for the payment notwithstanding the enactment of schedule 24. That is not the same as a case where money is laid out to acquire an actual asset, as trading stock, for a price which reflects its fair value, for the purpose of onward sale. As the London branch paid a fair or market price for the dividend rights, it follows that the whole of that expenditure was incurred with the object of acquiring the dividend rights. This stands to reason given that, as a result of that expenditure, the London branch acquired an asset worth the price it paid. The ability to deduct the expense of acquiring trading stock is merely the natural consequence or effect of purchasing it at a fair or market value.

511. BNP argued that, in their comments on *Kilmorie*, the Upper Tribunal in effect accepted that was a case where it was possible to divide and segregate the expenditure incurred on an asset into parts incurred for one purpose and parts for another and, by implication, that the division is to be made by reference to the value of the asset acquired. This is in contrast to a case, such as *Scotts Atlantic*, where nothing is acquired by the trader and there is no basis for any such division. The Upper Tribunal meant, therefore, that in *Kilmorie* the expenditure which reflected the fair value of the asset was incurred for the purposes of the trade; it was the remainder which was incurred for a non-trading purpose. In BNP's view this is confirmed by the discussion at [77] of the example given by Lord Cross in *Kilmorie* of the case where the trader pays £10 to his son-in-law for goods worth £10 and the comment that "the object of that expenditure will almost certainly be found as a matter of fact to be to obtain the goods".

512. In our view, whilst in *Kilmorie* their Lordships refer to the lack of the commerciality of the price as a factor, that is quite clearly in the context of and leading to the conclusion that the over payment demonstrated that the taxpayer's object was to facilitate a tax avoidance scheme. It was not simply the fact that the price was inflated which lead to their conclusion that the expenditure was not allowable. It was the fact that the inflated price showed that there was a non-commercial purpose which, in the context of the Commissioners' findings of fact, lead to that conclusion that there was a tax avoidance purpose.

513. As for the examples given by Lord Cross, read in context, Lord Cross was merely drawing attention to the fact that the particular object of the payment must be properly assessed in each case. It is not every ancillary non-trading purpose which will prevent a payment qualifying as wholly and exclusively incurred for trading purposes. In other words, buying an asset from a relative for its usual price will not convert the object of the payment from being for commercial trading purposes to non-trading purposes. On the other hand, paying a relative an overvalue for the asset, as he continued to note in his second example, may (as in *Kilmorie* itself) lead to the conclusion that the object of the payment is not in fact wholly commercial. In the context of examining whether the Commissioners had made correct conclusions that the object was in part for tax avoidance purposes, Lord Cross clearly considered that the over inflated price paid in that case was, in effect, evidence of that object. So he concluded that *Kilmorie* paid that price not because it was worth its while "but because the scheme provided for that price being paid".

514. We do not see this decision, therefore, as establishing a principle, as BNP argued, that if a fair price is paid for an asset of a kind used in the taxpayer's trade, that amount will necessarily qualify as deductible expenditure. In each case, the question is why, or with what object or purpose, the amount was laid out or expended. Whilst expenditure incurred in such circumstances ordinarily may well be incurred wholly and exclusively for the purposes of the trade, the decision does not establish that there is a presumption to that effect. There is still scope for finding that the price was not paid for trading purposes if that was not in fact the case. The focus on the over inflated price paid by the taxpayer in *Kilmorie* was referred to as the main factor demonstrating that a purpose or object in paying the amount in that case was to facilitate the tax avoidance scheme.

515. HMRC argued that there is no support for BNP's position in the Upper Tribunal's comments on *Kilmorie* in the *Scotts Atlantic* case. We agree. The Upper Tribunal recognised that there is a difference between a case where a payment can be separated into parts each of which has a separate purpose and that where the whole payment has two purposes (see [76]). They saw Lord Cross's first example as one in which "the object of that expenditure will almost certainly be found as a matter of fact to be to obtain the goods" and the second as one in which it "will generally be an obvious deduction from the circumstances that as a matter of fact he must have had an additional object in incurring the expenditure" but "neither conclusion follows as a matter of law, for the actual evidence before the tribunal may dictate or permit a different factual conclusion" (see [506] and [507] above).

516. All the Upper Tribunal drew from Lord Cross' examples, therefore, was that it is purely a question of fact as to what is the object of the expenditure. Lord Cross' examples were just that; examples of what might be expected to be the case. They were not put forward as establishing legal principles. On that basis, we cannot see that the Upper Tribunal was, as BNP asserted, endorsing a proposition that an amount spent on an asset must necessarily be deductible if the amount reflects its value. Rather once it has been found as a fact that the expenditure has two purposes, one being a business purpose and one not, then the expense is not deductible.

517. Moreover, the Upper Tribunal's conclusions on the taxpayer's first argument in *Scotts Atlantic* support this conclusion. They considered that the passage cited in *Bentleys* meant that it is not to be presumed that, if an effect necessarily follows from a payment, then the effect is an object of that payment. However, if in fact, on the subjective enquiry required, it is properly found to be what the taxpayer had in mind as the object of the payment, it is not precluded from being such because it is a necessary consequence of the payment. Hence, the fact that a contribution payment of the type involved in that case would usually result in a tax deduction neither leads to a conclusion that obtaining the deduction is a mere incidental effect of the payment nor that it is the object of the payment. A further enquiry is required. As in that case, therefore, the fact that it would usually follow as a necessary consequence that a trader who buys trading stock for its fair value and sells it for a profit obtains a tax deduction does not of itself lead to the conclusion that the payment is deductible. If, in truth, the appellant's purpose in incurring the expenditure was to obtain a tax advantage, the tribunal is not precluded from finding that was the taxpayer's object.

518. BNP also relied on *Drummond* but we agree with HMRC that the case is not in point. The question for capital gains purposes is whether the monies have been given (wholly and exclusively) as consideration for the acquisition of the asset. Hence, whilst the purpose of the taxpayer in *Drummond* in acquiring the insurance policies may well have been because he wanted to implement a tax avoidance scheme, that was simply not relevant. It seems to us that is not the same question as whether monies have been laid out wholly or exclusively for the purposes of the trade which, as set out in the case law, is a subjective question of looking at the taxpayer's intentions. The question what were the monies spent on is not the same as why were the monies spent.

519. BNP also argued that expenditure which is incurred wholly and exclusively for the purposes of a trade does not cease to be deductible simply because, in the particular circumstances, the receipt "generated" by the expenditure is not brought into the trader's tax computation on the basis of *Hughes v Bank of New Zealand* [1938] AC 36 ('*Hughes*'). Whilst that may well be the case, as HMRC noted, that decision sheds no light on when an expense is to be regarded as wholly and exclusively incurred for the purposes of the trade in the first place. At 378, Lord Tankerton merely acknowledged that expenditure in the course of the trade which is unremunerative is none the less a proper deduction, if wholly and exclusively made for the purposes of the trade. It does not require the presence of a receipt on the credit side to justify the deduction of an expense.

520. As BNP repeatedly emphasised, the London branch paid a price for the right to the dividends which reflected a fair value for the right (or at least the price was not an overpayment looking at what a third party may be expected to pay), the right is analogous to assets the London branch typically deals in and it was sold for a profit. In one sense, it can be said that monies spent on an asset typically bought and sold in the trade for its fair value are laid out for acquiring the asset which, as a factual matter, is thereby obtained. Whilst that may often lead to the conclusion that the asset was acquired for trading purposes, that is not the end of the enquiry and any wider purpose may be relevant. As the Upper Tribunal said in *Scotts Atlantic*, it does not

necessarily follow that because an effect follows as a natural consequence of the incurring of expenditure that that result is not a purpose of the expenditure. So the fact that it follows in the usual course that spending monies on an asset which is sold in the course of the trade gives rise to a tax deduction does not preclude that effect being the taxpayer's object if an enquiry into the taxpayer's mind reveals it to be such.

521. In this case, as we have set out in detail above, we consider it clear on an objective assessment that the taxpayer's aim in undertaking the transaction was to obtain the s 730 benefit. Those factors also demonstrate in our view that the London branch's objective in incurring the expenditure on the right to the dividend was to access the s 730 benefit. This was not a case of the London branch paying £149.1 million with the aim of acquiring an asset for sale in its trade to generate a commercial profit but of spending that amount to obtain a tax benefit with the acquisition and sale of the asset (as designed to achieve a profit) as the necessary steps required to achieve that.

522. That this was the aim of those involved in the project in a subjective sense is very clear from the internal correspondence, the papers prepared for the approvals process and the minutes of the TCC. We note, in particular, the email from Mr Neil Robinson dated 26 October 2005 extolling the tax benefits of the scheme, the email in a similar vein from Mr Scholes dated 11 November 2005 and that of Mr Robinson dated 8 December 2005 noting that "in an uncertain environment where disclosure can lead to a change in law it is critical that we try and source principal deduct transactions (such as Sumatra) when looking to optimize the tax position of the Bank and our clients in the UK" (see [54], [71] and [97]).

523. Whilst there were commercial effects of the transaction, these were introduced and designed with the objective of enhancing the prospect of achieving the s 730 benefit. Whilst the papers prepared for internal approval purposes refer in headline terms to the benefit of the so called "cheap" funding, the focus of the papers is on the tax effect of the transaction. The minutes of the meeting of the TCC reveal no consideration of the commercial merits of the transaction other than the obtaining of the tax benefit. The correspondence and the papers acknowledge that, in fact, the benefit for the BNP group was obtained immediately such that it would be in its interests to terminate the arrangements with ALIL immediately (see [106]). The OF team were remunerated by reference to the potential tax benefit. Mr Demon and Mr Peters both accepted that the transaction would not have happened but for the potential obtaining of the tax benefit and that it was least a main purpose of the transaction. Accordingly, we conclude that the expenditure incurred by the London branch in acquiring the dividend rights from BNP Lux was not incurred wholly and exclusively for the purposes of the trade of the London branch but (at least in part if not solely) for the purpose of obtaining the s 730 benefit for the BNP Group.

Closure notice issue

524. The next issue is whether HMRC are entitled to advance their argument on s 730(3). The amendment which is the subject of the appeal was made by HMRC on the closure of their enquiries into the taxpayer's position in the period in question in a

notice dated 22 October 2010. The dispute is whether this issue falls within the scope of the conclusions and amendments made on issue of the closure notice and thereby within the scope of the appeal proceedings. The parties differ on the correct approach to this issue on the basis of the decision of the Supreme Court in *Tower MCashback LLP 1 and Another v Revenue and Customs Commissioners* [2011] 2 AC 457 and [2011] STC 1143 and more recently by the Court of Appeal in the *Fidex* case.

Statutory provisions

525. HMRC may enquire into a company's corporation tax return under para 24 of schedule 18 to the Finance Act 1998. The provisions in schedule 18 relating to the completion of an enquiry state the following:

> (1) "An enquiry is completed when [an officer of Revenue and Customs] by notice (a "closure notice") [informs] the company they have completed their enquiry and state their conclusions. The notice takes effect when it is issued" (para 32).
>
> (2) The closure notice must:
>
> "(a) state that, in the officer's opinion, no amendment is required to of the return that was the subject of the enquiry, or
>
> (b) make the amendments of that return that are required -
>
> (i) to give effect to the conclusions stated in the notice …" (para 34(2))
>
> (3) "An appeal may be brought against an amendment of the company's return under sub-paragraph (2)." (para 34(3))

526. The tribunal has power, on an appeal made to it, to reduce the amount of an assessment or otherwise the assessment "shall stand good" under s 50 of the Taxes Management Act 1970.

Closure notice and related correspondence

527. In their closure notice issued on 22 October 2010 HMRC said the following:

> "I have completed my enquiry into the company's Tax return for the period 1 January 2005 to 31 December 2005 and my conclusion is as follows: -
>
> [The London branch] is not entitled to a deduction for the amount payable by it to acquire from [BNP Lux] the right to dividends from [HIL].
>
> My calculations are as follows

Loss for the period based on return as amended	£91,091,000
Acquisition costs of the strip (as D31 in comps)	£149,106,000
Revised profit	£58,015,000

Tax due at 30%
£17,404,500

> This notice amends the return to give effect to my conclusions."

528. HMRC sent a letter also dated 22 October 2010 (the "**accompanying letter**") setting out an explanation of their position. This stated the following at the start of the letter:

> "Our contention is that the purchase and subsequent sale of the dividend rights by [the London branch] should both be disregarded for taxation purposes. The return for 2005 as made excludes from taxation the proceeds of the sale of the rights so the adjustment required is to disallow the acquisition costs.
>
> We have alternative grounds for this adjustment, which we have set out below under the headings Ramsay and Lupton."

529. The *Lupton* issue referred to was the argument considered above that the purchase and sale of the right to the dividends was not a trading transaction. The *Ramsay* issue was that "when a realistic view is taken of the facts, the transaction in question does not fall within s 730 purposively construed".

530. To explain the "*Ramsay*" issue further, HMRC quoted quite extensively from the cases on the approach to purposive construction. They then set out the provisions of s 730 and what they considered to be its purpose and specifically the purpose of s 730(3), being to avoid double taxation. Having considered the commerciality (or rather in their view, the lack of commerciality) of the transaction HMRC concluded that:

> "the interposition of [the London branch] into the pre-planned transactions was solely for tax purposes and the evidence supports that [the London branch] hoped to obtain a trading deduction for the cost of purchasing the rights to dividends from BNP Lux whilst claiming that s 730(3) applied to the sale of rights to dividends so that it was not taxed on the sum received from ALIL …
>
> There are two parts to our argument based on our construction of s 730(3). The first is a consideration of what is a realistic view of the facts bearing in mind that that it is permissible to consider a pre-planned series of transactions as a composite and secondly whether in considering the purpose of the legislation here there is scope for the role [of the London branch] to be ignored on the authority of Lord Hoffman in *Macniven* at para 48…
>
> We say that taking a realistic view of the facts section 730(3) is not engaged because there is no prospect of double taxation as a result of the pre-planned composite transaction".

531. HMRC then set out in the accompanying letter the amendments required to the appellant's corporation tax return (by adding the acquisition cost of the dividends back into the computation as set out in the closure notice). They concluded by noting

that they were not pursuing two previous lines of argument including the argument now raised as regards s 730(3):

> "Other Arguments
>
> In our letter of 3 April 2009 we advanced two other arguments, namely that the application of the legislation at Section 730 ICTA 1988 does not permit [the London branch] to treat the sale proceeds from the dividend rights as non-taxable receipts and that if the £150,000,000 receipt is not taxable as a trading receipt by virtue of S 730(3) ICTA 1988 then it would be chargeable to corporation tax as a chargeable gain. We have decided not to pursue these contentions."

Case law

532. In *Tower MCashback*, a limited liability partnership, claimed capital allowances under s 45 of the Capital Allowances Act 2001 in relation to expenditure it claimed it had incurred on a software licence agreement. HMRC opened an enquiry in which they focused on a particular provision in s 45, being s 45(4), which withholds first year allowances for expenditure on software rights "if the person incurring it does so with a view to granting another person a right to use or otherwise deal with any of the software in question". In their closure notice, HMRC said "as previously indicated my conclusion is: the claim for relief under section 45 is excessive". The closure notice was sent with a covering letter which stated: "I am satisfied that the *Tower MCashback* scheme fails on the section 45(4) point alone."

533. HMRC later wanted to rely on a new argument, namely, that the taxpayer had not incurred the expenditure in buying the software licence within the meaning of s 45 because over 75% of the funds needed for the purchase had been borrowed against security provided by the seller on uncommercial terms. The Special Commissioner ruled in favour of HMRC that he had jurisdiction to consider the new argument. Mr Justice Henderson reversed this in the High Court (*HMRC v Tower MCashback LLP 1 and Another* [2008] EWHC 2387, [2008] STC 3366) but the Court of Appeal (*HMRC v Tower MCashback LLP 1 and Another* [2010] EWCA Civ 32, [2010] STC 809) and the Supreme Court decided in favour of HMRC.

534. Mr Justice Henderson made a number of comments which were referred to by the Supreme Court:

> (1) At [113] he noted that there was no express requirement for the officer to set out his reasons for his conclusions and that what mattered "is the conclusion which the officer has reached upon completion of his investigation of the matters in dispute, not the process of reasoning by which he has reached those conclusions."
>
> (2) He said, at [115], that there is a principle of tax law "to the general effect that there is a public interest in taxpayers paying the correct amount of tax……[which] still has at least some residual vitality in the context of section 50" such that the Commissioners must:

> "be free in principle to entertain legal argument which played no part in reaching the conclusions set out in the closure notice. Subject always to requirements of fairness and proper case management, such fresh arguments may be advanced by either side or may be introduced by the Commissioners on their own initiative."

(3) He then said, at [116], that this did not mean that an appeal against a closure notice "opens the door to general roving enquiry into the relevant tax return". Rather:

> "The scope and subject matter of the appeal will be defined by the conclusion stated in the closure notice and by the amendments (if any) made to the return. The legislation does not say this in so many words, but it follows from the fact that the taxpayer's right of appeal under section 31(1)(b) is confined to an appeal against any conclusion stated or amendments made by a closure notice. That is the only appeal which the Commissioners had jurisdiction to entertain."

535. At [128], he noted that "the result may from the Revenue's point of view be characterised as conferring a windfall benefit on the taxpayer" but that another way of looking at the limitation on the scope of the appeal is as "part of the protection given by Parliament to taxpayers under the self-assessment system. There is always a balance to be struck between the interest of individual taxpayers on the one hand and the interest of the State and the general body of taxpayers on the other hand. Parliament has decreed how the balance is to be *struck*…".

536. In the Court of Appeal, the majority of Moses LJ and Scott Baker LJ (with Arden LJ dissenting) largely appeared to agree with the reasoning of Henderson J but reached a different conclusion in applying those principles. Moses LJ also noted the public interest in the correct amount of tax being paid and, at [29], that the self-assessment regime contains a system of checks and balances which, at [31], it is not to be supposed that Parliament intended to be overridden by the retention of a system of "thoroughly uninformative notices of assessment and notices of appeal". He noted, at [31] and [32], that HMRC accepted some restriction being that it is implicit in the statutory scheme that an appeal "is confined to the subject matter of the conclusions and any amendments stated in the notice" (as was held by Dr John Avery Jones CBE in *D'Arcy v Revenue and Customs Comrs* [2006] STC (SCD) 543) but, at [33], "it all depends what one means by the 'subject-matter'."

537. Moses LJ referred, at [34], to Henderson J's comments at [113] and [116] and concluded, at [35], that he was driven (by the relevant provisions in the context of the restrictions imposed on HMRC's power to amend a self-assessment) to the same view as Henderson J:

> "The subject matter of this appeal is defined by the subject matter of the enquiry and the subject matter of the conclusions which close that enquiry. But that statement of principles serves only to give rise to further questions and problems. As this appeal demonstrates, there is likely to be controversy as to how one draws the boundaries of the

> subject matter of the conclusions stated in the closure notice. Are reasons for the conclusion to be distinguished from the conclusion stated, and if so, how?"

538. At [37], he warned against too rigid an approach noting that, as Parliament had not chosen to identify some legal principle on this issue, it would be wrong for the court to attempt to do so and any such statement of principle "is likely to condemn both taxpayer and the Revenue to too rigid a straitjacket" and may "prevent a taxpayer from advancing a legitimate factual or legal argument which had hitherto escaped him or deprive, on the other hand, the public of the tax to which it is entitled."

539. At [38], he said that "with those nebulous observations" he would leave it to the Commissioners (now the tribunal) to identify the subject matter of the enquiry and thus the subject matter of the conclusions in which exercise the tribunal will have to "balance the need to preserve the statutory protection for the taxpayer afforded by notification that the inspector has completed his enquiries and the need to ensure that the public are not wrongly deprived of contributions to the fisc."

540. He continued, at [41], to state that it is to the tribunal that the statute looks to identify what s 28ZA describes as the subject matter of the enquiry:

> "The closure notice completes that enquiry and states the inspector's conclusions as to the subject matter of that enquiry. The appeal against the conclusions is confined to the subject matter of the enquiry and of the conclusions. But I emphasise that the jurisdiction of the Special Commissioners is not limited to the issue whether the reason for the conclusion is correct. Accordingly, any evidence or any legal argument relevant to the subject matter may be entertained by the Special Commissioner subject only to his obligation to ensure a fair hearing."

541. At [42], he expanded on this as follows:

> "Protection of the public requires, at the least, that other issues arising from the subject matter of the enquiry ought to be considered, if necessary, by the fact-finding tribunal. In *D'Arcy* [2006] STC (SCD) 543 at para 11, the Special Commissioner ruled that the scope of an appeal against a conclusion or amendment made by a closure notice will depend on the facts. The conclusion in that case was, as described by Dr Avery Jones, very specific and relied upon the *Ramsay* principle. But the Special Commissioner permitted other issues arising from the facts to be advanced since the tribunal must form its own view on the law without being restricted to what the Revenue stated in their conclusion or the taxpayer states in the notice of appeal (see para 13). I see no reason for confining that view merely to legal issues. Provided a party can be protected from ambush, the only limitation on issues which might be entertained by the Special Commissioner is that those issues must arise out of the subject matter of the enquiry and consequently its conclusion, and be subject to the case management powers to which I have referred."

542. Lord Justice Moses concluded, at [51], that the closure notice did not of itself allow so restricted a view of the subject matter of the appeal as had been decided by Henderson J. Whilst "it did refer to previous correspondence which clearly focused on section 45(4), the closure notice itself was in plain terms a refusal of the claim for relief under section 45".

543. In the Supreme Court, Lord Walker, at [15], approved Henderson J's comments at [113], [115] and [116] of his judgment noting that he had reached his conclusion "despite having correctly made" those observations. He then referred, at [16], to the comments of Moses LJ, at [32] and [41] of his decision, concluding, at [17], that there was "little if any difference" between the majority of the Court of Appeal and Henderson J as to the principles to be applied; the difference was as to the application of those principles. He preferred the approach of Moses LJ.

544. Lord Walker cautioned, at [18], against the decision being taken as encouragement to draft every closure notice in wide and uninformative terms although, "if, as in the present case, the facts are complicated and have not been fully investigated, and if their analysis is controversial, the public interest may require the notice to be expressed in more general terms". As both Henderson J and the Court of Appeal observed, unfairness to the taxpayer can be avoided by proper case management during the course of the appeal. He noted that similarly, Dr Avery Jones observed in *D'Arcy v HMRC* [2006] STC (SCD) 543, para 1:

> "'It seems to me inherent in the appeal system that the tribunal must form its own view on the law without being restricted to what the Revenue state in their conclusion or the taxpayer states in the notice of appeal. It follows that either party can (and in practice frequently does) change their legal arguments. Clearly any such change of argument must not ambush the taxpayer and it is the job of the Commissioners hearing the appeal to prevent this by case management.'"

545. Lord Hope said, at [83], that, as the right of appeal under the relevant provision is against the conclusion stated in or amendment made by a closure notice, "it is desirable that the statement by the officer of his conclusions should be as informative as possible". He noted that the closure notice was in very bald terms and whilst "the statute does not spell out exactly what it means by the words 'his conclusions' … taxpayers are entitled to expect a closure notice to be more informative".

546. He continued, at [84], that such notices "are seldom, if ever, sent without some previous indication during the enquiry of the points that have attracted the officer's attention. They must be read in their context." In that case, as the officer drew attention to his previous indications and sent a covering letter which cast further light on the approach, he did not think that it was unfair to the taxpayers to hold that the issue as to their entitlement to allowances should be examined as widely as may be necessary to determine whether they are indeed entitled to what they have claimed. Furthermore:

> "while the scope and subject matter of the appeal will be determined by the conclusions and the amendments made to the return, s 50 of

> TMA does not tie the hands of the commissioners (now the Tax Chamber) to the precise wording of the closure notice when hearing the appeal."

547. In *Fidex,* the issue was whether under a complex scheme, the appellant had generated an allowable loss of nearly €84 million where Fidex sought to obtain the benefit of a specific rule in the loan relationship provisions (para 19A in the relevant provisions). In their closure notice, HMRC referred only to their argument on that provision but later sought to argue that the debit was not allowable under a different provision in the loan relationship rules. It was held that the tribunal was right to conclude that the subject matter of the enquiry/the closure notice and of the review related to the admissibility of the debit claimed and that the new argument could be raised as an additional ground upholding that conclusion.

548. In setting out a comprehensive review of *Tower MCashback*, Kitchin LJ noted, at [43], that the appellant drew attention to the use by Moses LJ in his judgment of the phrase "the subject matter of the enquiry" but, at [44], that he did not think Moses LJ had meant to expand the permissible scope of an appeal in his use of this phrase beyond that contemplated by Henderson J nor did he understand the Supreme Court to have sanctioned any such expansion. In his view, Moses LJ was, "doing no more than explaining that the closure notice must be considered in context and in light of the enquiry that preceded it".

549. He concluded, at [45], that the principles to be applied are those set out by Henderson J as approved by and elaborated upon by the Supreme Court which, so far as material to that appeal, may be summarised in the following propositions:

> "i) The scope and subject matter of an appeal are defined by the conclusions stated in the closure notice and by the amendments required to give effect to those conclusions.
>
> ii) What matters are the conclusions set out in the closure notice, not the process of reasoning by which HMRC reached those conclusions.
>
> iii) The closure notice must be read in context in order properly to understand its meaning.
>
> iv) Subject always to the requirements of fairness and proper case management, HMRC can advance new arguments before the FTT to support the conclusions set out in the closure notice."

550. He noted, at [51], that in his view the Upper Tribunal had been right not to take too rigid an approach as though this was a question of statutory construction. He agreed with them that "it is not appropriate to construe a closure notice as if it is a statute or as though its conclusions, grounds and amendments are necessarily contained in watertight compartments, labelled accordingly". He also thought they had rightly emphasised that "while there must be respect for the principle that the appeal does not provide an opportunity for a new roving enquiry into a company's tax return", the tribunal is not deprived of jurisdiction "where it reasonably concludes that a new issue raised on an appeal represents an alternative or an additional ground for supporting a conclusion in the closure notice". He said, at [64], that just as Lord Hope observed in *Tower MCashback*, it was not unfair to Fidex to hold that the issue

as to its entitlement to the debit should be examined as widely as might be necessary to determine whether it was indeed entitled to what it had claimed.

Discussion on closure notice issue

551. It is not disputed that it is clear from the principles set out in *Tower MCashback* and *Fidex* that the scope of the appeal in a case such as this is to be determined essentially by the subject matter of the conclusions and amendments set out in the closure notice. As Henderson J said, in the passages from his judgment expressly approved by Lord Walker in the Supreme Court, the tribunal cannot stray beyond that. The courts have emphasised that the tribunal is not merely acting as an arbiter between the parties but in the public interest in determining the correct amount of tax due. Inevitably, the exercise involves balancing the protection for the individual and the public interest in the payment of the right amount of tax. So, whilst the legislature has, as Henderson J noted, provided for the drawing of a line by reference to the subject matter of the conclusions, precisely where to draw that line, taking into account this balancing exercise, is left to the tribunal to determine on the facts of the particular case.

552. We note that Lord Walker, like Moses LJ, approved the comments of Dr Avery Jones in the *D'Arcy* case that it is "inherent in the appeal system that the tribunal must form its own view on the law without being restricted to what the Revenue state in their conclusion or the taxpayer states in the notice of appeal" and that it followed that "either party can (and in practice frequently does) change their legal arguments" although "clearly any such change of argument must not ambush the taxpayer and it is the job of the commissioners hearing the appeal to prevent this by case management".

553. As Lord Hope said, closure notices "must be read in their context" and section 50 does "not tie" our hands "to the precise wording of the closure notice" when hearing the appeal. As the Upper Tribunal said, as approved by Kitchin LJ in the Court of Appeal in *Fidex*, it is not appropriate "to carry out this exercise as though it were a matter of statutory construction or as though its conclusions, grounds and amendments are necessarily contained in watertight compartments, labelled accordingly".

554. BNP argued that the statement by HMRC in the closure notice is the entirety of the subject matter of the conclusion, namely, that the price paid by the London branch for the dividend rights was not deductible. The amendment made by the exclusion of the purchase price from the tax computation as a tax deductible amount is entirely consistent with this conclusion. Moreover, HMRC expressly said in the accompanying letter that they were not pursuing the s 730(3) argument.

555. BNP referred in particular to the passages from the judgment of Henderson J approved by Lord Walker in *Tower MCashback* and the summary set out by Kitchin LJ in *Fidex*. BNP asserted that, on that approach, whilst the assessment has to be made in context, it is the conclusion as set out in the closure notice which is paramount. In BNP's view, Lord Justice Kitchen's fourth proposition makes it clear that the question of jurisdiction and of fairness or case management are two entirely separate questions. It is only if the tribunal has jurisdiction to hear a particular

argument, on the basis that it is within the subject matter of the conclusion, that any question of fairness or prejudice can arise. Questions of fairness do not arise here as that prior jurisdictional test is not satisfied.

556. HMRC argued that, looking at the issue in the broader context of the correspondence, the subject matter of this appeal is the tax efficacy of the arrangements put in place by the BNP group. Section 730(3) has always been in issue; initially this was by reference to *Ramsay* as set out in the accompanying letter and review correspondence. There is no unfairness in requiring BNP to satisfy the tribunal on the s 730 score given the public interest in ensuring the correct payment of tax. The fact that this would involve altering the computations made in the closure notice is immaterial. These were produced on the basis of HMRC's primary case that the transaction was not a trading transaction.

557. HMRC referred to the approach set out by Moses LJ in the Court of Appeal in *Tower MCashback*. They considered that Lord Walker approved not just the conclusion of Moses LJ but also his reasoning. In their view, his judgment gives greater emphasis to the context, being in this case the relevant chain of correspondence leading up to the closure notice and in any review, and that this is not a question of arid construction. Moreover, it is clear that the public interest in the right amount of tax being paid is relevant to the question of the tribunal's jurisdiction as regards the very scope of the appeal as well as to case management issues of fairness.

558. They noted that the argument HMRC wish to raise does not raise any new issue of fact but is purely a question of law. Lord Walker suggested in *Tower MCashback* that, as is consistent with the tribunal's duty to determine the correct amount of tax, the tribunal cannot be confined to whatever the parties have said about the correct legal interpretation of a particular provision. In determining the subject matter of this appeal, it is not possible to separate the sale of the right to the dividends from the purchase of those rights. The appellant has to show that this was a trading transaction by reference to both limbs of the transaction. The appellant's scheme hinges, assuming this was a trading transaction, on the proceeds of the sale not being taxable under s 730(3). That is a pure question of the construction of s 730 as a question of law. It arises out of exactly the same facts which justify, on the appellant's case, treating the expenditure on the acquisition of the dividend rights as trading expenditure. From the correspondence, it is clear that the grounds of dispute put by HMRC related to both limbs of the transaction.

559. We note that the parties seem to suggest that there is a difference in approach between Henderson J and Moses LJ and as to whether the Supreme Court was fully endorsing the comments of Moses LJ. As raised in *Fidex*, Moses LJ referred several times to the need to have regard to the subject matter of the enquiry. At [41] of his judgment, he said that the tribunal must have regard to "the subject matter of the enquiry" as "the closure notice completes that enquiry and states the inspector's conclusions as to the subject matter of that enquiry". The only limitation, as he continued at [42], on what might be entertained "is that those issues must arise out of the subject matter of the enquiry and consequently its conclusion".

560. As Kitchin LJ said in *Fidex*, it does not seem, however, that Moses LJ intended to broaden the scope of the exercise beyond that described by Henderson J nor did he consider that the Supreme Court sanctioned any such extension. We note that Moses LJ was clearly of the view that the context of the subject matter of the enquiry may be highly relevant but, in each case, he focussed on the fact that the closure notice completes that enquiry. We take this to mean that the conclusions in the closure notice are to be informed by the subject matter of the previous enquiry, as the document bringing the enquiry to an end. This accords with the view of Lord Justice Kitchin that Moses LJ was simply doing no more than explaining that the closure notice must be considered in context and in light of the enquiry that preceded it. That Henderson J regarded context as relevant is inherent in his decision, which was essentially based on what was said in the surrounding correspondence, as limiting the scope to s 45(4).

561. In broad terms, as is clear from the amendment made by the closure notice and the related correspondence, the matter in dispute was whether the transaction had created an allowable trading loss of over £91 million which could then be surrendered by way of group relief. The amendment made by HMRC wiped out the claimed loss and produced a profit. This was achieved by HMRC adding back into the computation the amount of just over £149 million spent by the London branch on acquiring the dividend rights. The issue is essentially whether the statement in the closure notice, that the amount spent on the dividend right was not deductible, represents the entirety of HMRC's conclusion or is merely an argument or grounds for some broader conclusion.

562. Having regard to the context in which the closure notice was issued and, in particular, the statements in the accompanying letter, we agree with HMRC that it is clear that the factual scope of the matter in dispute when the closure notice was issued was not confined to the purchase side of the transaction only. Indeed, as HMRC argued, by its very nature the scope of the subject matter cannot be so confined.

563. HMRC concluded in the accompanying letter that the purchase and sale of the dividend rights should both be disregarded for taxation purposes. As the taxpayer's computation did not take into account the sales proceeds, the adjustment required was to add back in the purchase price. The rest of the letter sets out the grounds for that conclusion being (a) that the purchase and sale was not a trading transaction (on the authority of *Lupton*) and (b) alternatively that, as a matter of purposive statutory construction, on a realistic view of the facts, the purchase and sale of the dividend rights by the London branch was to be disregarded (the *Ramsay* argument). Under the *Ramsay* argument their view was that, on a purposive construction of s 730, the terms of s 730 (3) were never engaged as there was no question of double taxation (as set out in further detail above). Whilst we find HMRC's *Ramsay* argument somewhat difficult to follow, it is clear that they were basing it, whatever the merits of the argument, on their interpretation of a purposive approach to the construction of s 730, including s 730(3), albeit that their view was that the provision was simply not engaged.

564. It is clear from this correspondence that the focus of HMRC's enquiry and of the conclusion they then reached was on whether the transaction, being the purchase and sale of the right to the dividends by the London branch, resulted in an allowable trading loss of over £91 million as the London branch claimed. At the point when the closure notice was issued, they had two reasons for asserting that it was not, both of which looked at the taxation of the transaction in its entirety.

565. On that basis, we do not regard the conclusions or amendment set out in the closure notice, as assessed according to the context of the enquiry and related correspondence, to be confined to the narrow point that the London branch was not entitled to a tax deduction for the price paid for the dividend rights. Looked at in context, HMRC concluded the enquiry by taxing the transaction as though it were not a trading one or as though it is to be disregarded for fiscal purposes.

566. The result, in each case, is that there is no trading loss. The mechanics of denying the loss were to add back into the computation the price paid by the London branch for the acquisition of the dividend rights. In our view, the argument that s 730(3) does not operate, as BNP asserted, to exclude the proceeds of the sale of the transaction from the corporation tax computation, is simply another argument which supports the conclusion that the transaction has not created an allowable loss. The fact that a different mechanic would be needed to achieve that result, if the argument were to succeed, by adding the proceeds of sale into the computation is immaterial given that the overall result would be the same.

567. Given that, in our view, this argument can be raised within the scope of the conclusions embodied by the closure notice as interpreted in its context, the only remaining considerations are case management ones such as avoiding any ambush. However, there is no such concern in this case. The appellant has had sufficient time to consider this argument and indeed it does not raise any argument to the contrary. We also note that we do not consider that, as a matter of principle, there can be any difference between the raising of a wholly new argument and the reviving of an argument that had been raised but dropped. In each case, having decided that it is within the tribunal's jurisdiction to hear the argument, the only considerations preventing it from being heard would be case management ones.

Section 730 issue

568. We turn finally to the substantive issue on the application of s 730(3). Essentially, the issue is whether s 730(3) applies to prevent the proceeds from the sale of the right to the dividends from being taxed in the hands of the London branch.

569. Section 730 had its roots in s 24 of the Finance Act 1938 which, as was common ground, was enacted in response to the decision of the Court of Appeal in *IRC v Paget* 21 TC 677. In that case, it was held that the proceeds of sale of interest coupons on bonds held by Miss Paget as investments were not taxable as income. The provisions were anti-avoidance measures designed to prevent investors alienating rights to interest on securities (whilst retaining the securities themselves), normally

for a capital sum, thereby avoiding the charge to income tax, which would be imposed on the receipt of the interest itself.

570. That this was the intention behind s 730 is acknowledged in the explanatory notes to the draft legislation which, when subsequently enacted (as para 2 of Schedule 7 to the Finance (No 2) Act 2005), made a number of changes to s 730 to produce the version in force when the transaction took place (the "**applicable version**"). The notes state:

> "Section 730 ICTA 1988 prevents avoidance of tax where a person sells or transfers the right to income from a security without selling or transferring the security itself. It reverses a court decision in the 1930s that the proceeds of sale of such income were not taxable."

Provisions of s 730

571. We have set out below the full text of the applicable version and highlighted the main differences with the version which was in force immediately before that (the "**preceding version**"), by including the previous wording in the applicable version in italics.

> "730 Transfers of rights to receive distributions in respect of shares
>
> (1) Where in any chargeable period the owner of any shares [*securities*] ("the owner") sells or transfers the right to receive any distribution [*interest*] payable (whether before or after the sale or transfer) in respect of the shares [*securities*] without selling or transferring the shares [*securities*], then, for all the purposes of the Tax Acts, that distribution [*interest*], whether it would or would not be chargeable to tax apart from the provisions of this section –
>
> (a) shall be treated as [*shall be deemed to be*] the income of the owner or, in a case where the owner is not the beneficial owner of the shares [*securities*] and some other person ("a beneficiary") is beneficially entitled to the income arising from the shares [*securities*], the income of the beneficiary, and
>
> (b) shall be treated as [*shall be deemed to be*] the income of the owner or beneficiary for that chargeable period, and
>
> (c) [*shall not be deemed to be the income of any other person*]
>
> (2) This section does not have effect in relation to a sale or transfer if the proceeds of the sale or transfer are chargeable to tax. [*For the purposes of subsection (1) above, in the case of a sale or other realisation the proceeds of which are chargeable to tax by virtue of section 18(3B) the interest so deemed to be the income of the owner or beneficiary shall be deemed to be equal in amount to the amount of those proceeds*.]
>
> (2AA) [*This section does not have effect for the purposes of Chapter 2 of Part 4 of the Finance Act 1996 (loan relationships)*.]
>
> (3) The proceeds of any subsequent sale or other realisation of the right to receive the distribution shall not, for any of the purposes of the Tax

Acts, be regarded as the income of the seller or the person on whose behalf the right is otherwise realised. [*Nothing in subsection (1) above shall affect any provision of this Act authorising or requiring the deduction of income tax –*

(a) from any interest which, under that subsection, is deemed to be the income of the owner or beneficiary, or

(b) from the proceeds of any subsequent sale or other realisation of the right to receive that interest;

but the proceeds of any such subsequent sale or other realisation shall not, for any of the purposes of the Tax Acts, be deemed to be the income of the seller or the person on whose behalf the right is otherwise realised.]

(7) In this section –

'distribution', in relation to shares in a company, -

(a) has the same meaning as it has in the Corporation Tax Acts (see section 209), but

(b) also includes any amount that would a distribution if the company paying it were resident in the United Kingdom;

'shares' means shares in a company."

[*In this section –*

'interest' includes dividends, annuities and shares of annuities, and 'securities' includes stocks and shares."]

572. As highlighted above, the main changes made in 2005 to the preceding version to produce the applicable version, as explained in the explanatory notes issued at that time, were as follows:

(1) The explanatory notes introduce the provisions which include the relevant changes by stating that they "close a number of loopholes and block a number of avoidance schemes disclosed under part 7 Finance Act 2004 and elsewhere... the main categories of effective schemes are ones which convert interest-type income into a capital gain or an untaxed receipt."

(2) The provisions originally related to both sales of dividends/distribution and interest coupons. However, the extension of the loan relationship rules applicable to securities meant that it was no longer necessary for s 730 to apply to sales of interest on securities (as set out at notes 26 and 27 of the explanatory notes). So s 730 was changed to confine its scope in the applicable version to sales of income distributions on shares/stock. Hence the amendment of the relevant definitions.

(3) No real explanation is given in the notes for the removal of the previous s 730(1)(c) which provided that the income distribution which was deemed to be taxable under s 730(1) was not to be deemed to be the income of any other person. It was merely stated, at note 17,

that the relevant provision "removes the non-application of any tax charge on the recipient of the actual dividend."

(4) A new s 730(3) was introduced which, at 20 of the notes, was stated to be needed to "ensure that there is no double taxation on the sale of coupons".

(5) The changes from the previous wording in various places from "shall be deemed to be" to "shall be treated as" were stated in the notes to be to modernise the language.

(6) The change to sub-s (2) was stated to be to reflect changes made by the Income Tax (Trading and Other Income) Act 2005 and reverse the order of priority as between other charges on the sale of coupons. The other charges referred to appear to be those under the dividend investment provisions which tax the proceeds of sale of dividends on non-UK investments in certain circumstances.

Discussion on s 730 issue – submissions

573. BNP did not dispute that the aim of an exercise of statutory construction is to discern what Parliament intended, but that intention has to be discerned from the words chosen and, in this case, the wording of s 730(3) is clear and unambiguous. The very broad wording clearly covers income received in the form of trading income which would otherwise be taxable as such. The provision, therefore, excludes the proceeds of the sale of the right to the dividends realised by the London branch from the scope of s 730(1).

574. BNP said that there is no indication in s 730 that it is not to apply to financial traders. On the contrary, the very broad references in sub-s (3) to "any subsequent sale" of the dividend coupon and that the proceeds of any such sale are not to be regarded as the income of the person "for any of the purposes of the Tax Acts" suggest it applies to traders. The most obvious person who would fall within this is a trader and the most obvious head of charge is that on trading income. Indeed, leaving aside the provisions of s 18(3B) ICTA and Chapter 1 Part 4 ITTOIA 2005 (the "**foreign dividend provisions**") to which HMRC referred, there does not appear to be any other relevant head of charge which could be in point.

575. The appellant considered that this interpretation is supported by the House of Lords' decision in *Hughes*. The issue in that case was whether trading receipts, which comprised interest income, were exempt from tax under provisions which allowed the Treasury to issue securities with a condition that interest thereon "*shall not be liable to tax or super tax*" and the rule made thereunder that "*no tax shall be chargeable in respect of* … [broadly, certain interest or dividends on certain securities belonging to non-UK residents]". Lord Thankerton rejected, at [374], the argument that the relevant provisions merely exempted relevant interest paid to non-UK residents from the head of charge for interest "qua interest" (under schedule D case III) and did not exclude it from being taken into account as a trading receipt in the computation of trading profits (under schedule D case I).

576. HMRC argued that, on a purposive approach, looking at the history of the provision, as an anti-avoidance provision introduced in response to *Paget,* and the limited intended effect of the changes made in 2005, it cannot be the case that Parliament intended to create the effect that BNP's interpretation would have. It is clear from the language used in the preceding version, that it would not have had that effect. BNP's approach is based on a literal and strained construction of the statutory language, without proper regard to the legislative history and purpose of the relevant provisions. Such an approach is outdated and unpersuasive in the light of the modern approach to statutory interpretation as, set out in *Barclays Mercantile Business Finance Ltd v Mawson* [2005] 1 AC 684 and, most recently, in *UBS AG v Revenue and Customs Commissioners & DB Group Services (UK) Ltd v Revenue and Customs Commissioners [2016] UKSC 13, [2016] 1 W.L.R. 1005* (see Lord Reed at [61]).

577. HMRC referred to the limited effect the changes to the provisions were intended to have, as set out in the explanatory notes. They noted, in particular, that the notes described the purpose of the specific change to s 730(3) as being "to ensure that there was no double taxation on the sale of the coupons". They asserted that it is clear that explanatory notes may be taken into account as an aid to construction from the case of *R v Montila* [2004] 1 WLR 3141 where the House of Lords, at [35], approved what Lord Steyn said in *Westminster City Council v National Asylum Support Service* [2002] UKHL 38.

578. In HMRC's view it is clear that, as both the explanatory notes and statutory language reveal, s 730 is not addressing the situation where any proceeds fall within the computation of a trader's trading profits. It is aimed at cases where a sale of the right to future dividends would, absent s 730(1), give rise to a capital receipt and where it is, therefore, appropriate to treat the full amount of the dividend comprised within the coupon as the income (not merely a trading receipt) of the relevant person (under s 730(1)). This is not necessary as regards a financial trader, for whom the proceeds of any sale of the distribution would constitute a trading receipt in any event. The provision in sub-s (2), that s 730 is not to apply where the proceeds of a sale or transfer are chargeable to tax, is broad enough to cover proceeds comprising receipts which are brought into account in computing a trader's taxable income. As noted, the purpose of s 730(3) was to avoid double taxation in this situation but there is no such concern where the re-seller is a financial trader.

579. The wording of the provision does not, as BNP asserted, indicate that sub-s (3) is intended to apply to traders; investors also purchase and subsequently sell financial instruments. On the contrary the "proceeds of sale" on the sale by a trader of a right to a distribution would not normally be regarded as "the income" of the trader but simply as a receipt that is taken into account in computing that income, after deduction of expenses. Accordingly, the inference is that sub-s (3) applies only where a subsequent sale is not by way of trade but the proceeds would otherwise be treated as taxable income arising to the seller, such as under the foreign dividend provisions. The function of s 730(3) is simply to prevent those charges arising.

580. HMRC referred in particular to the use of the term "the income" of the subsequent seller as indicating that sub-s (3) simply does not apply where a person

receives a trading receipt as opposed to pure income profit. HMRC noted that Parliament did not use the broader wording that the proceeds of any subsequent sale cannot be "chargeable to tax" (the language used in sub-s (2)). The principle that a trading receipt is not "income" is well established in the UK tax code; it is only the overall profit of a schedular computation which is treated as income under the Tax Acts (as Hoffmann J held in *George Wimpey International Ltd v Rolfe (Inspector of Taxes)* [1989] STC 609 at 615). The distinction between income and income receipts has long been recognised in respect of coupons/dividends and financial traders. This was a point made by Lord Romer in the *Paget* case itself and also in *Cenlon Finance Co Ltd v Ellwood (Inspector of Taxes)* [1962] AC 782 (per Lord Reid at 795).

581. HMRC regarded the decision in *Hughes* as of no assistance to the appellant. They noted that the wording used in the relevant provisions was very different to that in sub-s (3); it stipulated either that the interest would not be "liable to tax" or that "no tax shall be chargeable" in respect of interest. Moreover, it was found that the legislation in issue clearly manifested an intention on Parliament's part to exempt the interest from income tax (the purpose being to encourage non-residents to invest in gilts). *Hughes*, therefore, provides no help in the construction of this provision given the different wording and purpose of the legislation in issue.

582. In HMRC's view their interpretation is supported by the more recent authority of the Court of Appeal's decision in *Vojak (Inspector of Taxes) v Strand Options & Futures Ltd* [2003] EWCA Civ 1457 [2004] STC 64 ('*Strand Options*'). In that case, the dispute was whether s 208 ICTA 1988 provided an exemption from corporation tax on chargeable gains. Section 208 stated:

> "208 Except as otherwise provided by the Corporation Tax Acts, *corporation tax shall not be chargeable on dividends and other distributions* of a company resident in the United Kingdom, nor shall any such dividends or distributions be taken into account in computing income for corporation tax."

583. The dispute was whether the wording that corporation tax "shall not be chargeable on … distributions" applies only where the distribution is a pure income receipt or also where it is included as part of a chargeable gain. The court agreed with HMRC that the words "chargeable on … distributions" suggest a tax which is directly charged on dividends/distributions as such, rather than charged only indirectly when the income is included in and is part of the computation of a taxable amount. They said this was reinforced by the contrast with the second part of s 208, which refers specifically to dividends or distributions being "taken into account in computing income". In a capital gains context, the distribution is not directly the subject of tax, but is one element taken into account in computing the chargeable gain. If it had been intended to exclude it from the capital gains computation, it would have been "more natural to do so by including a specific reference to chargeable gains in the second part of s 208…"

584. In HMRC's view, there is a strong analogy between the reasoning in *Strand Options* and their position in this case. As in that case, there is a distinction to be drawn between the taxability of the dividend/distribution as pure income and as one

element of the overall computation of a trader's profits. That the legislature has stated that the relevant proceeds shall not be regarded as "*the income*" of the relevant person and has not used the broader formula, that they are not to be taken into account in computing income, clearly indicates that the provision only applies to prevent them being taxable as income as such. It does not prevent such proceeds from being brought into account as one element in a trader's overall trading income computation under schedule D case I. Had that been the intention, the legislature could have used the broader formula (as in the second part of s 208) but has not done so.

585. HMRC also noted that, in *Strand Options*, the Court of Appeal rejected the taxpayer's reliance on the *Hughes* case. At [19], Carnwath LJ said he did not find this a helpful authority in the present context as, as the Judge had said in the High Court, "the Court's interpretation of completely different tax statutes, relating to different subject matter and dating from a completely different era, can only be, at best, of marginal assistance in the interpretation of TA 1988 s 208."

586. BNP countered that the history of s 730 cannot be of material assistance given it has undergone substantial changes, including major changes from the preceding version to the applicable version. Moreover, whilst s 730(1) is an anti-avoidance provision (which in effect deals with future Miss Pagets), sub-s (3) itself is concerned with avoiding double taxation as regards a person who purchases the relevant distribution rights and sells them on.

587. BNP noted that, on HMRC's interpretation, s 730(3) would be limited to apply solely to non-dealers in coupons who purchase and subsequently sell rights to distributions on shares in foreign companies by way of investment (on the basis it applies only where the foreign dividend provisions apply). If that was really what the draftsman of sub-s (3) intended, the provision could simply have said so. The draftsman must have been aware of the foreign dividend provisions as they were specifically referenced in the preceding version (see the previous sub-s (2)). It appears, therefore, that the draftsman chose to express sub-s (3) in the widest possible terms.

588. BNP asserted that HMRC's position, that sub-s (2) is broad enough to exclude traders from the scope of s 730(1) (on the basis that in their hands "the proceeds of the sale or transfer are chargeable to tax") but that such traders are not within sub-s (3), is inconsistent. Both sub-sections concern the taxability of the proceeds of sale; if traders come within the ambit of sub-s 2, they must logically also fall within sub-s (3).

589. In BNP's view, if it is accepted that s 730(3) applies in principle to financial traders, it must follow that that the relevant proceeds of sale are not to be regarded as a taxable trading receipt in the trader's hands. Such proceeds of sale can never be "pure income profit" in the hands of a trader because the purchase price and other expenses are set against the proceeds. On HMRC's interpretation, therefore, s 730(3) would never in practice apply which cannot be the intention. There is nothing in the language of the provision to suggest that, in this context, "income" should be limited to "pure income profit". Indeed, the use of the word "proceeds" makes it clear that the provision is concerned with receipts rather than profits.

590. In BNP's view HMRC's interpretation involves speculating as to the intention behind the provisions or assuming what the intention is and then seeking to strain or rewrite the words of the statute to make the two align. However, Chadwick LJ warned against that approach in the Court of Appeal decision in *Frankland v IRC* [1997] STC 1450 at page 1464 (in the context of inheritance tax but the principle is of universal application). He said that whilst legislation must be construed in its statutory context and with due regard to the purpose which the legislature may be taken to have been seeking to achieve:

> "that purpose must, I think, be identified in the legislation itself and in any other relevant and admissible material. It is not permissible to speculate, a priori, as to what the legislature must or might have intended, and then strain the statutory language used in order to give effect to that presumed purpose."

591. HMRC responded that BNP's interpretation gives rise to absurd results. The tribunal must adopt an approach that avoids the absurdity that BNP's interpretation produces as was set out by Neuberger J (as he then was) in *Jenks v Dickinson (Inspector of Taxes*) [1997] STC 853 at 870 and as indicated in the cases of *Luke v IRC* [1963] AC 557 (at 577), 40 TC 630 at 646 and *O'Rourke (Inspector of Taxes) v Binks* [1992] STC 703 at 579–580, 40 TC 630 at 648. Unlike some of the cases cited by Neuberger J, in this case the tribunal does not have to use a strained interpretation. Rather, it merely needs to give proper consideration to the words that Parliament has used in s 730(3), having regard to the legislative purpose of both the original provision and the amending provision. HMRC are not starting with an a priori assumption as to what the provisions mean. They are simply looking at the statutory context and at the actual wording of the provision. On that basis, it is clear that "the income" means effectively pure income profit. When the Parliamentary draftsman wants such an amount to be excluded also from being taken into account in computing income or computing gains, there is a well-established form of wording which is normally followed (as in s 208) but that is not used here.

592. BNP said that, even if there were such an anomaly as HMRC suggest, that cannot justify HMRC's construction of s 730(3), the wording of which is absolutely clear. If, on a proper construction of those words, their application leads to a particular result, then that result has to be respected even if it could give rise to the outcomes which HMRC assert are anomalous unintended results. There are occasions where the legislation simply gives rise to such results, particularly, as regards overlapping codes of complexity, such as, the interaction of s 730 with the rules about deduction of expenditure. This was recognised by Henderson J in *D'Arcy* at [47] and recently in *Bowring and another v Revenue and Customs Commissioners* [2016] STC 816 where Mr Justice Barling said one cannot, and should not "... strain the ... clear meaning and effect of the legislation, to the extent which would be necessary to produce the outcome for which [HMRC] argued."

593. The absurd results which HMRC referred to are that, in their view, on BNP's approach, s 730(3) would apply in circumstances where there is no risk of double taxation and would open the door to multiple avoidance of tax. On BNP's interpretation, a share dealer who is the first to sell the coupon (but retains the shares),

would realise taxable income equal to the amount of the distribution (under s 730(1)) but the second and any subsequent share dealers who acquire and sell the coupon would enjoy a fiscal windfall. Each such trader could deduct the cost of acquisition but, on the appellant's view of s 730(3), could exclude the receipt from the trading computation, thereby almost guaranteeing the realisation of a trading loss which bears no reality to the financial outcome for the trader. These are manifestly absurd results which cannot have been the intention of Parliament.

594. BNP responded that the position HMRC set out is not, in fact, generally the result which follows from its interpretation. In a typical case, whilst a financial trader would obtain a deduction for the purchase price paid for the acquisition of the dividend right for the purposes of his trading computation, he would be liable to tax on a chargeable gain computed by reference to the proceeds of sale. That is because s 730(3) does not exclude the proceeds from being taxed as a chargeable gain and the trader would not obtain a deduction in the capital gains computation for the purchase price (under s 37(1) and s 39(1) TCGA.) The London branch only escapes this charge because it is not within the scope of corporation tax on capital gains as regards the sale of the right to dividends.

595. HMRC saw two difficulties with BNP's analysis.

(1) There is no rational explanation why Parliament would have intended to create a hybrid asset, as is the result of BNP's analysis. Particularly in relation to individuals, income tax and capital gains tax have materially different rules for the recognition of receipts and expenditure, the availability of reliefs, the use of losses and the rates at which tax is charged. A policy of allocating receipts and expenditure relating to the same asset to different taxes would be guaranteed to result in complexity and anomaly.

(2) On BNP's analysis, a non-resident carrying on a trade through a permanent establishment in the UK could deduct the cost of a right to dividends in computing the trading profits of the permanent establishment but would fall outside the scope of any charge to tax on the proceeds of sale altogether (as it would not be within the scope of tax on chargeable gains). There is no rational reason why Parliament would want to create such a situation.

596. BNP asserted that HMRC's construction would result in the very double taxation which the explanatory notes state s 730(3) is intended to avoid. A "subsequent" trader would be liable to tax on the proceeds of sale notwithstanding the proceeds reflect the value of the dividend on which the original seller is taxed. The final purchaser who actually receives the dividend would also be subject to income tax on the income (assuming he acquired the right on investment account) because of the repeal of the previous s 730(1)(c). Excluding the proceeds of sale realised by the trader from tax in such circumstances has precisely the intended effect of avoiding double taxation. In this case, BNP Lux is not potentially taxable under s 730(1) in any event because it is not within the scope of UK tax on the receipt (under s 151 of

the Finance Act 2003). But that does not make any difference to the proper interpretation of the provision (and HMRC do not suggest that is the case).

597. HMRC noted that the "subsequent" trader would only be taxable on the real surplus or loss generated from the purchase and re-sale of the right to the dividend (and not the amount of the dividend itself); the profit/loss would be computed in the usual way with the financial trader obtaining a tax deduction for the price it paid to acquire the dividend rights. They agreed that, following the repeal of s 730(1)(c), the dividend could be taxable as income in the hands of the actual recipient in accordance with normal principles. However, in their view, the incidence of double taxation is likely to be more theoretical than real; in most circumstances, either the transferor or the transferee (or both of them) are likely to be outside the charge to tax in respect of such dividends. As the House of Lords' decision in *R v Dimsey* [2001] UKHL 46 [2001] STC 1520 (at [56] to [60]) shows, in the context of an anti-avoidance provision, such largely theoretical possibilities should not distort the construction of the provision. HMRC concluded that in any event, BNP's construction of sub-s (3) does nothing to remedy such possibilities. It applies only to the proceeds from a subsequent sale or realisation of the right to the dividend, it does not impact on the taxation treatment of the recipient of the actual dividend.

Discussion and conclusion

598. There is no dispute that under the modern approach to the interpretation of tax legislation, as is well established in case law, we must apply a purposive approach to the interpretation of s 730(3). In our view, looking at s 730(3) in the overall context of s 730, the wording used indicates that it does not apply to exempt a trader, who makes a subsequent sale of a right to a distribution, from tax on any trading profit realised on that sale as computed under the normal rules.

599. As noted and as was common ground, s 730 was introduced to prevent investors realising a capital profit on the sale of an income stream. Although the section has been changed a number of times over the years, there is no reason to think that the rationale for its existence changed. The explanatory notes issued in relation to the applicable version cite that as the reason for the provision.

600. Section 730(1) provides that where the owner sells or transfers the right to receive any distribution in respect of shares without a sale/transfer of the shares then "that distribution … shall be treated as the income of the owner [or of the beneficial owner of the income]". This is clearly aimed at rendering the distribution itself taxable as such in the hands of the owner. Section 730(2) provides that s 730 does not have effect in relation to a sale or transfer of the right to a distribution, without a sale/transfer of the shares, if the proceeds are chargeable to tax. Where the owner is a trader the proceeds of the sale of the right are chargeable to tax in the trader's hands in that they are brought into account in the computation of his trading profits in the usual way. It is clear, therefore, that the combined effect of these sub-sections is that a trader is not within the scope of a charge under s 730(1). That accords with the rationale of preventing the conversion of what would otherwise be income receipts into capital returns.

601. To recap, s 730(3) provides that "the proceeds of any subsequent sale or other realisation of the right to receive the distribution shall not, for any of the purposes of the Tax Acts, be regarded as the income of the seller or the person on whose behalf the right is otherwise realised".

602. There was similar wording in the preceding version although it was more limited in scope. In summary, the previous provision stated that nothing in s 730(1) prevented the deduction of income tax from interest which was deemed under that section to be the income of the owner or from the proceeds of any subsequent sale of such a right to interest but that such proceeds shall not, "for any of the purposes of the Tax Acts, be deemed to be the income of [the relevant party]". The relevant wording only applied, therefore, to the proceeds of a subsequent sale of interest income. The deeming wording indicates that such proceeds, which would otherwise be taxable in the hands of the relevant party (such as where they were in any event taxable as trading income), would remain so taxable. The concern appeared to be that such proceeds would not be deemed to be taxable as interest income as such. In the preceding version, therefore, s 730(3) was not providing a trader, who buys and sells a right to income, with a blanket exemption from tax on the proceeds of sale.

603. The explanatory notes state that the aim of s 730(3) in the applicable version is to ensure that there is "no double taxation on the sale of the coupons". We consider that, from the wording of the provision itself and in the context of the clear meaning of the other provisions of s 730(1), the better interpretation of this provision is that it is confined to preventing the proceeds of sale from being taxed as though they are "the income", in the sense of pure income profit, such as a distribution, of the relevant recipient. We accept that, as argued by HMRC, due to the operation of the schedular system as in place at the time, there is a distinction between a trading receipt which is brought into account as an element in computing a trader's overall trading income and a pure income receipt such as a distribution or interest income. The reference to the proceeds falling within s 730(3) not being regarded as "the income" of the relevant person implies that it is only the prevention of a charge on the relevant proceeds as pure income which is covered.

604. We do not consider that this is a strained interpretation of the wording used. It is simply the outcome of applying a purposive approach in this case. The interpretation we adopt leads to the result that a trader is largely unaffected by the s 730 rules and simply taxed on the resulting profit from the buying and selling of the dividend rights in the usual way. This is in accordance with the aim behind the legislation of preventing tax avoidance by investors in effect converting income into capital. It accords with the fact that a trader is clearly excluded from any charge under s 730(1) on the basis that the proceeds are taxable in the trader's hands in any event. On the other hand, BNP's approach produces the manifestly absurd result that a trader who first sells the dividend rights is outside the scope of the main charging provision, such that he is taxed in the normal way on any resulting profit, but any subsequent trader who buys and sells the right would be wholly outside the scope of any tax charge whatsoever. Nor do we see that the provisions can be said, on BNP's interpretation, to operate to prevent a double charge to tax in the intended way where, for example, the subsequent trader buys the right from an investor who is within the

scope of s 730(1). It remains the case that it would be wholly out of kilter with the overall operation of these provisions for a subsequent trader to escape any tax charge on the proceeds of sale it realises.

605. We find it very difficult to see that the legislature intended the meaning of the provision which BNP argued for on the basis that the otherwise manifestly absurd tax effects would be "made good", as BNP asserted, through the combined effect of the income and capital gains rules. Such a hybrid approach would be highly unusual and of itself gives rise, as HMRC noted, to a number of problems.

606. We appreciate that this interpretation means that, in practice, the application of s 730(3) is limited to cases where the dividend income provisions apply which is a narrow range of cases. However, we do not see that of itself affects matters. Section 730 is a relatively narrow anti-avoidance provision applicable in limited circumstances. That there are only limited situations in which there could be a double tax charge on the sales proceeds as "income" is not perhaps surprising.

607. In our view, the *Hughes* case does not add to the debate given the different wording in issue and the purpose of those rules. Similarly *Strand Securities*, as a decision on the interpretation of a different set of provisions on the particular wording used, can only be of limited assistance. We have based our decision on the interpretation of the wording used in this provision as set out above.

Conclusion

608. For all the reasons set out above, we have concluded that.

(1) The transaction comprising the purchase and sale of the right to the dividends by the London branch was not undertaken by it in the course of its financial trade.

(2) In any event, the price paid by the London branch for the acquisition of the right to the dividends was not incurred wholly or exclusively for the purposes of the London branch's trade but at least in part (if not solely) for the purpose of realising the s 730 benefit.

(3) HMRC are entitled to raise the s 730(3) argument.

(4) Section 730(3) does not operate to exclude the proceeds of sale realised by the London branch on the sale of the right to the dividends to ALIL from being brought into account in the computation of its trading income for corporation tax purposes.

609. The appeal is accordingly dismissed.

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

GREG SINFIELD
TRIBUNAL JUDGE

HARRIET MORGAN
TRIBUNAL JUDGE

RELEASE DATE: 12 JUNE 2017

APPENDIX

REFERENCE LIST – NAMES AND ABBREVIATIONS

Name	Description
A&L	Alliance & Leicester plc, the parent of ALIL
ALIL	Alliance & Leicester Investments Limited, a subsidiary of A&L
Bayfield, Stuart	A member of OF
Berg, Eric	A member of the BNP Lux tax team
BNP	BNP Paribas SA, parent company of the BNP Group
BNP Group	BNP Paribas Group which provides banking and financial services in various countries
BNP Lux	BNP Luxembourg SA, a subsidiary of BNP
BNP UK	BNP PUK Holding Limited, a subsidiary of BNP
Delafontaine, Christophe	Global Head of OF and Chair of the TAC based in Paris
Demon, François	Head of GF
GF	Gestion Financiere, a division of BNP Group's finance department
HIL	Harewood Investments No. 5 Limited
HMRC	The Respondents, the Commissioners for Her Majesty's Revenue and Customs
London branch	The London branch of BNP
Majchrzak Gilot, Stephanie	Head of the BNP Lux structured transactions team
OF	Optimisation Finance, a team in the London branch which put together the transaction

Peters, James	A member of OF
Pouliguen, Patrice	Group Head of tax of the BNP Group
Read, Oliver	A member of OF
Robinson, Neil	Head of OF in the UK
Scholes, Peter	Head of UK tax
Stanton, Marcus	A banking consultant and expert witness for HMRC
Trifiletti, Robert	A member of BNP's UK accounting team
TAC	Transactions Approval Committee
TCC	Tax Coordination Committee of the BNP Group
Williams, Nick	A member of OF