**Appeal number: TC/2015/3004**

***JURISDICTION – appellant not seeking to challenge amendment to tax return in this Tribunal as its grounds of challenge beyond Tribunal's jurisdiction – but appellant seeking ruling on whether receipt income or capital - whether Tribunal has jurisdiction – no – appeal struck out***

***CORPORATION TAX – whether damages paid for solicitor's negligence in settling a claim based on* Sempra *taxable as income – whether payment of ACT in breach of Treaty right created a relevant non-lending relationship – yes – whether in alternative taxable under s 979 CTA 9 as other income – yes – appeal would be dismissed if not struck out***

**FIRST-TIER TRIBUNAL**
**TAX CHAMBER**

**AMALGAMATED METAL CORPORATON PLC** **Appellant**

**- and -**

**THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS** **Respondents**

**TRIBUNAL: JUDGE BARBARA MOSEDALE**

**Sitting in public at the Royal Courts of Justice, the Strand, London on 26-28 June 2017 with further representations from the appellant on 11 August and HMRC on 25 August 2017.**

**Mr F Fitzpatrick QC for the Appellant**

**Mr R Baldry QC and Ms E Wilson, Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents**

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DECISION

1. I shall refer to the appellant company, as it was referred to in the hearing, as 'AMC'. On 8 April 2011, AMC was awarded damages of £7,655,473.13 by a judgment of the High Court against its former solicitors ('Wragge'). While receipt of the damages was recorded in its accounts, it did not declare receipt of this sum in its tax return. HMRC opened an enquiry and then on 24 April 2013 amended AMC's return to increase its trading income by the amount of the damages, and consequently to significantly increase its tax liability.

2. On 2 May 2013, the appellant appealed the amendment to HMRC; on 16 April 2015 it appealed the amendment to this Tribunal.

## JURISDICTION

3. Rather bizarrely for a tax appeal, AMC's position given in its counsel's skeleton argument was that AMC agreed that the sum paid by Wragge was subject to corporation tax and that 'the assessment made by HMRC should be upheld', a statement I cannot ever recall reading in a skeleton argument submitted by an appellant before.

4. It was established at the outset of the hearing that the appellant does not really think that the amendment is correct; its position is that the Tribunal's limited jurisdiction means that this Tribunal must uphold the amendment, even though the appellant does not think the amendment was correct in law. Even so, that scarcely explains why the appellant has brought the case to the Tribunal as even it considers that I must dismiss their appeal.

5. Just how this somewhat unusual position arose was explained to me as follows. There is a real dispute between the parties as to whether the appellant is entitled to the benefit of ESC D33 on the payment by Wragge. The potential relevance of ESC D33 is clear on the face of it:

> **Zim Properties Ltd—compensation and damages**
>
> **1 Introduction**
>
> A person who receives a capital sum derived from an asset is treated for the purposes of capital gains tax as disposing of that asset. The case of Zim Properties Ltd v Proctor 58 TC 371 has established that the right to take court action for compensation or damages is an asset for capital gains tax purposes. It follows that a person who receives compensation or damages, whether by court order or arbitration or by negotiated settlement as a result of a cause of action may be regarded as disposing of the right of action. A capital gain may accrue as a result.
>
> ...
>
> **8 Relief by concession**

> Where a gain arises on the disposal of a right of action, the case may alternatively, by concession, be treated in accordance with the following paragraphs of this statement.
>
> ....
>
> **11 No underlying asset**
>
> A right of action may be acquired by a claimant in connection with some matter which does not involve a form of property which is an asset for capital gains tax purposes. This may be the case where professional advisers are said to have given misleading advice in a tax or other financial matter, or to have failed to claim a tax relief within proper time. Actions may be brought in relation to private or domestic matters. Where the action does not concern loss of or damage to or loss in connection with a form of property which is an asset for capital gains tax purposes, the approach in paragraph 9 above of treating the compensation as deriving from the asset itself is not appropriate. In these circumstances any gain accruing on the disposal of the right of action will be exempt from capital gains tax up to a limit of £500,000 for any compensation awarded in a single set of legal proceedings.
>
> Any awards of compensation above this threshold will need to be reviewed on a case-by-case basis to ensure that they remain within the Commissioners' collection and management powers. Therefore, such claims will need to be notified to HM Revenue and Customs in writing.

It is the appellant's position that the payment by Wragge is in the nature of a capital sum, and therefore, presumably bar the query over the size of the payment, I assume its position is that it is entitled to the benefit of the concession which allows persons receiving damages from their solicitors for matters where there was no underlying asset to treat the receipt as exempt for capital gains tax purposes.

*The dispute is over the applicability of an ESC*

6. The parties were agreed that I have no jurisdiction over the applicability or otherwise of this concession. I agree with them: this Tribunal is constrained by the Court of Appeal decision in *BT Pension Trustees* [2015] EWCA Civ 713 at [142-143]:

> [142] The statutory jurisdiction conferred upon the FtT by s.3 TCEA 2007 is in our view to be read as exclusive and the closure notice appeals under Schedule 1A TMA do not extend to what are essentially parallel common law challenges to the fairness of the treatment afforded to the taxpayer. The extra-statutory concession is, by definition, a statement as to how HMRC will operate in the circumstances there specified and its failure to do so denies the legitimate expectation of taxpayers who had been led to expect that they would be treated in accordance with it. We are not concerned as in these statutory appeals with the direct application of the taxing instrument modified, or otherwise, by any relevant principles of EU

> law. The sole issue in relation to ESC B41 is whether it was fairly operated in accordance with its terms.
>
> [143] We therefore consider that the reasoning of Sales J in *Oxfam v HMRC* has no application to the statutory jurisdiction under s.3 TCEA 2007 in the sense of giving to the FtT and the Upper Tribunal jurisdiction to decide the common law question of whether HMRC has properly operated the extra-statutory concession. The appeals are concerned with whether the Trustees are entitled under s.231 to claim the benefit of the credits on FIDs and foreign dividends. Not with what is their entitlement under ESC B41. This reading of TCEA 2007 is strengthened by s.15 TCEA 2007 which gives the Upper Tribunal jurisdiction to decide applications for judicial review when transferred from the Administrative Court. It indicates that when one of the tax tribunals was intended to be able to determine public law claims Parliament made that expressly clear. There are no similar provisions in the case of the FtT.

7. The Tribunal is quite clearly bound by the Court of Appeal's conclusion that it cannot, at least where there are no applicable EU law principles, consider whether a taxpayer is entitled to the benefit of an extra statutory concession. This is a direct tax appeal and there do not appear to be any applicable EU law principles that might make ESC D33 justiciable in this Tribunal. The conclusion must be that this Tribunal has no jurisdiction to consider the appellant's appeal made on the basis that ESC D33 relieves it from tax liability on the damages paid to it by Wragge.

8. Why, then, did the appellant bring its appeal in this Tribunal and not the administrative division of the High Court, which seems to me must be the proper forum for a claim that HMRC has breached AMC's legitimate expectations by failing to apply ESC D33 to the payment received from Wragge? And why have HMRC not objected to the appeal on the grounds I have no jurisdiction to hear it?

9. The parties accept that they cannot confer jurisdiction on this Tribunal simply by agreeing between themselves that it does have jurisdiction. Their position is that the Tribunal, while it has no jurisdiction to rule on the applicability or otherwise of D33, does have jurisdiction to determine whether the payment by Wragge was of an income or capital nature. This is in dispute between the parties because it is a condition precedent for the application of ESC D33 that the payment be of a capital nature: see above, where ESC D33 is limited to 'a person who receives a capital sum derived from.....' in the first line of the introduction to it.

10. In the hearing, I expressed doubt whether this was within my jurisdiction as the parties are agreed that, so far as this Tribunal is concerned, the amendment to AMC's tax return was correct whether or not the payment was of an income or capital nature. Whether the sum was of an income or capital nature only affects AMC's tax liability because, if it was of capital nature, ESC D33 might become applicable. My first impression was that the Tribunal would be trespassing on the jurisdiction of the administrative division of the High Court if it were to decide the question of whether the payment was of income or capital nature, as that was something the administrative

division would have to decide if AMC judicially reviewed HMRC's refusal to apply ESC D33.

*A right to appeal free-standing decisions?*

11. The parties did not agree that this Tribunal lacked jurisdiction and relied on the case of *Murdoch v Amesbury* [2016] UKUT 3 (TCC) as authority that it did. That was a case about whether the Upper Tribunal had jurisdiction to hear an appeal from an FTT decision in certain, somewhat unusual, circumstances; I understood that AMC and HMRC considered that the same rationale would apply when considering whether the FTT had jurisdiction to hear an appeal from an HMRC assessment or amendment.

12. I am unable to agree with the parties. The reason for that is perhaps best explained by considering the facts and outcome of *Murdoch v Amesbury*. In that case, the FTT had been asked to make a determination of where a boundary was located. The FTT decided it did not have jurisdiction to make that determination but went on to make it anyway. The 'successful' litigant, being the one whom the determination favoured, sought to rely on the FTT's determination of where the boundary lay in another legal context (despite the FTT having made it while recognising it had no jurisdiction to do so.) The 'unsuccessful' party appealed the determination on boundary to the Upper Tribunal, and the Upper Tribunal had to decide whether it had jurisdiction to hear the appeal, as neither litigant challenged the FTT's decision that it had not got the jurisdiction to make the determination of the boundary in the first place.

13. The Upper Tribunal decided that it did have jurisdiction to hear the appeal and did re-make the determination of where the boundary lay even though it accepted the FTT had itself had no jurisdiction to make that determination and the FTT's decision on jurisdiction was not under appeal.

*No right to appeal aspects of a decision not under appeal*

14. That (somewhat surprising) conclusion was reached by the Upper Tribunal after consideration of the Court of Appeal decisions of *Lake v Lake* [1955] P 336 and the more recent one of *Compagnie Noga 'Importation e d'Exportation SA v Australia & New Zealand Banking Group Ltd* [2002] EWCA Civ 1142 ('*Cie Noga'*) which made it clear that a party which does not wish to challenge a judicial determination of a matter cannot appeal a finding of fact that was made as part of that determination. In other words, the winning litigant can't appeal a finding of fact or of law that led to its winning the appeal, even if it does not like that finding:

> '...if the decision when properly analysed and if it were to be recorded in a formal order would be one that the would-be appellant would not be seeking to challenge or vary, then there is no jurisdiction to entertain an appeal.' (*Cie Noga* at [27])
>
> '...if...the court had gone on to make a decision in relation to the legal consequences which one party would not seek to challenge, in my view that party would not be entitled simply to appeal the findings because it

did not like the reasons for the decision in his or her favour....' (*Cie Noga* at [28])

15. In *Murdock v Amesbury*, the Upper Tribunal reasoned that that meant that findings of fact which were not a part of the operative decision could be appealed even if there was no appeal against the operative decision. As they put it in [49] of their decision, the FTT in that case could be seen as having reaching two independent decisions, one on jurisdiction and one on the question the subject of the dispute between the parties (the location of the boundary). The appellants sought to challenge the second but not first of these, and the Upper Tribunal permitted that (even though the first decision really made the second decision an apparent nullity).

16. The conclusion may seem very surprising as it perpetuates the situation of a court making a determination on a matter on which it has no jurisdiction. Be that as it may, it is binding in this Tribunal if it is not inconsistent with the higher authorities of *Lake v Lake* and *Cie Noga*. And that depends on whether it was correctly distinguished from them.

17. My conclusion is that it is not inconsistent with them. What the Upper Tribunal concluded was that the appealed decision (on boundary) was made by the FTT considering evidence and law which was entirely irrelevant to and independent of the unappealed decision (on jurisdiction). In *Lake v Lake*, however, the would-be appellant wanted to appeal a finding of fact on which the unappealed decision of the lower decision-making body depended: the higher court could not reconsider that finding of fact without potentially calling into question the decision that was not being appealed, and over which therefore it had no jurisdiction.

18. Another way of putting this is that in *Lake v Lake* the appellant wanted to attack the very foundations (the findings of fact) of the determination, but without calling into question the determination. The foundations of a building cannot be attacked without risking its stability: so if the Court did not have jurisdiction to re-consider the determination because it was not under appeal, it did not have jurisdiction to consider the foundations (the findings of fact or law) that went to make that determination.

19. In *Murdock v Amesbury*, there were two separate determinations, and only the findings of law and fact that went into the second of those determinations were challenged, and the Upper Tribunal's decision on that had no impact on the first determination which was quite independent. So *Murdock v Amesbury* was not inconsistent with *Lake v Lake*: I must take it that it was correctly decided although, if I was facing the same question, but without the benefit of the Upper Tribunal's decision in that case, I would have been of the opinion that the Upper Tribunal in that case had no more jurisdiction to consider the question of the location of the boundary than the FTT had.

20. However, proceeding on the assumption that *Amesbury v Murdoch* was correctly decided, the case before me seems to fall squarely on the *Lake v Lake/Cie Noga* side of the line. The appellant seeks to challenge HMRC's decision to amend its tax return: that decision was made on the basis that ESC D33 did not apply, and that decision rested, at least in part, on HMRC's decision that the receipt was of an

income nature. The question of income/capital is inextricably linked to the decision on D33. A decision by me on whether the receipt was income/capital would either affirm or call into question HMRC's decision to amend the tax return (and its refusal to apply D33). Indeed, that is why the parties invite me to make it. But I have no jurisdiction to consider the applicability of ESC D33. So, like the Court of Appeal in *Lake v Lake*, as I have no jurisdiction on the main determination (in this case, the amendment to the tax return on the basis that D33 was inapplicable), I have no jurisdiction to consider a finding which led to that determination (that the receipt was of income nature).

21. The appellant says that all it wants me to do is explain *why* I must dismiss its appeal: do I dismiss it because the payment from Wragge was in the nature of income, or do I dismiss it because, although a capital sum, I have no jurisdiction over the application of a concession? But that demonstrates the very interdependent nature of the issues: one feeds directly into the other and on the authority of *Lake v Lake* and *Cie Noga* I do not have jurisdiction to decide whether the payment was income or capital because I do not have jurisdiction to decide that the amendment was wrong for failure to apply an ESC.

*Conclusion*

22. The appellant has lodged the appeal with this Tribunal despite accepting that it is putting forward no grounds of appeal on which this Tribunal could allow the appeal. It seems to me that that means there is no dispute over which the Tribunal has jurisdiction and that under Rule 8(2)(a) of this Tribunal's Rules I must (and do) strike out the appeal for lack of jurisdiction.

23. However, like the FTT in *Murdoch v Amesbury*, my decision on jurisdiction is as much subject to appeal as any other decision I reach. So, in case I am wrong on the question of jurisdiction, and because the parties have expended a great deal of time and money in bringing the case before the FTT, it seems that I must make a ruling on the question of income/capital even though I consider I do not have jurisdiction to do so. And that is because, if the Upper Tribunal decides I am wrong to refuse jurisdiction, it will save the cost to the parties and the tribunal of having to remit the case. Indeed, in the hearing I said to the parties that I would do so, even if I concluded that I had no jurisdiction.

24. Nevertheless, I am somewhat reluctant to do so as I feel it is trespassing on what is properly within the jurisdiction of the administrative division of the High Court. However, it seems unlikely that any finding I make would bind either party in any other proceedings: in *PML Accounting* [2017] EWHC 733 (Admin), the Judge decided that, as the FTT in that case had not had jurisdiction to make the determination which it made, its decision did not bind the parties even though it was not appealed.

25. And that, it seems to me, provides the simple answer to the dilemma in *Murdoch v Amesbury:* the FTT had no jurisdiction to make the determination on boundary and therefore its decision on boundary was a legal nullity that should not

needed to have been appealed. While I have explained why I consider myself bound to reach a conclusion on the dispute over whether the damages were of income or a capital nature, I consider for the reasons given above, my decision below is made without jurisdiction and is a legal nullity.

## THE INCOME/CAPITAL DISPUTE

### The facts

*The ACT background*

26. The issue in this appeal can only be understood if set against the long-running litigation in respect of advance corporation tax, or ACT as it is generally referred to.

27. The ACT regime was introduced in 1972. It was abolished in 1999. While it was in existence, a company was required to pay each quarter corporation tax calculated as a proportion of the dividends it had paid in that quarter. As corporation tax was not otherwise due until 9 months after the end of its accounting period, this gave the tax its name *advance* corporation tax. When ordinary, or mainstream, corporation tax ('MCT') because due 9 months after the end of the company's accounting period, credit was given for the ACT already paid.

28. In normal circumstances, therefore, ACT was, as its name suggests, an advance payment of tax that would become due in any event; however, circumstances could arise under which the company's MCT liability was less than the ACT it had already paid. The ACT could not then be utilised against the MCT liability although it could be endlessly carried forward against possible future liability to MCT: ACT which had not been set against MCT was in the long-running litigation referred to as 'unutilised ACT'.

29. The law at the time the ACT regime existed permitted a company owned by another company to make, with its parent, a group income election ('GIE') the effect of which was that the subsidiary could pay dividends to its parent without payment of ACT. But the right to make a GIE applied only to companies with UK resident parents.

*Metallgesellschaft*

30. In *Metallgesellschaft Ltd* C-397 and 410/98 (2001) the CJEU ruled that the UK rules on ACT and GIEs infringed the right of establishment guaranteed by article 52 of the EC Treaty:

> [76] ...it is contrary to art 52 of the Treaty for the tax legislation of a member state, such as that in issue in the main proceedings, to afford companies resident in that member state the possibility of benefiting from a taxation regime allowing them to pay dividends to their parent company without having to pay [ACT] where their parent company is

> also resident in that member state, but to deny them that possibility where their parent company has its seat in another member state.'

It ruled that companies with non-UK parents which had been forced to pay ACT because they were unable to make a GIE were entitled to compensation, although that compensation was to be determined according to national laws.

31. A great many companies with non-UK parents then lodged claims in the High Court claiming compensation for their payments of ACT, both those which had been utilised against MCT and those which were still unutilised. The High Court made a group litigation order (the 'ACT GLO') on 26 November 2001 which litigants could join. The courts were required to decide on what basis it was proper to calculate the compensation and the appropriate limitation period for the claims.

32. It was unclear exactly how and what payments of ACT required compensation. The Revenue accepted that it was liable to pay compensation on ACT paid within 6 years of the date of claim on the basis that it was money paid by mistake as wrongfully demanded tax and/or under the principles in *Woolwich*, both of which types of claims had a 6 year time limit from date of payment. The parties were in dispute over how the compensation for these 'in time' claims should be calculated. The Revenue did not think that it should pay any compensation at all for ACT paid more than 6 years before the date of claim (these were referred to as the 'pre-limitation' claims): the appellants disputed this on the basis that, they said, payments were made under mistake of law, which had an unlimited period of claim as long as the claim itself was lodged within 6 years of the discovery of the mistake.

*The test cases*

33. As the parties were unable to resolve the issues, the ACT GLO was divided into two sections, one relating to time limitation issues for the 'pre-limitation' claims and one relating to quantum issues for all types of claim, including unutilised ACT.

34. *Deutsche Morgan Grenfell Group plc* [2006] UKHL 49 ('*DMG*') was the lead case for the limitation issues. The courts were called to decide whether a claim lay for payment by mistake of law, and thus whether the Revenue was liable to pay compensation for the pre-limitation ACT. In very brief summary, the House of Lords ruled that they were.

35. *Sempra Metals Ltd* [2007] UKHL 34 was the lead case for quantum issues and it decided, in very brief summary, that the compensation should be calculated as interest on a compounded basis.

36. The overall effect of these decisions was to make what was referred to as the 'pre-limitation' claims (in other words, those for ACT paid more than 6 years before the date the claim was lodged in the High Court) very valuable because of the effect of compounding over a long period of time, particularly as rates of interest were high in the 1970s and 1980s.

*The relevance of the ACT litigation to AMC*

37. The following facts were not in dispute; largely they are a summary of the much more detailed summary of the decision of the High Court in *Amalgamated Metal Corporation PLC v Wragge & Co (a firm) and Wragge & Co LLP* [2011] EWHC 887 ('*AMC v Wragge')*, the findings of which were accepted by HMRC. There was also an agreed statement of facts.

38. AMC was a company resident in the UK which had a EU-resident parent company. Over many years, it had paid ACT to the Revenue on dividends which it had paid to its parent. AMC became aware of the ACT GLO and instructed its solicitors, Wragge & Co (later Wragge & Co LLP) to pursue claims on its behalf. Wragge duly lodged a claim in the High Court on 15 January 2002 and AMC joined the ACT GLO.

*The settlement of AMC's claims*

39. On 7 March 2002, the Inland Revenue made parties within the ACT GLO an offer to settle the quantum issue on terms of simple interest calculated at a specified rate. This offer was only made in respect of ACT paid within 6 years of the date of claim; in other words, it did not relate to the 'pre-limitation' ACT claims.

40. On 21 February 2003, the Revenue made an offer to settle the pre-limitation claims. The offer to settle was also on a simple interest basis and was stated to be conditional upon the resolution in favour of the taxpayers of the test case on the limitation issue. In that sense, it was quite different to the earlier offer in respect of in-time claims, as acceptance of that earlier offer would mean that HMRC became liable to pay the claim at the agreed rate: the 21 February 2003 was an offer to settle the pre-limitation claims at the agreed rate if and only if the test case litigation resulted in a finding that such claims were not in law out of time, in other words, that there was a valid claim for restitution on the grounds of mistake of law.

41. On 18 March 2003, the Revenue clarified both offers: the offer relating to in-time claims did not affect out-of-time claims, which would remain live even if the offer to settle the in-time claims was accepted. The offer in respect of out-of-time claims was confirmed to be conditional upon the *DMG* test case resolving the time limit issue in favour of the taxpayers. The Revenue gave only a short time frame for acceptance of the offers, but then extended the closing date to the end of 15 April 2003.

42. AMC, conscious, it seems, that whether the measure of restitution was simple or compound interest was much less significant to its in-time claims than to its pre-limitation claims, instructed Wragge to settle, and only to settle, its in-time claims on the basis of the offer made by the Revenue. Wragge, however, with ostensible authority to act on AMC's behalf, agreed on 15 April 2003 with the Revenue to settle both the in-time and pre-limitation claims on the basis of the offers made.

*The dispute with Wragge*

43. As I have said, the offer in respect of the pre-limitation claims had been conditional upon the taxpayers winning the test case on mistake of law, which they did when the House of Lords issued its decision in *DMG* in 2006. It seems it was only after that decision was released that AMC discovered that Wragge had, back in 2003, settled its pre-limitation claims as well as its in-time claims, because HMRC's liability to AMC was then determined by the terms of the settlement agreement.

44. AMC appointed new solicitors. Following release of the House of Lords' decision in 2007 in *Sempra* that the claims should be calculated on a compound interest basis, it because apparent Wragge had settled AMC's claim for pre-limitation ACT for a sum considerably lower than AMC would have been entitled to had no settlement been reached. On 20 October 2009, AMC issued a claim against Wragge for damages.

45. On 19 March 2009, HMRC had paid AMC the following amounts:

(a) £179,419 in respect of its in-time utilised ACT claims (calculated on a simple interest basis as per the terms of the 2003 settlement);

(b) £4,829,569.02 in respect of its pre-limitation ACT claims (calculated on a simple interest basis as per the terms of the 2003 settlement);

(c) £648,777.05 in repayment of unutilised ACT together with interest thereon calculated on a compound basis as per *Sempra* in the sum of £4,583,710.79.

46. AMC declared the amounts paid to it by HMRC (excluding the repaid ACT at (c)) as interest in its accounts for the year ended 31/12/09 and paid corporation tax on them.

47. Judgment in *AMC v Wragge* was delivered on 8 April 2011. Steele J found in favour of AMC; he agreed with AMC that the payment to AMC of £4,829,569.02 by HMRC in respect of its pre-limitation claims was £7,655,473.13 less than it would have been had Wragge not acted improperly. He awarded that sum as damages to AMC. The damages were duly paid to AMC.

48. AMC's accounts for the relevant year to 31 December 2011 showed the receipt from Wragge as 'other operating income.' As I said at §1, in its tax return for that period, filed on 20 December 2012, it did not declare the receipt as subject to tax. HMRC opened an enquiry and, on 24 April 2013, amended AMC's tax return to show the receipt as subject to tax. On 2 May 2013, AMC appealed the amendment to HMRC, and on 16 April 2015 it was appealed to this Tribunal.

*The witnesses*

49. As I have said, the above facts were not in dispute, but the appellant did call two witnesses.

50. Mr Victor Sher (normally known as Harold Sher) was director and chairman of AMC. He had been employed by AMC since 1973 and was Group Managing Director and Chief Executive at the time of the events in question. He gave written evidence of the background to the dispute and settlement which was not in dispute save for his comment that Steel J made a finding of negligence against Wragge. Mr Sher accepted in cross-examination that he was not purporting to make a statement about the law but was merely reflecting his understanding that Steel J had made such a finding.

51. Mr Baldry did later submit that Steel J's finding was that Wragge had exceeded its authority as agent; Mr Fitzpatrick's position was that Steel J had also found that Wragge was liable in tort for negligence to AMC. I find that (as is clear from his decision) that Steel J found for AMC on both grounds, although he dealt with the contract point (breach of authority) first and therefore technically that was the basis of his decision, with his finding of negligence being obiter. However, I do not think the basis of Steel J's decision makes any difference to the question I am called on to decide.

52. The second witness was Mr Neil Rosen who was Group Financial Controller of AMC at the time of the events in question. He explained how the receipts had been treated in AMC's accounts. The payment from Wragge was treated as 'other operating income' as Mr Rosen, an accountant, had at the time thought that was the appropriate place in the accounts in which to record the receipt. The auditors were satisfied it was correctly accounted for. The money paid by HMRC on the settlement (see §46) was treated as 'interest' in the accounts and similarly the auditors were satisfied that that was the correct treatment.

53. I accept his evidence, but it does not appear to be relevant: neither party suggested that the accounting treatment accorded to the various receipts was wrong, while at the same time neither party suggested that the accounting treatment was determinative of the tax position.

54. Having set out the relevant facts, I move on to consider the legal position.

## Outline of the legal dispute

55. The appellant is liable to corporation tax on its profits. By s 8(3) of the Taxation of Chargeable Gains Act 1992 ('TCGA') corporation tax is chargeable on capital gains on the principles of the TCGA. Those principles include s 22(1) which provides that capital sums derived from (a) compensation for damage to assets or (c) capital sums received in return for forfeiture or surrender of rights are both subject to capital gains tax, although they also include s 37(1) which provides that capital gains tax is not charged on consideration which is taken into account in computing profits or gains for the purposes of income tax.

56. Both parties appeared to accept that s 37(1) meant that if the damages paid by Wragge were ***not*** properly charged to corporation tax as income of the company, then they would be chargeable to corporation tax under either s 22(1)(a) or (c) subject to

the possible applicability of ESC D33. The dispute was whether the damages were properly chargeable to corporation tax as income of the company.

57. HMRC's position is that the damages were subject to tax as income because:

> (1) under the loan relationship rules, the damages were either or both (a) interest payable to AMC under s 481(3)(a) Corporation Tax Act 2009 ('CTA 2009') or (b) profits arising to AMC from a related transaction in respect of the right to receive interest under s 481(3)(c) of the same Act; or
>
> (ii) they were miscellaneous income not otherwise chargeable to tax and therefore taxable under s 979 CTA 2009.

58. HMRC appeared to accept that if the damagers were not subject to tax under any of these provisions, then they only fell into the net of corporation tax under s 22 TCGA, and if that provision applied, then ESC D33 also potentially applied. As I have said, all parties accepted that I could not make a ruling on whether ESC D33 was applicable and I agree.

59. The appellant does not accept that either s 481 or 979 CTA 2009 applied to the damages: its position is that it was a capital sum which can only fall into the net of taxation because of s 22 TCGA and therefore its case is ESC D33 is applicable.

60. I am only asked by the parties to determine whether the damages are taxable under s 481 or 979 CTA 2009 or neither. I have already said that I will make that determination although I do not think that I have jurisdiction to do so, and therefore any decision I make on this will not be binding even if not appealed.

61. It was common ground between parties, and I agree as was plain on the face of s 979, that the loan relationship rules in s 481 took priority over s 979, so I first consider whether the damages were taxable under the loan relationship provisions.

## (A) The loan relationship rules

### Whether the payment of ACT created a relevant non-lending relationship

62. The loan relationship rules in s 302(1) of Chapter 5 of the Corporation Tax Act 2009 provide that a company has a loan relationship in the following circumstances:

> **302 'loan relationship', 'creditor relationship', 'debtor relationship'**
>
> (1) For the purposes of the Corporation Tax Acts a company has a loan relationship if –
>
> (a) the company stands in the position of a creditor or debtor as respects any money debt (whether by reference to a security or otherwise), and
>
> (b) the debt arises from a transaction for the lending of money.

63. It was not suggested that there was a loan relationship in respect of the ACT between AMC and the Revenue, or AMC and Wragge. Clearly the payment of ACT by AMC to the Revenue was not made because AMC had agreed to lend the money to the Revenue; the payment was made because all parties at the time believed that AMC was paying it under a legal obligation to pay it as tax. And clearly there was no loan relationship between AMC and Wragge: AMC did not pay any money to Wragge, and the money paid by Wragge to AMC was damages under a court order: Wragge's debt to AMC did not arise from a transaction for the lending of money but out of a breach of the legal services contract between Wragge and AMC and/or the tort of negligence.

64. But that does not make the loan relationship provisions irrelevant, as Part 6 of the CTA 2009, and in particular s 481, deems certain other relationships to be loan relationships. So the question is whether there was a deemed loan relationship between the parties. S 481 provides:

> **481 Application of part 5 to relevant non-lending relationships**
>
> (1) If a company has a relevant non-lending relationship –
>
> (a) Part 5 (loan relationships) applies in relation to the relevant matters (see subsection (3) and (5)) as it applies in relation to such matters arising under or in relation to a loan relationship, but
>
> (b) the only credits or debits to be brought into account for the purposes of this Part in respect of the relationship are those relating to those matters.
>
> (2) Accordingly, subject to subsection (1)(b), references in the Corporation Tax Acts to a loan relationship include a reference to a relevant non-lending relationship.

65. Whether this deeming provision applies in the context of this appeal therefore depends on two questions:

> (a) the relationship being a 'relevant non-lending relationship'; and
>
> (b) the payment sought to be taxed being (or relating to) a 'relevant matter'.

66. Section 479(1) contained the definition of relevant non-lending relationship, which was follows:

> **479 Relevant non-lending relationships not involving discounts**
>
> (1)A company has a relevant non-lending relationship if –
>
> (a) the company stands, or has stood, in the position of a creditor or debtor in relation to a money debt,
>
> (b) the money debt did not arise from a transaction for the lending of money (and so, because of section 3021)(b), there is no loan relationship), and
>
> (c) the money debt is one of the kinds mentioned in subsection (2).

67. These conditions are clearly cumulative. The parties were agreed, as I am, that s 479(1)(b) is fulfilled. As I have said at §63, there was no lending of money between AMC and HMRC or between AMC and Wragge, so condition (1)(b) was clearly met. So the question is whether conditions 479(1)(a) and (c) were also met.

**Was there a money debt?**

68. Condition s 479(1)(a) required AMC to stand in the position of a creditor (or debtor) in relation to a money debt. So this condition depended on other definitions, such as that for 'money debt', which was contained in s 303(1), as follows:

> **303 'money debt'**
>
> (1) For the purposes of this Part a money debt is a debt which –
>
> (a) falls to be settled -
>
> (i) by the payment of money,
>
> (ii) by the transfer of a right to settlement under a debt which is itself a money debt, or
>
> (iii) by the issue or transfer of any share in any company,
>
> (b) has at any time fallen to be so settled, or
>
> (c) may at the option of the debtor or the creditor fall to be so settled.

69. The meaning of 'money debt' in the context of different corporation tax legislation was considered in *Shop Direct Group and others* [2014] STC 1383, although I did not understand either party to suggest that it was not applicable here. Briggs LJ at [49-52] drew a distinction between a 'primary monetary obligation' and other primary obligations, the breach of which occasioned an entitlement to damages assessed by the court. The former was a liability to debt, the latter to damages. A primary monetary obligation was a money debt, even if the amount of money owed was difficult to ascertain, and even if the source of the obligation to pay the money was a statutory right to compensation. He said at [52] that:

> '...to stand as a creditor in relation to a money debt, a person must have some form of entitlement to it. That entitlement may be proprietary, ie an entitlement in rem, restitutionary or statutory ...But it may also be contractual.....'

70. HMRC relied on this. Their position was that, while neither AMC nor the Revenue appreciated it at the time, nevertheless when AMC paid the various amounts of ACT which were later to be the basis of the pre-limitation claims, it was paying sums to the Revenue which were not due to the Revenue. They were not due to the Revenue because the UK law which required the ACT to be paid was unlawful, as was later declared by the CJEU in the case of *Metallgesellschaft* (above). The money was, as found by the House of Lords, to be paid under mistake of law and therefore, says HMRC, from the moment the ACT was paid to the Revenue by AMC, the Revenue owed AMC under the law of restitution a money debt equivalent to the overpaid ACT.

71. The ACT was, of course, later set off against MCT and had long ceased to be outstanding. But that made no difference to HMRC's case. For the period that the ACT was paid, but before an equivalent amount of MCT fell due, AMC had paid money to the Revenue which (although it did not know it at the time) was not, says HMRC, money due to the Revenue. AMC during that period was, therefore, says HMRC, a creditor in relation to a money debt owed to it by the Revenue (and satisfied when the Revenue allowed the MCT to be off-set against it). This would be a money debt within s 303(1)(b), as a money debt which 'has at any time fallen to be so settled'.

72. Of course, applying the principles of *Shop Direct*, it was only the relationship as between AMC and the Revenue which could constitute a money debt: the primary obligation between Wragge and AMC had been contractual and for breach of which and/or for tort AMC was owed damages. Even though the damages may have been easy to assess in the sense they were equivalent to what HMRC describe as the money debt between the Revenue and AMC, there was no money debt between AMC and Wragge (at least up to the point that the damages were awarded). But for these purposes that is irrelevant: the question is whether there was a money debt between AMC and the Revenue immediately after AMC paid the ACT to the Revenue.

*Was the ACT due?*

73. The appellant does not consider that there was a money debt. Without disputing the correctness of Briggs LJ's analysis of the meaning of money debt, its point is more fundamental: it says that the ACT *was* legally due and payable to HMRC. Its case is that the ACT was lawfully due and payable because AMC had not made a GIE: the illegality in UK law was the inability of companies with EU parents to make a GIE. The illegality was not the requirement to pay ACT in the absence of a GIE. As the appellant put it, its mistake was not in paying the ACT, but in not realising that it had the right to make a GIE which, if exercised, would have obviated the need to pay ACT. So, reasons the appellant, no money debt was owed by the Revenue to the appellant during the period between the payment of the ACT and its set-off against the MCT.

74. The cases (*Metallgesellshaft, DMG* and *Sempra)* clearly proceeded on the basis that an amount equal to the ACT was owed by the Revenue to the taxpayers who had been unable to make GIEs: the appellant's explanation is that the Revenue's failure to respect the appellant's right of freedom of establishment rendered the Revenue liable in damages to the appellant, those damages being exactly equivalent to the amount of the ACT. In other words, the principle amount due to AMC was not the ACT but an amount equivalent to its loss from its inability to make a GIE, which was of course an amount equivalent to the ACT. Applying *Shop Direct,* on the appellant's case, there was no money debt between AMC and the Revenue: the principle amount owing was damages.

*(a) Metallgesellshaft*

75. The appellant relies, for its case that the Revenue owed AMC damages and not a money debt, on the reasoning of the CJEU in *Metallgesellschaft,* the House of Lords

in *DMG* and the Court of Appeal in *FII Test Claimants.* Both parties went through each judgment picking out sections favourable to their case. But I think it is important, before placing too much reliance on the exact phrases used, to remember that none of the judgments were concerned with the question of whether, while it was unutilised, the ACT was a money debt.

76. Nevertheless, the issue of whether the ACT was owed by the Revenue to AMC was, at least indirectly, before the CJEU because the UK government's case was that, as the principle sum (the ACT) had been repaid (by way of set-off against MCT), the taxpayer's claim was for ancillary relief (interest on that principle sum), which was, under EU doctrine, a matter for the national courts; and under UK law no interest was payable as the principle sum had been repaid before the claim had been issued (applying the doctrine in *La Pintada* [1985] AC 104). Therefore, ran the UK government's case, Metallgesellshaft was owed nothing despite any breach by the UK of the taxpayer's right to freedom of establishment.

77. It should not have been surprising that the CJEU did not agree that there was no remedy for the breach of the EU Treaty. In paragraphs [82-87] the court said the levying of tax in breach of community law resulted in a liability on the national government to repay those charges: but in that case, the illegality was not in levying of the tax but levying it early. , it was only by paying interest on that sum that the UK could remedy its breach of the Treaty:

> '[87]...the claim for payment of interest covering the cost of loss of the use of the sums paid by way of [ACT] is not ancillary, but is the very objective sought by the claimants' actions....In such circumstances, where the breach of Community law arises, not from the payment of the tax itself but from its being levied prematurely, the award of interest represents 'reimbursement' of that which was improperly paid and would appear to be essential in restoring the equal treatment guaranteed by ...the Treaty.'

Further, national law could not in such a situation prevent a payment of interest, and therefore render practically impossible the exercise of the rights conferred by EU law:

> '[96].....the Treaty requires that resident subsidiaries and their non-resident parent companies should have an effective legal remedy in order to obtain reimbursement or reparation of the financial loss which they have sustained and from which the authorities of the member state concerned have benefited as a result of the advance payment of tax by the subsidiaries. The mere fact that the sole object of such an action is the payment of interest equivalent to the financial loss suffered as a result of the loss of use of the sums paid prematurely does not constitute a ground for dismissing such an action. While, in the absence of Community rules, it is for the domestic legal system of the member state concerned to lay down detailed procedural rules governing such actions, including ancillary questions such as the payment of interest, those rules must not render practically impossible or excessively difficult the exercise of rights conferred by Community law.'

78. The appellant read this as meaning that the interest award was the principle sum and therefore the underlying ACT was not a principle sum owing: HMRC read it as confirming that during the period ACT was paid but before it was offset, it had been unlawful to levy it: it was a money debt.

79. As a matter of principle, it is difficult to see in logic why the repayment of a debt before the action commenced would make the nature of the right to be paid interest on that sum any different or better than the right to be paid interest on the sum if it had not been repaid: that would appear to put creditors in the fortunate position of having been repaid in a doubly better position than those who have not yet been repaid.

80. And while it is true that the CJEU talked of the claim in *Metallgesellschaft* as not being ancillary, I do not think they were intending to state that the right to interest was not parasitic upon the right to be repaid the tax unlawfully levied. The tenor of what they said was that the premature levying of the ACT was unlawful: the payment of the ACT was unlawfully demanded up to the point that the MCT became due. The right to interest was parasitic on that premature ACT. All the CJEU was saying was that while, ordinarily, parasitic claims to interest were within the national remit, such national rules had to be overridden where (as in the *Metallgesellshaft* case) their effect otherwise would be to deny the claimant a remedy for breach of its rights to freedom of establishment.

81. *Metallgesellschaft* did not include a claim for unutilised ACT but one can speculate that if it had, the CJEU would have left any award of interest to the national court, as in that case national rules did not prevent an award of interest.

82. In conclusion, there is nothing in *Metallgesellshaft* to suggest that the award was damages rather than interest on the ACT that had been levied too early in breach of the Treaty. I do not think *Metallgesellschaft* offers the appellant any basis for saying that the ACT was lawfully demanded and lawfully paid by AMC. On the contrary, the CJEU seemed quite clear that the payment of ACT was unlawful:

> [83] It is important to bear in mind ...that what is contrary to Community law...is not the levying of a tax in the UK on the payment of dividends by a subsidiary to its parent company but the fact that subsidiaries, resident in the UK, of parent companies having their seat in another member state were required to pay that tax in advance whereas resident subsidiaries of resident parent companies were able to avoid that requirement.

And at

> [87] ...the breach of Community law arises, not from the payment of the tax itself but from its being levied prematurely.....

83. So I reject the appellant's case on *Metallgesellschaft* and move on to consider whether *DMG* or *FTT Test Claimants* are authority for the appellant's proposition that the ACT was lawfully due and therefore unable to comprise a money debt owing to AMC.

*(b) DMG*

84. The appellant also relied on what was said in *DMG*, particularly what Park J said at first instance ([2003] STC 117):

> [22]...the mistake of law which DMG made was not that it paid ACT which was not payable: the ACT was as a matter of law payable when DMG paid it, and the decision of the CJEU in *Metallgesellschaft/Hoechst* does not mean that it was not payable. Rather the mistake of law which DMG made was that it did not realise that it and DBI could have made group income elections with DBAG, which would have had the effect of preventing the ACT from being payable.

85. What Park J said clearly supports the appellant's position. The difficulty for the appellant is that Park J was appealed. The Court of Appeal reversed Park J: it in turn was reversed by the House of Lords. So the question is what the House of Lords ruled and whether the Lords agreed with Park J on this point.

86. Lord Scott, while delivering a dissenting judgment, did agree with Park J on this point. At [88] he clearly saw DMG as having a right to damages rather than a right to repayment. He said the ACT was due to the Revenue, albeit had DMG not paid it, any claim for payment against DMG may have been defendable on basis of a cross-claim for breach of EU law.

87. The appellant considered that Lord Hope also agreed with Park J. He said:

> "[62]...Park J's analysis was the correct way of looking at what happened in this case. It was the mistaken belief that group relief could not be claimed that led inevitably to the liability to pay ACT which, absent a valid claim to group relief, DMG was not in a position to dispute....But, as Park J was right to recognise, if the mistake about the availability of group income relief had not existed, the ACT would not have been paid. It follows that the payments were made under a mistake."

HMRC considered what Lord Hope said ambiguous on the question of whether the ACT was unlawfully paid: it was not, after all, significant to the point at issue in that case, which was whether the ACT was paid under a mistake of law. However, while I agree that he made no clear statement that the ACT was lawfully due, nevertheless Lord Hope clearly agreed with Park J, who did say that.

88. The appellant's case was that a majority of the Lords' supported its position because Lord Walker also considered that the ACT was lawfully due. But with that I cannot agree. Lord Walker said:

> [135] ...The appropriate remedy for DMG is, as the Revenue concedes, restitutionary in nature. It is not for the repayment of a principle sum unlawfully exacted from the taxpayer, but for its unlawful exaction before it became due.....

and

> [143] ...I agree with the judge's conclusions, and I largely agree with his reasoning, though I respectfully think that he was rather over-analytical in his approach....DMG paid the ACT because it mistakenly thought that it had to. The fact that there was a procedural requirement for a GIE does not alter the substance of its mistake, since (as Park J expressly found ...at [11]) any attempt at making a GIE would undoubtedly have been rejected in this case.

So, while he agreed the payment was one of mistake of law, he considered that the ACT had been unlawfully exacted.

89. Lord Hoffman clearly did not agree with Park J on this point. He said:

> [20]...The effect of the decision in *Metallgesellschaft* ...was that the Inland Revenue had not been entitled to the money. Nor could the Revenue have thought that DMG was intending to make an interest-free loan to the British government or that there was any other proper ground on which they had been entitled to retain it.....
>
> [32]...Park J took a rather sophisticated view of the nature of the mistake. He said that the mistake was not about whether ACT was payable. DMG had not made an election and therefore it was payable. The mistake was about whether DMG should have been allowed to elect. But I agree with the Court of Appeal that the mistake was about whether DMG was liable for ACT. The election provisions were purely machinery, which DMG would undoubtedly have used, by which it could enforce its right to exemption from liability.

Earlier he had stated:

> [5]...[The CJEU] held that the companies which had been unlawfully required to pay ACT were entitled to restitution or compensation....

and

> [8] The first question...is whether DMG has a cause of action which can be described as being 'for the relief from the consequences of a mistake' ....It claims that it seeks relief against having paid money to the Inland Revenue in the mistaken belief that, since s 247 ICTA 1988 made no provision for a group election by a company with a German parent, it was obliged to pay ACT. In fact, art 43 EC made this denial of a right of election unlawful and, in consequence since DMG would have exercised its election, it was not obliged to pay ACT.

90. Lord Brown dissented on one point (the date at which the mistake was discovered) which did not affect outcome of appeal. At [161] he agreed 'with almost all' of the speeches of Lord Walker, Lord Hoffman and Lord Hope, and nothing he said in his entire judgment indicates which judge he thought was right on the issue of whether the ACT was lawfully due, which (since he agreed with judges who expressed opposing views on this point) was clearly not an issue he was concerned with in giving his judgment. Indeed, his entire speech was concerned with the question (irrelevant in this appeal) of the date at which the mistake was discovered.

91. In conclusion, I accept Lord Scott and Lord Hope agreed with Park J that the ACT was lawfully due, but it is clear that Lord Hoffman and Lord Walker did not accept this. Lord Brown did not express a view. As a matter of the law of precedent, therefore, unless there is other binding authority in another case, it is something on which I must make up my own mind. And I proceed to do so.

*(c) DMG – which judgments to prefer?*

92. It is helpful to look at the whole of the judgments rather than pick out individual paragraphs. Lord Scott's view was that the mistake was over the GIEs which meant that the ACT was lawfully due (see above citation): there was therefore no unjust enrichment of the Revenue, so no claim lay in restitution:

> [89]....The ACT was paid because there was a legal obligation under a valid statutory provision for the money to be paid. DMG's remedy was ...not a restitutionary one for repayment of money paid that was not due, or for the repayment of money paid under a mistake, but was, and is, a claim for compensation to recover the loss caused by the breach of Community law.'

In other words, his agreement with Park J that the ACT was lawfully due was fundamental to his dissent: it was his reason for concluding that there was no remedy in restitution. And this was because the right to restitution only applies where there is unjust enrichment: there is no enrichment of a recipient where the claimant has paid what he owed the recipient.

93. None of the other judges dealt expressly with the requirement to show enrichment of the defendant before there could be a claim for money paid by mistake. Lord Walker and Lord Hoffman, of course, considered that the ACT was not due when it was paid, and so the point did not really arise for them. There was clear enrichment of the Revenue on the law as they saw it.

94. Lord Brown, as I have said, dealt only with his dissent about the date on which the mistake was discovered.

95. Lord Hope's decision, however, was inconsistent with the principle that the law of restitution is founded on the principle of reversing unjust enrichment: he decided that an action for mistake of law lay despite also finding that the ACT had been lawfully due and paid to the Revenue.

96. His decision dealt with various issues such as whether a claim in restitution lay despite the defendant being a public body and despite the availability of other remedies. He found (as cited above) that the payment was made by a mistake over the availability of GIEs to subsidiaries with EU parents. But what Lord Hope did not analyse in his judgement was whether there was unjust enrichment of the Revenue. Although he refers occasionally to 'unjust enrichment' in his speech, he does not expressly deal with the conundrum that if the tax is due, how could the Revenue be said to be enriched? The failure to consider this inherent contradiction weakens the persuasiveness of his views.

97. And his conclusion, that DMG was entitled to recover the money paid by mistake, albeit it was lawfully due, seems to me to be inconsistent with his earlier decision in *Kleinwort Benson* [1998] UKHL 38. In *Kleinwort Benson,* Lord Hope described the concept of unjust enrichment as being at the heart of the law of restitution and said:

> '....The common law accepts that the payee is enriched where the sum was not due to be paid to him,...'

Lord Hope's entire speech which followed in *Kleinwort Benson* was premised on basis that the sum at issue in that case was paid when it was not legally due: it was this part of his speech that was cited and relied on in *FII Test Claimants* in the extract from that case I have cited below (see §101). But in *DMG,* Lord Hope appears to have overlooked his own analysis in *Kleinwort Benson.* If he had followed his earlier analysis, he must surely have agreed with Lord Scott's dissenting judgment. And as that would have remained a minority view, the view of the other judges in the majority should be preferred.

98. What Lord Hope said in *DMG* on this point was also inconsistent with what he later said in *Sempra*, the other ACT GLO test case:

> '[31]...Sempra paid the tax when it did in the mistaken belief that it was obliged to do so when in fact it was being levied prematurely. ....'

99. In passing I note that Park J at first instance, like Lord Hope, also concentrated on the nature of the mistake and the date the mistake was discovered but did not deal with issue of enrichment. The failure to consider this issue detracts from the persuasiveness of his decision on this issue too.

100. In conclusion, the views of 3 out of 5 law lords (Lord Walker, Hoffman and Scott) in *DMG* were, or were consistent with, the fundamental justification for restitution of monies paid by mistake that unjust enrichment should be reversed, and, further, there is no enrichment where the monies are lawfully due. The only way the decision in *DMG* can be consistent with other authorities, such as *Kleinwort Benson* on the law of restitution is if it is understood on the basis that, despite what Lord Hope said, the ACT was not lawfully due to the Revenue and the Revenue was thereby enriched by their receipt of it. For this reason, Lord Walker and Lord Hoffman's views are to be preferred to Lord Hope's (and to Lord Scott's dissenting view).

*(d) FII Test Claimants*

101. The appellant referred me to the Court of Appeal's decision in *FII Test Claimants* [2010] EWCA Civ 103 for further confirmation of Lord Hope's view on the point that the ACT was lawfully due. But the Court in *FII Test Claimants* did not consider, let alone approve, what Lord Hope said in *DMG*: they did rely on what he said *Kleinwort Benson*, to which I have already referred, that enrichment was fundamental to an action for restitution:

> [181] As to the second construct, the enrichment is said to have been the greater amount of lawful tax paid in year 2 or subsequent years

> than would have been paid but for the mistake in thinking that the Case V charge in year 1 was valid and the use of reliefs in year 1 for that reason. This cannot, in our judgment, found a claim in restitution. The short answer to the claim is that the tax paid in year 2 or subsequent years was lawfully due and so cannot be the subject of recovery under *Woolwich* or as a payment under a mistake: see *Kleinwort Benson v Lincoln City Council* [1998] UKHL 38, [1999] 2 AC 349 at 408B (Lord Hope).

102. I understand the appellant's point on *FII Test Claimants* to be that the tax relief at issue in that case should be seen as being on a par with the ability to make a GIE in *DMG*. In *FII Test Claimants*, the taxpayer paid its Year 2 tax as it had exhausted its tax relief against the unlawful tax levied in Year 1. Here AMC paid ACT as it was unlawfully denied tax relief (the GIE).

103. At first glance, this appears a valid and persuasive comparison between the two cases. But on analysis it is not. Using up a tax relief against an unlawful tax does not make unlawful the payment of other, lawfully due, tax, merely because the relief would have been utilised against that lawful tax had it been understood to be available for the purpose. Such a situation cannot be compared to the ACT GLO where tax relief was unlawfully denied to taxpayers, making the payment of the underlying tax unlawful.

104. In other words, in *DMG* the taxpayer was found to be entitled under the law of restitution to repayment of tax which was not lawfully due (because it had been unlawfully denied a tax relief); but in the *FII Test Claimants* case, the taxpayer was found not to be entitled (under the law of restitution) to repayment of tax which was lawfully due; the fact that it could have set tax relief against that lawful tax had it not already used the relief against an unlawful tax liability, did not make the lawful tax liability unlawful.

105. In short, in *DMG* the premature demand of MCT (the subject of the claim) unlawfully breached the right to freedom of establishment. In *FII Test Claimants,* however, the year 2 tax (the subject of the claim) was not levied discriminatorily or in breach of EU law. It was lawfully demanded. As was said in *FII Test Claimants* at [182] but which is not the case here:

> '...there was no mistake by the Claimants about the lawfulness of the tax paid in year 2. It was lawfully due. The mistake was in year 1 in relation to the tax due in that year and the need for the set off of reliefs to reduce it. The connection between the payment of tax lawfully due in year 2 and the mistake in year 1 is not sufficiently direct to satisfy the requirements of causation in restitution. The loss is too remote.'

106. Properly understood, the *FII Test Claimants* actually supports HMRC's position as the case reiterates that there are two parts to a claim of money paid by mistake: the appellant must show that there was an operative mistake and that the defendant was unjustly enriched. Enrichment means that the payment the subject of the claim must not have been due in law. As the above citations show, the Court of Appeal in *FII Test Claimants* was quite clear that if the payment was due in law, there was no

enrichment, and no claim in restitution. Therefore, because the Lords in *DMG* found that there was a claim in restitution, it follows, by a process of reverse engineering, that the ACT cannot have been lawfully due.

*(e) British American Tobacco*

107. For further confirmation of their position, HMRC referred me to the franked investment income litigation which, they said, had always treated the ACT as unlawfully demanded. As an example, I was referred to the recent case of *British American Tobacco* in the FTT, where the hearing had taken place but judgement was reserved at the time of the hearing before me. The judgment in *BAT* was delivered on 12 July 2017 after the close of the hearing and is reported at [2017] UKFTT 558. It appears it was assumed by all parties and the judge in that case that the ACT at issue was unlawfully charged.

108. I do not think that much can be read into this: the making of an assumption does not make that assumption correct in law. Nevertheless, as after the close of the hearing in this appeal, HMRC drew my attention to the decision in *BAT*, I gave the appellant leave to comment on it (with the right for HMRC to respond). The appellant's point in response was that *BAT* concerned franked investment income, and an unlawful denial of a relief was no part of the scenario in that appeal. So nothing, in the appellant's view, could be read into the assumption in the *BAT* appeal that the ACT was unlawfully due. The case was entirely distinguishable.

109. HMRC in their response to that did not agree. They considered that the ACT was unlawfully due under either the scenario in either line of cases. The appellant may have wanted to respond to this but I have not given them the opportunity to do so as I do not think that the answer to whether the ACT was unlawfully levied from AMC lies in the *BAT* case. I accept the appellant's point that the cases are distinguishable: the answer to the question of whether the ACT was unlawfully due in this appeal lies in *Metallgesellshaft* and *DMG* and I set out my conclusions on that below.

*Conclusion on money debt*

110. I do not accept the appellant's case that the ACT was lawfully paid and therefore could not constitute a debt. As I have explained, the Lords' decision in *Kleinwort Benson* was that there could only be a restitutionary remedy where the sum was not due: it follows that because DMG (and AMC in its turn) were given a restitutionary remedy, that the ACT was not due to the Revenue.

111. Park J's decision that the ACT was due to the Revenue is not binding on me (as it was appealed) and is not persuasive as it contradicts the basis of the law of restitution and is inconsistent with what Lord Walker and Lord Hoffman said on appeal.

112. Lord Scott's contrary view is not persuasive because it was the reason for his dissenting decision that there was no remedy in restitution, whereas I am bound by the

majority (Brown, Walker, Hoffman and Hope) who decided in favour of DMG that there was a restitutionary remedy. Lord Hope's view is also not persuasive, even though he was a part of the majority, because it also contradicts the basis of the law of restitution and what he said in *Kleinwort Benson* which requires the recipient to be enriched before the claimant is entitled to restitution; he also appears to have changed his mind by the time of *Sempra*.

113. The view of Lord Walker and Lord Hoffman that the ACT was not due is persuasive as that view is consistent with what the House of Lords said in *Kleinwort Benson* was the basis of the law of restitution and therefore consistent with their decision that DMG had a remedy in restitution.

114. *Shop Direct* indicates that a restitutionary claim will give rise to a money debt. That makes sense: a restitutionary claim is not for damages to be assessed by the court but for the repayment of a sum of money. Restitution means restitution: a sum of money has been paid which the law of restitution requires to be paid back.

115. Therefore, I find as a matter of law for the period before the ACT was offset against the MCT, there was a money debt owing from the Revenue to AMC. It follows from that finding that AMC stood in the position of a creditor in relation to a money debt, because the ACT paid by AMC was owed to AMC by the Revenue.

**Was it 'a debt on which interest is payable to...the company'?**

116. Reverting to the legislation which I set out at §66 above, there were 3 conditions in s 479(1) which had to be met in order for a relationship to be a relevant non-lending relationship. As I have said at §67, the parties were agreed that the middle condition (s 479(1)(b)) was met; I have now found that the first condition, s 479(1)(a)) was met as AMC had stood in the position of a creditor in relation to the ACT, which was a money debt. So I move on to consider the third condition in s 479(1)(c). That condition depended on whether the debt was one of the kinds mentioned in s 479(2), and that section provided as follows:

> (2) The kinds of debt are-
>
> (a) a debt on which interest is payable to or by the company,
>
> (b) a debt in relation to which exchange gains or losses arise to the company,
>
> (c) a debt in relation to which an impairment loss (or credit in respect of the reversal of an impairment loss) or release debit arises to the company in respect of an unpaid (or previously unpaid) business payment, and
>
> (d) a debt in relation to which a relevant deduction has been allowed to the company and which is released.

117. HMRC's case was that the money debt fell within s479(2)(a) as 'a debt on which interest is payable to...the company'. Their position was that when the ACT was paid early, it was a debt due by HMRC to AMC (although no one knew it at the

time) and that interest was payable on that debt. HMRC do not suggest that s 479(2)(b)-(d) are applicable and so I will only consider (a).

118. HMRC relies on the CJEU's decision in *Metallgesellshaft* and the House of Lords' decision in *Sempra* as authority that AMC was entitled to, and awarded, interest on the ACT. In other words, it is HMRC's case that the CJEU and House of Lords found that the ACT was 'a debt on which interest is payable to...the company'.

119. The appellant does not agree with this analysis.

120. To the extent that the appellant's analysis is a repeat of its case that the early payment of ACT was not a money debt owing by the Revenue to the taxpayer, I reject it for the reasons already given. But even taking account of my decision that at the time it was unutilised the ACT comprised a money debt, that leaves open the possibility that the award in *Sempra* was not of interest, but some kind of other remedy for unlawfully being kept out of its money. Indeed, AMC's case is that what was awarded in *Sempra* was a free-standing remedy of restitution to disgorge from HMRC the benefit of failing to recognise the taxpayer's right to freedom of establishment. It was not, says the appellant, interest on the ACT.

121. In order to make good this submission, the appellant relied on three matters and I will consider each in turn below:

(a) The award was restitutionary in nature and therefore was not an award of interest, even if calculated as if it were interest;

(b) The CJUE in *Metallgesellshaft* referred to the claim for compensation being the principle sum and the Lords in *Sempra* recognised that the compensation was free-standing, and not dependant on the payment of the ACT; and,

(c) thirdly, the award was to subtract the benefit of having the ACT from the Revenue and was not payment to the taxpayer for the use of the ACT over time.

*Was it calculated as interest but not interest?*

*(a) Metallgesellshaft*

122. Was AMC entitled to or awarded interest on the ACT? My understanding of the CJEU's conclusion at [96] in *Metallgesellshaft* (cited at §77) was that the premature levying of ACT was unlawful as it was discriminatory: but in circumstances where the principle sum had been repaid and national law would therefore leave the taxpayer without a remedy for this breach of Community law (because national law prohibited the payment of interest where the principle sum was repaid before the litigation commenced), that national law was to be of no effect and compensation in the form of interest was to be awarded.

123. Earlier in its judgment, the CJEU frequently referred to the compensation to be awarded as interest:

> [93] ...in the present cases, it is precisely the interest itself which represents what would have been available to the claimants, had it not been for the inequality of treatment, and which constitutes the essential component of the right conferred on them.
>
> [94]....the award of interest is an essential component of compensation for the purposes of restoring real equality of treatment...
>
> [95] In circumstances such as those in the cases in the main proceedings, the award of interest would therefore seem to be essential if the damage caused by the breach of article 52 of the Treaty is to be repaired.

124. However, it seems to me that the CJEU's decision cannot be read as conclusively determining that the award in *Sempra* was interest. The CJEU was not using the word 'interest' with the intention it should have the exact same meaning it carries under English and Welsh law, and in particular in the loan relationship rules. The CJEU was, as it always did, and was only able to do, making a decision applicable across the EU on the meaning of EU law. Its use of the word 'interest' in this context had, one must presume, its specific EU-law meaning, whatever that is.

125. All that can really be taken from the CJEU's decision with reference to what the was that, despite the rule in *La Pintada*, the UK must award compensation to the taxpayer for being kept out its money, compensation which they described as 'interest'.

126. For the purpose of the loan relationship rules, I have to determine whether, as a matter of English & Welsh law, the award made in *Sempra* was interest on the ACT.

*(b) definition of interest*

127. The parties did not appear to dispute the legal nature of interest: their dispute was whether interest was what the House of Lords awarded in *Sempra*. So what is interest?

128. In *Re Euro Hotel (Belgravia) Ltd* [1975] STC 682 at 691e Megarry J said, after reviewing the authorities, including Rowlatt J's off-quoted statement in *Bennett v Ogston* (1930) 15 TC 374 that interest was 'payment by time for the use of money':

> ...running through the cases there is the concept that as a general rule two requirements must be satisfied for a payment to amount to interest, and a fortiori to amount to 'interest of money'. First, there must be a sum of money by reference to which the payment which is said to be interest is to be ascertained. A payment cannot be 'interest of money' unless there is the requisite 'money' for the payment to be said to be 'interest of'. ...Second, those sums of money must be sums that are due to the person entitled to the alleged interest....'

129. My comment on this would be that, having approved what was said in *Bennett v Ogston*, Megarry J, in saying that the sum must be paid by reference to a principle sum, must have impliedly limited this to payments by reference to the use over time of the principle sum, otherwise the definition would seem to be rather wider than

intended. Other cases, such as *Riches v Westminster* (below) have assumed interest to be a payment for the use (or deprivation) of a sum of money for a period of time. I agree with HMRC that interest is an amount calculated by reference to another sum of money and by reference to the time for which that sum of money was outstanding.

130. I must apply those principles here.

*(c) the award in Sempra*

131. The appellant accepts that the award in *Sempra* was calculated in the same manner as interest: indeed the *Sempra* case largely concerned whether the calculation of the award should be compounded. The appellant's point, which I did not really understand HMRC to dispute, was that the manner of the calculation cannot change the fundamental nature of what was being awarded. The appellant's case is that the award in *Sempra* was to disgorge from the Revenue the benefit it received from denying the taxpayer its right to freedom of establishment, which just so happened, for the sake of convenience, to be calculated in the same way as interest would be calculated.

132. I accept the appellant is right to say that the mere fact it was calculated in the same way as interest does not make the award interest. In *John Lewis Properties plc* [2003] STC 117 Dyson LJ said:

> ... the way in which the lump sum has been calculated does not shed light on how it should be classified.... 'It confuses the measure of the payment with the payment itself'...

And in the earlier House of Lords case of *Glenboig Union Fireclay* 12 TC 427 Lord Buckmaster said, in a case where compensation calculated on the basis of loss of profit was nevertheless found to be capital in nature:

> '...But there is no relation between the measure that is used for the purpose of calculating a particular result and the quality of the figure that is arrived at by means of the application of that test....'

133. So I accept the fact that the award in *Sempra* was calculated as compounded interest does not tell the Tribunal whether the nature of the award was interest. So I consider what interest is, and whether what was awarded was interest, or merely calculated in the same manner as interest.

134. The point was addressed by the House of Lords in *Riches v Westminster Bank Ltd* [1947] AC 390. In that case, the taxpayer successfully sued a person for a sum of money and was in addition awarded interest on that sum by the court. The question was whether the defendant was bound to deduct tax on the amount awarded as interest under the Income Tax Act 1918. The appellant's case was that, although described and measured as interest, the sum was really a part of his award of damages and so not subject to deduction at source.

135. Lord Wright considered cases such as *Glenboig* and said:

> '...the distinction through these cases is whether the payments were payments of profits, that is, were income, or were payments on capital account estimated in terms of interest...a good illustration is to be found in *Glenboig Union*....in which it was held that the sum there awarded was in truth, though described as interest, only a method of determining the value of the fireclay sterilised in the hands of the company for which it was entitled to compensation. That was a payment on capital account; it was for the destruction of a capital asset, which was indeed the source of profits but could not be regarded as income....
>
> ...the contention is that money awarded as damages for the detention of money is not interest and has not the quality of interest. ... the essence of interest is that it is a payment which becomes due because the creditor has not had his money at the due date. It may be regarded either as representing the profit he might have made if he had had the use of money, or conversely the loss he suffered because he had not that use. The general idea is that he is entitled to compensation for the deprivation....The essential quality of the claim for compensation is the same and the compensation is properly described as interest.

Lord Simonds (with whom Lord Porter agreed) said:

> '...It is sufficient to say that in order to attract tax it must be established that the sum in question was income, and that it was that species of profit or gain which answers the description 'interest of money'....
>
> ....the argument is that...if it is damages, then it is not 'interest in the proper sense'....this argument appears to me fallacious. It assumes an incompatibility between the ideas of interest and damages for which I see no justification. It confuses the character of the sum paid with the authority under which it is paid. Its essential character may be the same, whether it is paid under the compulsion of a contract, a statute or a judgment of the court...But the real question is still what is its intrinsic character, and in the consideration of this question a description due to the authority under which it is paid may well mislead.'

Lord Normand gave a similar judgment although in addition he cited with approval the case of *Schulze v Bensted* (1916) SC 188 where the Lord President approved a dictionary definition that interest was 'the creditor's share of the profit which the borrower or the debtor is presumed to make from the use of the money'.

Viscount Simon said:

> '...the appellant contends that the additional sum....though awarded under a power to add interest to the amount of the debt, and though called interest in the judgment, is not really interest such as attracts income tax, but is damages. The short answer to this is that there is no essential incompatibility between the two conceptions. The real question, for the purpose of deciding whether the Income Tax Acts

> apply, is whether the added sum is capital or income, not whether the sum is damages or interest...
>
> ....It is not capital. It is rather the accumulated fruit of a tree which the tree produces regularly until payment....'

136. It can be seen from these citations that all the Lords in that appeal were agreed in their conclusion that the interest awarded as damages was interest within the meaning of the relevant taxing statute: their reasoning for this conclusion was also consistent among the five Lords. Damages awarded to compensate for the loss of use of a sum of money for a period of time was interest; and that was distinct from a case where the damages were to compensate for the loss of an asset, where the value of the asset was calculated by reference to the loss of the use of the asset for a period of time.

137. There is a telling contrast between what Dyson LJ said in *John Lewis Properties* cited above at §132 about the way in which a lump sum has been calculated not shedding light on how it should be classified, where he quoted the comment that 'it confuses the measure of the payment with the payment itself', and what Lord Simonds said in *Riches* about incorrectly assuming an incompatibility between interest and damages which 'confuses the character of the sum paid with the authority under which it is paid'. Even if at first glance these comments may appear to be inconsistent, they are not. They are reconciled if interest is understood to be a payment (made for any reason) which is intended to be a payment referable to, in the sense of having the use for a period time of, a principle sum: however, where the payment is actually intended to be in respect of the entire capital value of an asset, it is irrelevant that it is actually calculated by reference to the profits the asset could earn.

138. In conclusion, I reject the appellant's first ground for saying the award in *Sempra* was not interest. I agree with HMRC that *Riches v Westminster* does show that, though the award in *Sempra* was made to reverse the Revenue's unjust enrichment following a payment made under mistake of law, the character of that award was that it was intended to be a payment referable to, in the sense of being in respect of the use for a period of time of, a principle sum being the ACT. The cases of *Glenboig* and *John Lewis Properties* do not mean that in some way, because the award in *Sempra* was a restitutionary award, it cannot also be interest.

139. I consider that the Lords in *Sempra* were clear that the award they were making was an award of interest, albeit one made under the law of restitution:

> [22]...I also think that the time has come to recognise that the court has jurisdiction at common law to award compound interest where the claimant seeks a restitutionary remedy for the time value of money paid under a mistake
>
> [25]...The unjust enrichment principle supports the free-standing cause of action to recover interest, which is the measure of the enrichment.
>
> (Lord Hope)

> [178] the crucial insight in the speeches of Lord Nicholls and Lord Hope is...the recognition that what Lord Nicholls calls income benefits are more accurately characterised as an integral part of the overall benefit obtained by a defendant who is unjustly enriched. Full restitution requires the whole benefit to be recouped by the enriched party: otherwise 'the unravelling would be partial only'.....
>
> Lord Walker (agreeing with Lord Hope and Lord Nicholls)

*(d) conclusion on whether it was calculated as interest but not interest*

140. There is no essential incompatibility with an award of compensation made by a court with interest: if the award is of income nature, compensating for being kept out of a sum of money for a period of time, it is interest.

*Was it a free standing award?*

141. The appellant's next point was that the award made in *Sempra* was free-standing compensation, a principle sum, and not ancillary to a principle sum, and that relies heavily (again) on dicta of Lord Hope.

*(a) Sempra*

142. In particular, the appellant relies on what Lord Hope said in [1] and a few other paragraphs:

> [1] ...Questions about interest usually arise where the claim is presented as ancillary to a claim for a principle sum for which the court is asked to give judgment for the recovery of a debt or as damages. Less usually they can arise where interest is sought on a principle sum which has been paid before judgement. But in this case interest is the measure of the principle sum itself.
>
> ....
>
> [11]...the claim for payment of interest covering the loss of use over time of the sums paid by way of ACT is the very objective sought in the main proceedings. It is the principle sum claimed. We are not concerned in this case with the ancillary claim under the statute for simple interest. This is not a claim for discretionary interest on a sum for which judgment is given for the recovery of a debt or damages or which is paid before judgement.....
>
> ....
>
> [25]...The unjust enrichment principle supports the free-standing cause of action to recover interest, which is the measure of the enrichment.
> ....

143. In particular, the appellant relied on the fact that in [1] Lord Hope appeared to categorise Sempra's claim as something independent of a claim for interest on a principle sum, and in [11] and elsewhere referred to it as the principle sum and a free-standing cause of action.

144. However, if the appellant's case is that the award in *Sempra* was free standing from the ACT in the sense that (using Megarry J's phrase from *Euro Hotels)* the ACT was not 'a sum of money by reference to which the payment which is said to be interest is to be ascertained' this faces high hurdles:

(1) Such a meaning would appear to defy logic;

(2) Lord Hope himself did not appear to use 'free-standing' in that sense;

(3) None of the other Lords in *Sempra* took the view suggested by the appellant.

145. Taking the point on logic first. All the lords were agreed that the compensation, if payable, was payable because HMRC had had the ACT early. This was also clear from the CJEU's judgment. The point was that the breach of the taxpayer's treaty rights had involved the taxpayer in loss because it had paid corporation tax earlier than it would have paid it had its Treaty rights been respected. Logically, the compensation cannot be divorced from the reason the compensation was payable, which was the payment of the ACT. Logically, the ACT was the 'sum of money by reference to which' the award in Sempra was 'ascertained'.

146. Taking the second point next, Lord Hope himself recognised, as was obvious, that it was the early payment of the ACT that directly led to the loss which was to be compensated in *Sempra*:

> [31]...The essence of the claim is that the revenue was unjustly enriched because Sempra paid the tax when it did in the mistaken belief that it was obliged to do so when in fact it was being levied prematurely. So the revenue must give back to Sempra the whole of the benefit of the enrichment which it obtained. The process is one of subtraction, not compensation.
>
> [32]....subtraction of the enrichment from the defendant includes more than the return of the money that was transferred at its nominal or face value. That value, in this case, has already been accounted for. The subject matter of Sempra's claim is the time value of the enrichment. That is the amount that has to be assessed.

147. In those paragraphs, Lord Hope recognised that the claim to compensation for the time value of the enrichment (the compensation sought by Sempra in that appeal) was simply a part of subtraction of the overall enrichment from the Revenue arising from the payment of ACT. He effectively recognised that the ACT was the 'sum of money by reference to which' the award in Sempra was 'ascertained'.

148. It seems to me that his references to 'free-standing', cited above in [1], [11] and [25] and also made elsewhere in his judgement, must be seen in the context of what he was being asked to decide. He was being asked to decide whether the doctrine in *La Pintada*, which was that the right to interest on unpaid debts only arose if the debt was unpaid when the writ was issued, blocked the right to compensation in this case. So Lord Hope, when stating (see [8]) that the claim to compensation for breach of rights was independent of the right to recover the ACT, meant that it was independent in the sense that the claim could be pursued even if at the date the writ was issued, the

ACT had been repaid/set-off. That is what he meant by 'free-standing cause of action'. He meant that the cause of action could be lodged with the court without being paired with a writ for repayment of the ACT. He was not making any comment about whether or not the compensation was interest on the ACT.

149. Thirdly, nothing said by the other judges supports the appellant's view that that the ACT was not 'a sum of money by reference to which [the award in Sempra] is to be ascertained'. On the contrary, Lord Nicholls clearly saw the ACT as the sum of money by reference to which the award in Sempra was to be ascertained:

> [101] ...Sempra's claim is that it paid ACT in response to an unlawful demand and under a mistake of law....Sempra's claim is that under both causes of action restitution requires the inland Revenue to pay Sempra the value of the benefit the Inland Revenue obtained by having use of the money Sempra paid as ACT.
>
> [102] In principle, this claim is unanswerable. The benefits transferred by Sempra to the Inland Revenue comprised, in short (1) the amounts of tax paid to the Inland Revenue and, consequently (2) the opportunity for the Inland Revenue...to use this money for the period of prematurity....Restitution by the revenue requires (1) repayment of the amounts of tax paid prematurely (this claim became spent once set off occurred) and (2) payment for having use of the money for the period of prematurity.

150. Lord Walker stated broad agreement with both Lord Nicholls and Lord Hope ([154]) but did not recognise any disagreement between the two on the issue addressed above, no doubt because, if properly analysed, there was no difference between what they said on this issue. Nevertheless, at [183] he referred to cases, such as *Sempra,* where the 'principle sum' (the ACT) had been repaid before the issue of the writ, implying that he did see the compensation as referable to the ACT.

151. Lord Mance, while dissenting on the main issue in the appeal (how the award was to be calculated), appeared to agree with Lord Nicholls on the issue that the award was parasitic to the ACT. At [238] he said:

> [238] '..a situation like the present merely because the principle sum was recouped before action brought. It is true that such an extension involves recognising an independent equitable claim to recover interest....
>
> ....the essence of the UK's legislative scheme, and of the levying of ACT under it, was that the revenue would receive payment of tax prematurely, to hold until it as recouped by set off against mainstream corporation tax liability. Sempra was thus, by making taxable profits....able to recoup most of the principle sums by set-off. By the same token, to limit recovery of interest to a situation in which Sempra was *un*able to recoup the principle sums of ACT paid and had to sue for them, would be to confine recovery to atypical circumstances.'

152. Lord Scott, again, dissented. Nevertheless, his dissent related to whether there was compensation payable in restitution: he clearly saw any claim to interest as being ancillary to the overpayment of ACT: [132].

153. In conclusion, I agree with HMRC that, while expressing it differently, all the lords in *Sempra* recognised that the claim to compensation for the early payment of the utilised ACT was a claim which was parasitic upon that ACT and that in effect the ACT was 'a sum of money by reference to which the [the award in *Sempra]* is to be ascertained', but they were also saying that, because it arose under the law of restitution, it was compensation which was payable independently from the ACT, in the sense that the taxpayer could lodge a claim for the compensation even if at the date of the writ the ACT had already been repaid/set-off.

*(b) Westdeutsche*

154. Part of the appellant's case that the award in *Sempra* was an award of a principle amount was based on the Lords' ruling in *Westdeutsche Landesbank Girozentrale v Islington London BC [1996] AC 669* that compound interest could not be awarded as ancillary relief in restitutionary claims for a principle sum: in *Sempra* Lord Hope appeared to decline to depart from that decision, indicating that it should be distinguished on the basis that the award in *Sempra* was a principle amount itself and not ancillary relief:

> [36] Furthermore the interest in question in the present case is, as the Court of Justice stressed ... the principle sum itself. In my opinion the decision in the *Westdeutsche* case does not address this point. We were not asked to overruled that decision, because it is distinguishable on this ground.....

155. I do not agree that the effect of *Westdeutsche* was that the amount awarded in *Sempra* was not interest: even if Lord Hope was correct to view it as a principle sum rather than ancillary relief, he clearly regarded it as an amount of interest: he said in terms in [36] '...the interest in question in the present case....'.

156. In any event, Lord Hope's views on this were not shared by the three other lords in *Sempra* who considered *Westdeutsche.* Lord Scott did not consider the case: it was not relevant to his analysis, which was that there was no unjust enrichment and so no award should be made for the pre-limitation claims.

157. Lord Nicholls chose to overrule *Westdeutsche:* [112]; as did Lord Mance [240], and as did Lord Walker [184]. Lord Walker pointed out that the distinction which Lord Hope sought to make was anomalous:

> [183]...The House's decision in the *Westdeutsche* case...could be distinguished ...on the basis that in the *Westdeutsche* case the House was not concerned....with a case where part of the principal had been repaid before issue of the writ...But such a distinction would be anomalous and might be thought to leave the law in an even less satisfactory state.

158. He did not really elaborate on what he meant by that, no doubt because it was obvious: why should a person entitled to restitution, who has not yet received back the principle sum, only be entitled to *simple* interest on it, whereas a person entitled to restitution, but in the more advantageous position of having already received back the principle sum, be entitled to *compound* interest on it?

159. In conclusion, whether or not properly described as a principle sum or ancillary relief, what was awarded in *Sempra* was seen by all the lords as being interest; in any event only Lord Hope saw *Westdeutsche* as distinguishable from *Sempra*; the other lords saw it as incompatible and so departed from it, thus indicating that the award in *Sempra* was comparable in nature to an award of ancillary relief on claims where the principle sum was still outstanding..

*(c) Metallgesellschaft*

160. The appellant also relied on what was said by the CJEU in *Metallgesellschaft* as indicating that the CJEU saw the award as free-standing and not ancillary to the ACT and, therefore, not as interest on the ACT. The CJEU said:

> [87] In the main proceedings, however, the claim for payment of interest covering the cost of loss of use of the sum paid by way of advance corporation tax is not ancillary, but is the very objective sought....

And as I have said, the CJEU went on to rule that EU law required the national law to award compensation even if under domestic law there would be no ancillary relief on sums repaid before the writ was issued.

161. But in saying that the award sought and given in the case was not ancillary but the principle sum was clearly not intended by the CJEU to mean that what was to be awarded by national law was not interest. It clearly was interest under EU law as that is how the CJEU referred to it as cited above in §77. The CJEU saw no incompatibility between the award being both free-standing and interest: and the explanation of that is that is the same as for *Sempra.* By seeing the interest as being the 'very objective', or freestanding, or as the principle sum, the CJEU meant that it was possible to bring the claim for the relief *without* pairing it with a claim for repayment of the underlying ACT. But that did not change the character of the award from being an award of interest.

*(d) Was it a free-standing award – conclusion*

162. In conclusion, the court in *Sempra* and *Metallgesellschaft* referred to the right to claim interest on the ACT during the period it was unutilised using terminology such as 'principle sum' or 'free-standing' but what they meant by this is that the claim could be brought even though the ACT had long since been repaid or set-off. Nevertheless, both courts were clear that the character of the award was interest; it was referable to a principle sum (the ACT) and was a payment measured by the time that that sum was outstanding.

*Was the award one of subtraction of benefit?*

163. The appellant's last point (see §121) was that, even if the award of compensation was by reference to the ACT, in the sense described above, it was an award representing subtraction of benefit from the Revenue. Therefore, the award could not be described as being by reference to the ACT, in the sense of being payment for the use of the ACT over time. And this was the case, said the appellant, even though it was measured by reference to the ACT in the sense that it was calculated as interest on the ACT.

*(a) discussion*

164. Again the appellant relied on what Lord Hope said in *Sempra*:

> [31]...The essence of the claim is that the revenue was unjustly enriched because Sempra paid the tax when it did in the mistaken belief that it was obliged to do so when in fact it was being levied prematurely. So the revenue must give back to Sempra the whole of the benefit of the enrichment which it obtained. The process is one of subtraction, not compensation.
>
> [32]....subtraction of the enrichment from the defendant includes more than the return of the money that was transferred at its nominal or face value. That value, in this case, has already been accounted for. The subject matter of Sempra's claim is the time value of the enrichment. That is the amount that has to be assessed.

165. In other words, the justification for the award of interest was to extract from the Revenue the benefit they had obtained from unlawfully having the use of the corporation tax before it should have been paid to them (when the MCT was due). The other law lords saw a similar justification.

166. The law lords in the majority (Lords Hope, Nicholls and Walker) went on to decide that subtraction of the benefit from the Revenue was to be achieved by awarding an amount equal to the cost of the money over time, calculated on a compounded basis, but on rates reflecting the Revenue's cost of borrowing.

> [33]...money has a value, and in my opinion the measure for the right to subtraction of the enrichment that resulted from its receipt does not depend on proof by Sempra of what the revenue actually did with it. It was the opportunity to turn the money to account during the period of the enrichment that passed from Sempra to the revenue...Restitution requires that the entirely of the time value of the money that was paid prematurely be transferred back to Sempra by the revenue.
>
> Lord Hope
>
> [101]....restitution requires the inland Revenue to pay Sempra the value of the benefit the Inland Revenue obtained by having use of the money Sempra paid as ACT.
>
> [102] In principle, this claim is unanswerable. The benefits transferred by Sempra to the Inland Revenue comprised, in short (1) the amounts of tax paid to the Inland Revenue and, consequently (2) the opportunity

> for the Inland Revenue...to use this money for the period of prematurity....Restitution by the revenue requires (1) repayment of the amounts of tax paid prematurely (this claim became spent once set off occurred) and (2) payment for having use of the money for the period of prematurity.
>
> Lord Nicholls

167. Lord Walker said something similar at [193]. The minority (Lords Mance and Scott) did not agree. They considered that the logic of the law of restitution, founded upon the concept of unjust enrichment, dictated that the Revenue only had to repay their exact enrichment, not some figure of notional enrichment. The dissenters would only have required the Revenue to repay the benefit they could be shown to have received from having the early use of the ACT.

168. The dissent highlights what the majority decision actually was: the Revenue was not actually ordered to disgorge any actual benefit they had obtained from having the ACT early. They were ordered to pay an amount referable to the principle sum, and referable in the sense it was calculated as the cost of use of that sum over time. As was later noted by Lady Justice Arden in *Littlewoods* [2015] EWCA Civ 515 at [164] the Lords left open the possibility that in another case the creditor might not be awarded interest calculated in this manner if, for instance, the debtor could show benefit to him was less than compound interest.

169. But what was awarded in *Sempra* was interest, albeit the justification for it was as a proxy to subtract from the Revenue the unjust enrichment.

170. The appellant also referred me to what was said in *Schulze v Bensted*, cited above at §135 because it had been relied on by Lord Normand in *Riches.* The appellant reasoned that if interest was the creditor's share of the profit, then interest was not what was awarded where the purpose of the award was to extract benefit from the debtor. I do not agree with this proposition nor that *Schulze* is authority for the proposition. The full quote itself indicates that it is two sides of the same coin: interest compensates the creditor for loss of use of principle sum for a period of time while at the same time it extracts from debtor a sum which represents the value of having the principle sum for a period of time. A rule that, on the one hand, payments for the use of money over time which compensated the appellant are 'interest' while, on the other hand, payments for the use of money over time which are intended to extract profits from the debtor are not interest, would be wrong and unworkable: the same sum of money achieves both outcomes.

*(b) Was the award one of subtraction of benefit – conclusion*

171. The award in *Sempra*, and therefore the award which AMC would have received from HMRC if Wragge had not wrongfully settled its claim for a lesser amount, would have been one for interest. While the justification for awarding interest was to extract unjust enrichment from HMRC, it was an award which was to reflect use of a principle sum over time. It does not make it any the more or less interest because it was measured on the debtor's cost of borrowing rather than the creditor's rate of interest on deposits.

*Conclusion on whether it was it 'a debt on which interest is payable to...the company'*

172. I do not think how the 'interest' was calculated affects its classification: it is interest whether it is compound or simple, whether it is calculated on the borrowing rates available to the Revenue or the lending or borrowing rates available to Sempra. It does not matter whether it was to deprive the Revenue of having the use of the sum of money for a period of time or to compensate the taxpayer for not having the use of that same sum for a period of time. In all these cases the sum awarded was a sum referable to a principle sum (the ACT) and referable in the sense it was a payment for the use of that principle sum over time.

173. I note in passing, as HMRC referred me to it, that the FTT in *Coin-a-drink* [2015] UKFTT 495 held that interest on VAT repayment claims was taxable and that was not appealed; it is consistent with my analysis but offers no insight into the questions before me so I do not analyse the case any further.

174. I also note that it was a part of HMRC's case that the appellant accepted that the interest awarded by the court in *Sempra* on top of the main award made in that case, and representing the time use of the money from the date of claim, was properly taxable as interest, and therefore, said HMRC, it was irrational to dispute that the main award in *Sempra* was interest. I have not dealt with this submission as I have decided for other reasons that the main award in *Sempra* was interest.

**Relevant matters?**

175. The effect of my conclusion is that the payment of the ACT at the root of this appeal gave rise to a money debt, of a kind mentioned in s 479(2), owed by the Revenue to AMC. That means that there was a relevant non-lending relationship within the meaning of s 481 CTA 09 (set out at §64). But part 5 of CTA 2009 only applies to that 'non-lending relationship' to the extent of 'relevant matters' (see s 481(1)(a)).

176. It is worth referring to the exact terminology used in the legislation not least because the parties' in the skeletons and submissions frame the question in a manner that appears to miss out an element of it:

> **481 application of part 5 to relevant non-lending relationships**
>
> (1) If a company has a relevant non-lending relationship –
>
> (a) Part 5 (loan relationships) applies in relation to the relevant matters (see subsection (3) and (5)) as it applies in relation to such matters arising under or in relation to a loan relationship, but
>
> (b) the only credits or debits to be brought into account for the purposes of this Part in respect of the relationship are those relating to those matters.
>
> ....
>
> (3)The relevant matters in the case of a relevant non-lending relationship within s 479 are –

> (a) interest payable to or by the company in respect of the relevant non lending relationship;
>
> ....
>
> (c) in the case of a debt on which interest is payable to the company, profits (but not losses) arising to the company from any related transaction in respect of the right to receive interest.

177. HMRC's case is that payment from Wragge to AMC should be brought into account as income under the loan relationship rules. Therefore, the question is whether the payment from Wragge was a credit (s 481(1)(b)) which related to a relevant matter, as defined in s 481(3). The appellant and HMRC, however, read this provision as meaning that, rather than 'relating to' the relevant matter, the payment from Wragge must *be* the relevant matter.

178. On what I think is the proper reading of s 481, the question in this appeal is straightforward. A 'relevant matter' in s 481(3)(a) includes interest payable to AMC in respect of the relevant non-lending relationship. The interest that (up to the date of the unauthorised settlement of AMC's claim by Wragge) was owed by the Revenue to AMC was interest in respect of the relevant non-lending relationship. That is because it was clearly (as per *Sempra)* payable in respect of the ACT, and the ACT comprised the relevant non-lending relationship (because AMC had stood as creditor in relation to the money debt, being the ACT). I do not see that it makes any difference that until the House of Lords gave judgment in *Sempra*, which was long after the unauthorised settlement of AMC's claim, no one knew if or how much interest was owed by the Revenue to AMC.

179. The credits to be brought into account under s 481(1)(b) comprise those 'relating to' the relevant matters. The relevant matter, as I have said in the previous paragraph, was clearly the interest that (up to the date of the unauthorised settlement made by Wragge) the Revenue owed to AMC. The payment by Wragge to AMC following *AMC v Wragge* was clearly one which was 'relating to' that interest, as it was damages for AMC's loss of entitlement to that interest.

180. On the appellant's and HMRC's formulation of s 481, however, the question is less straightforward. Their reading is that the payment by Wragge must be (rather than relate to) the relevant matter, and if it is not, then it is not within the loan relationship rules. So I will, in the alternative, address this issue, although my decision is as set out in the previous paragraph and it concludes the appeal against the appellant (or would do if I had any jurisdiction in this matter).

181. If the appellant's and HMRC's formulation is right, then (to be within s 481(3)(a)) the payment by Wragge must be 'interest payable to...[AMC] in respect of the relevant nonlending relationship'. The appellant's case was that it was not. In part its case on this was a repeat of what had been said earlier about the claim between AMC and the Revenue not being a money debt and not being for interest. I have resolved that against it already. Putting those issues aside, the appellant's case was:

(a) the Wragge payment was not interest; and

(b) even if it was, it was not in respect of the relevant non-lending relationship.

*Was the Wragge payment interest?*

182. I deal firstly with the question whether the Wragge payment was interest. I have already cited at length from a number of cases giving an explanation of what interest is as a matter of law.

183. The appellant points out that its successful claim against Wragge was for loss and damage caused to it by Wragge having acted outside its authority or, in the alternative, having been negligent. It was not, says the appellant, interest payable to the company.

184. I have already said that considering the authorities such as *Euro Hotel, Bennettv Ogsten, and Riches v Westminster,* I agree with HMRC that interest is an amount calculated by reference to the amount, and the time outstanding, of a principle sum and its nature as interest is not affected by the fact it was awarded as damages. It is, for the reasons given at §§163-171, irrelevant that it was to extract the benefit of having the use of the sum for a period of time from the debtor.

185. The new question here, that did not fall to be answered when considering whether the award in *Sempra* was interest, is whether it makes any difference if the person who pays it was not at any point the debtor who owed the principle sum.

186. On this point, HMRC's case rested on *Re Hawkins Dec'd* [1972] Ch 714. In that case the deceased was a guarantor of a debtor's liability, including his liability to pay interest. As the debtor defaulted, the guarantee was called in and there was a question over the nature of the amount paid in lieu of interest. The Judge said:

> ....I find it hard to see why what he receives in discharge of the obligation should change its character according to who pays it and under what obligation, if any. If a tenant pays half his rent and the guarantor pays the other half, I suppose it would be said that of the sum put into the landlord's hands, only half of it is rent, the other half being a guarantor's payment in lieu of rent. I do not see why it should not all be rent. What matters is the nature or quality of the thing paid and not the source of the obligation to pay it. Rent is rent, a fine is a fine, a debt is a debt, and interest is interest, whoever pays it....
>
> (Megarry J at page 728)

187. The appellant quite correctly points out that this appeal is not on all fours with *Re Hawkins.* Wragge had never owed AMC the principle sum (the ACT) nor did Wragge guarantee HMRC would make payment to AMC of its claim in the ACT GLO; the Revenue's liability to pay AMC compound interest had ceased long before Wragge was found liable to pay AMC damages.

188. But Megarry J's dicta is quite general:

> 'what matters is the nature or quality of the thing paid and not the source of the obligation to pay it'

189. This echoes what Lord Simond said in *Riches v Westminster* that

> '[i]ts essential character may be the same, whether it is paid under the compulsion of a contract, a statute or a judgment of the court...But the real question is still what is its intrinsic character, and in the consideration of this question a description due to the authority under which it is paid may well mislead.'

190. My conclusion is that it is not relevant that Wragge never owed AMC the principle sum by guarantee or otherwise: what matters is that Wragge was found liable to pay in damages an amount equal to a sum of money calculated by reference to the amount, and the time outstanding, of that principle sum.

191. I accept that, unlike in *Riches v Westminster*, the order of the court at issue in this appeal was not to pay interest in addition to damages, but to pay damages. I do not see that it makes any difference: the court in *Riches* accepted that the entirety of the award was damages, but that did not prevent that element of it calculated by reference to the amount, and the time outstanding, of the principle sum being interest. And the same is true here. The entirety of the award in *AMC v Wragge* was an amount calculated by reference to the figure, and the time outstanding, of the principle sum, so the entirety of the award was interest.

192. I accept that the appellant is right to say that the award in *AMC v Wragge* was one step removed from the award in *Sempra*: it was an award that was calculated to be equal to the amount HMRC would have paid AMC but for Wragge' unauthorised settlement of AMC's claim. In other words, it was an amount calculated to be equal to an amount calculated by reference to the figure, and the time outstanding, of a principle sum. But I do not see that being one step removed in this sense makes any difference. The same could be said of the guarantor's payment in *Re Hawkins*, but the payment was still interest, as it was an amount calculated to be equal to interest. It was replacement interest.

193. AMC said that Wragge did not step into HMRC's shoes and in some sense this is true: Wragge never owed the principle sum to AMC. But when it settled AMC's claim without authority, it did in effect step into HMRC's shoes in that it rendered itself liable to pay an amount equivalent to the interest that HMRC would otherwise have had to pay AMC.

194. The appellant repeated what it said earlier that the mere fact something is computed as interest does not make it interest. But I have already dealt with this. If it is an amount computed by reference to the figure, and time outstanding, of a principle sum, it is interest, even if paid as damages or in restitution.

*Were the damages in respect of a relevant non-lending relationship?*

195. My conclusion is that the award of damages from Wragge to AMC was interest. But was it paid in respect of a relevant non-lending relationship, that relevant non-

lending relationship being (as I have already found) the fact that AMC had stood as creditor in relation to its early payment of ACT?

196. At first glance, I would say that the damages award paid by Wragge was clearly 'in respect of' AMC's position as creditor vis-à-vis the Revenue: it was Wragge's unauthorised settlement of that non-lending relationship that lay it open to the claim for damages.

197. The appellant does not agree. Its case is that:

(a) The Wragge payment was damages not interest;

(b) HMRC's obligations to AMC in respect of the utilised ACT ended in 2003; and

(c) Looked at realistically the payment by Wragge was in respect of its professional negligence and not the underlying action against the Revenue.

198. As far as point (a) is concerned, I have already dealt with, and rejected, this. The payment was both compensation and interest. It was interest as compensation.

199. As to point (b), I agree that the obligation HMRC had (although it did not know it at the time) to pay AMC in respect of its pre-limitation claims an amount equal to the excess of compound interest over simple interest ceased in 2003 (or, on HMRC's case, in 2005) when the claim was settled. But I do not agree that that means Wragge's obligation to pay damages was not 'in respect of' that obligation by HMRC. On the contrary, it was Wragge's unauthorised settlement of that non-lending relationship that lay it open to the claim for damages. The one replaced the other precisely because of Wragge's wrongful act in releasing the Revenue from the obligation.

200. Point (c), as I understood, was a reference to the decision in *Zim Properties v Proctor*(above) at page 108 where Warner J said:

> It seems to me that , if one is to search for 'the reality of the matter' the reality is that the taxpayer company derived the [money] from its right to sue the firm.

201. Superficially, that case can be compared to this one. In that case, as in this case, the wrongful act of the taxpayer's legal adviser deprived the taxpayer of the opportunity to obtain a sum of money. The conclusion in that case was nevertheless that the reality of the matter was that the taxpayer derived its right to the damages from its right to sue its legal advisers: not from the underlying source of funds that the legal adviser's wrongful act had terminated. So, says AMC, the reality of the matter in this case is that AMC derived its right to the damages from its right to sue Wragge, and not from the underlying source (the claim against the Revenue for compound interest) which Wragge by its wrongful act had terminated.

202. But the true reality is that such a comparison cannot be made. The question posed by the tax legislation at issue in *Zim Properties* was very different to the one

posed by the loan relationship legislation at issue in this appeal. The legal adviser's negligence in that case had deprived the taxpayer of the ability to sell some real property at a large profit: the taxpayer claimed that the damages were for a part disposal of that real property. The test in the legislation was whether a 'capital sum [was] derived from' the real property. The decision that it was not seems an entirely predictable one: how could the damages be derived from the real property when the taxpayer remained as much the owner of the real property before as after the negligent act of its adviser? There had been no part disposal of the real property: what had been terminated through the adviser's negligence was a lucrative contract under which the property could have been sold, not any right to the real property itself.

203. In contrast, in this case, the test is 'in respect of': there is no requirement to show that the right to the damages was derived from, or formed a part of, the relevant non-lending relationship. Moreover, the reality of the matter is that Wragge's wrongful act did terminate an aspect of that relevant non-lending relationship: it brought to an end the Revenue's liability to pay compound interest on the ACT (the money debt). It is entirely true to say that the damages were 'in respect of' that relevant non-lending relationship. It might even be true to say that the right to the damages was derived from the AMC's rights against the Revenue arising from that relevant non-lending relationship, but as that is not the test, I do not have to consider it.

204. In conclusion, had I not already dismissed the appeal (or would have dismissed the appeal if I had jurisdiction) on the grounds explained in §178-179, I would dismiss it on the construction of s 481 given by HMRC and the appellant. And that is because I find the payment by Wragge was a relevant matter. In other words, it was interest payable to AMC in respect of the relevant non-lending relationship for the reasons given above.

**Was it a related transaction?**

205. For the sake of completeness, and because the parties invested time and money in putting the case to me, even though my conclusion above renders it unnecessary, I will set out my views on the second part of HMRC's case on the taxation of the damages on the basis of the relevant non-lending relationship rules.

206. I have concluded that the payment of the ACT at the root of this appeal gave rise to a money debt, of a kind mentioned in s 479(2), owed (until offset against MCT) by the Revenue to AMC and that comprised a relevant non-lending relationship. But part 5 of CTA 2009 only applies to that 'non-lending relationship' to the extent of 'relevant matters' (see s 481(1)(a)). There are six relevant matters listed in the legislation (s481(3) but HMRC only suggest that two are potentially applicable (see §176). I have dealt with s 481(3)(a) and 'interest...in respect of the relevant non-lending relationship'. The second potentially relevant heading is (c) in the same sub-section which is:

> in the case of a debt on which interest is payable to the company, profits (but not losses) arising to the company from any related transaction in respect of the right to receive interest

207. As before, on what I think is the proper reading, s 481(1)(b) means that the Wragge payment is only caught by this provision if it is a credit which relates to the matter in s 481(3)(c) and a matter within (3)(c) is a profit arising to the company from a related transaction in respect of the right to receive interest. The appellant's and HMRC's reading is that the Wragge payment is only caught if it **is** a profit arising to the company from a related transaction to the right to receive interest on the debt. I don't think it makes any difference to (3)(c) which formulation is used.

*Definition of related transaction*

208. What is a related transaction? They are defined in s 304 CTA 2009 as:

> **304 'Related transaction'**
>
> (1) In this Part, 'related transaction', in relation to a loan relationship, means any disposal or acquisition (in whole or in part) of rights or liabilities under the relationship.
>
> (2) For this purpose the cases where there is taken to be such a disposal and acquisition include those where rights or liabilities under the loan relationship are transferred or extinguished by any sale, gift, exchange, surrender, redemption or release.

209. However, my view is that although the definition in s 304(2) is not exhaustive, nevertheless it was not intended to capture the creation of the relevant non-lending relationship but was rather to capture events which took place after the relevant non-lending relationship had been created as it refers to the rights being 'transferred or extinguished by any sale, gift, exchange, surrender, redemption or release'. In conclusion, the initial creation of the rights under the relevant non-lending relationship was not a 'related transaction' within s 304(2).

210. HMRC's view is that when Wragge entered into the 2003 agreement with HMRC (§42) purportedly on behalf of AMC, there was a disposal of rights acquired under the loan relationship and therefore that disposal was a 'related transaction' (s 304(1)); the payment to AMC following the ruling in *AMC v Wragge* was a profit (s 481(3)(c) arising to AMC out of that related transaction.

211. The appellant, needless to say, does not agree. It gives four reasons why it thinks HMRC's analysis in the above paragraph is wrong. It says, as it had already said in respect of this case, that the utilised ACT was not a money debt and, secondly, that the compensation payable by HMRC in respect of it was not interest. I have dealt with and rejected these two objections above and do not need to consider them a second time.

212. The other two reasons were that:

(a) S 481(3)(c) was not, says the appellant, in force at the relevant time;

(b) The Wragge payment was not, says the appellant, profit arising from the 2003 settlement.

213. The second is a shorter point and I take it first

*Was the Wragge payment a profit from a related transaction?*

214. As I have said, HMRC's case on this is that AMC's settlement with HMRC was the related transaction. The appellant's position is that even if that is right, the Wragge payment was not (says the appellant) a profit from that settlement. It points out that HMRC incurred a liability to pay AMC under that agreement, and did pay AMC, £4,828,346.19. That liability was calculated on simple interest. That, says the appellant, was the profit to AMC from the 2003 agreement.

215. I do not agree with this analysis. HMRC's liability to pay AMC interest arose from the payment of ACT to it by AMC (albeit no one knew this at the time). With hindsight, all the 2003 agreement did was to release HMRC from its full liability to pay compound interest to AMC on the ACT, while leaving its liability to pay simple interest on the ACT intact.

216. Even accepting that the simple interest was not profit to AMC from the settlement, the appellant's position is that the Wragge payment did not arise from the 2003 settlement. There was no liability in the settlement agreement for the Revenue to pay anything other than simple interest to AMC.

217. While that is of course true, HMRC's point is that it was inherent in the settlement that Wragges (although no one knew it at the time) incurred a liability to AMC, because the very act of committing AMC to the settlement was wrongful. So, says HMRC, the liability on Wragge to pay damages to AMC arose from the 2003 settlement agreement.

218. I agree with this. If the 2003 settlement agreement was a related transaction, it was a disposal of rights (within s 304(1)) under relevant non-lending relationship in the sense that AMC's rights to be paid compound interest by the Revenue were extinguished (s 304(2)) by release. So the question is whether the Wragge damages were a profit arising to AMC from that release/disposal of rights. And it seems to me that they were, because Wragge had no authority to release AMC's rights against the Revenue, which meant that the release of the rights by Wragge automatically and immediately gave rise to AMC's right of action against Wragge.

219. So in conclusion, the Wragge payment of damages was a profit to AMC arising from the 2003 settlement agreement, which was a related transaction.

*Was s 481(3)(c) in force?*

220. That conclusion is irrelevant unless s 481(3)(c) was in force at the relevant time. The commencement provision for s 481 was contained in paragraph 72 of Schedule 2 CTA 2009. The effect of that was that no profit arising under s 481(3)(c) was to be taken into account where the related transaction took place before 16 March 2005.

221. HMRC's accepted that the related transaction was the Agreement with HMRC which was entered into in 2003. Prima facie, HMRC are therefore accepting that the related transaction took place before 16 March 2005 and that therefore that s 481(3)(c) is not applicable.

222. HMRC do not accept that. A 'related transaction' was the 'disposal or acquisition (in whole or in part) of rights or liabilities' under the relevant non-loan relationship (see S304(1)). HMRC's case is that the 2003 Agreement was a disposal of rights under AMC's relevant non-lending relationship with the Revenue, but that disposal was conditional upon resolution of the ACT GLO and in particular resolution of the question of whether the claims were time-barred. The final decision in *DMG* was released in 2006 and so, say HMRC, the related transaction, in other words, the disposal, took place after 16 March 2005.

223. I do not agree. The effect of the 2003 Agreement was that AMC gave up any rights in its chose in action against HMRC other than the right to be paid compensation calculated on the basis of simple interest in the event DMG was successful in the ACT GLO limitation issues. AMC's disposal of its right to be paid compensation calculated on any other basis ceased at the date of the Agreement in 2003: therefore, by the date of the decision in *DMG,* AMC had already given up the right to be paid anything more than compensation calculated with simple interest. The disposal of the right to be paid compensation calculated by reference to compound interest was not conditional: it ceased in all circumstances on the date of the 2003 Agreement. The only thing that remained conditional after the date of the 2003 Agreement was the right to be paid compensation calculated as simple interest.

224. The appellant supported its case on this by referring me to *Lyon v Pettigrew* 58 TC 452 a case on the meaning of 'contract is conditional' in CGTA 79 where Walton J said:

> ...The words 'contract is conditional' have traditionally, I think, been used to cover really only two types of case. One is a 'subject to contract' contract, where there is clearly no contract at all anyway, and the other is where all the liabilities under the contract are conditional upon a certain event....But is is quite clear that the present contract is not in the slightest like that'

225. The appellant's point was that the 2003 Agreement had immediate effect as it ended its right to be paid compound interest and required AMC to immediately withdraw from the class action seeking compound interest (which AMC did). I agree with the appellant on this: the right to compound interest was disposed of in 2003.

226. The appellant also referred me to Steel J's ruling in *AMC v Wragge* where in [66-67] he referred to the right to contest the compound interest being lost in 2003. HMRC accepted the findings of fact in that decision, and in any event I have reached the same finding that the right to compound interest was given up by AMC in 2003.

227. That conclusion would resolve this issue against HMRC, although that is irrelevant to the disposal of this appeal, as I have already decided that HMRC succeeds on its primary case under the loan relationship rules.

**(B) Miscellaneous income otherwise not chargeable to tax?**

228. If I have jurisdiction, therefore, I would decide the applicability of the loan relationship rules in favour of HMRC. I would dismiss the appeal. However, as with all the earlier questions, as the parties asked me to consider whether s 979 is applicable if the loan relationship rules did not capture the damages, I will do so even though my decision on this is not operative.

229. S 979 CTA 2009 charges 'income not otherwise charged' to tax:

> **979 charge to tax on income not otherwise charged**
>
> (1) The charge to corporation tax on income applies to income that is not otherwise within the application of that charge under the Corporation Tax Acts.

230. HMRC's case is the damages from Wragge were income, and if not chargeable under the loan relationship rules, would be charged under s 979 as 'income that is not otherwise within the application of that charge'.

231. The appellant did not accept that the damages from Wragge were income, or that if they were, they were within the charge of s 979. So there are two questions:

(a) Were the damages income?

(b) If they were, do they fall within the scope of s 979 (assuming they are not caught by the loan relationship rules and that my decision on this above is wrong)?

**Were the damages income?**

232. As I understand it, the appellant's position is that the damages from Wragge were capital in nature because they extinguished an asset (the chose in action against Wragge for negligence/breach of contract); HMRC consider that the damages were income in nature because HMRC see them as replacing a sum of money (compensation in the form of compound interest that would have been payable by the Revenue to AMC were it not for Wragge's wrongful act) that would have been subject to corporation tax on income had it been received.

*Attwooll*

233. HMRC relied on the Court of Appeal's decision in *London Thames Oil Wharves v Attwooll* (1967) 43 TC 491. In the *Attwooll* case, a person negligently damaged property (a jetty) belonging to the taxpayer, which the taxpayer used for the purpose of generating income. The taxpayer received compensation from the negligent party and under an insurance policy which was intended to (a) recompense it for the cost of repairing the jetty and (b) make good the loss of profit during the time (about two years) that the jetty was out of action being repaired. The revenue accepted that the compensation for the cost of repairs was not subject for tax, but considered that the compensation for the lost profits was subject to tax. And that was the question before the Court of Appeal. It would only be taxable if it was income as, at that time, there was no taxation on capital receipts.

234. Diplock LJ said at page 515:

> Where, pursuant to a legal right, a trader receives form another person compensation for the trader's failure to receive a sum of money which, if it had been received, would have been credited to the amount of profits (if any) arising in any year from the trade carried on by him at the time when the compensation is so received, the compensation is to be treated for income tax purposes in the same way as that sum of money would have been treated if it had been received instead of the compensation. The rule is applicable whatever the source of the legal right of the trader to recover the compensation....
>
> ...the source of a legal right is relevant to the first problem involved in the application of the rule to the particular case, namely, to identify what the compensation was paid for. If the solution to the first problem is that the compensation was paid for the failure of the trader to receive a sum of money, the second problem involved is to decide whether, if that sum, money had been received by the trader, it would have been credited to the amount of profits (if any) arising in any year from the trade carried on by him at the date of receipt, that is, would have been what I shall call for brevity an income receipt of that trade. The source of the legal right to the compensation is irrelevant to the second problem. The method by which the compensation has been assessed in the particular case does no identify what it was paid for: it is no more than a factor which may assist in the solution of the problem of identification'

235. In other words, Diplock LJ was saying that if the compensation was for a sum of money that would have been income of the trade had it been received, then the compensation should be taxed in the same way.

236. He made it clear that the question of what the compensation was paid for should be carefully analysed: the mere fact that the compensation was calculated by reference to income did not mean that it was paid for loss of that income. Compensation paid 'for the destruction or permanent deprivation of the capital asset used by a trader for the purposes of his trade' would not be taxable. In such a case:

> .....As a result of such destruction or deprivation the trader ipso facto abandons that part of his trade which involves the use of the capital asset of which he has been deprived by destruction or otherwise, and profits which he would but for its destruction have made by its use or exploitation will thereafter no longer form part of the profits arising from the trade which he continues to carry on....
>
> ...Even if the compensation payable for loss of the capital asset has been calculated in whole or in part by taking into consideration what profits he would have made had he continued to carry on a trade involving the use or exploitation of the asset, this does not alter the identify of what the compensation is paid for, to wit, the permanent removal from this business of a capital asset which would otherwise have continued to be exploited in the business....

237. *Attwooll* is therefore consistent with *Glenboig* (see §§132-135 above): the compensation in *Glenboig* was for total loss of the ability to exploit a capital asset, and was therefore a capital receipt, albeit it had been calculated by reference to what income that asset could have earned. In *Attwooll,* the asset was only damaged, and so the compensation was *for* lost income (as well as calculated *as* lost income) and it was liable to income tax.

238. *Attwooll* was applied in *Donald Fisher (Ealing) Ltd v Spencer* [1989] STC 256. In that case, the taxpayer was the owner of a long lease, who recovered damages from its agent who had failed to serve a notice countering a notice for a rent increase above market value, thus rending the taxpayer liable to a higher rent than it would otherwise have been. The taxpayer claimed that the damages were a capital receipt representing a diminution of the value of its long lease. But the court applied *Attwooll* and held that it was a trading receipt as it was compensation for the business incurring higher business expenses then otherwise: it was subject to corporation tax. It was not a capital receipt as the lease remained in existence.

239. *Attwooll* was also applied in a case relating to investment, rather than trading, income. In the Privy Council case of *Raja's Commercial College v Gian Singh & Co Ltd* [1977] AC 312 the landlord had obtained damages against its former tenants who had out-stayed their lease and thus prevented the landlord from putting in a new tenant. The Privy Council held that the damages for trespass were compensation for lost rent and taxable as income. They specifically approved what Diplock LJ said in *Attwooll.*

*Qualification on Attwooll?*

240. The House of Lords considered *Attwooll* in *Deeny v Gooda-Walker Ltd* [1996] STC 289. The appellant was a name at Lloyds who received damages for negligent conduct of the underwriting business carried out in his name by his agent. The issue was whether the calculation of the appropriate damages should take into account liability to tax on the damages: the Revenue was joined to the action on the side of the appellant, taking the position that the damages were subject to tax.

241. The defendant's position was that the compensation to be awarded for its negligent conduct of the business was not a trading receipt and not liable to tax (and therefore, he claimed, the compensation should be reduced to reflect the fact that, had he not been negligent, the higher profits earned would have been subject to tax). The appellant won: the Lords unanimously ruled that the compensation itself was a receipt of the underwriting trade as it arose out of contracts with the agent entered into by the appellant in the ordinary course of its business.

242. Lord Hoffman went on to say that an application of what Diplock LJ had said in *Attwooll* would have led to the same conclusion: what he meant was that, as the compensation was for loss of income that would, if received, have been taxable as a receipt of the trade, the compensation was therefore similarly a receipt of the trade. He approved what Diplock LJ had said in *Attwooll* without reservation. However, Lord Browne-Wilkinson noted that there was at least one Court of Appeal case which had held that compensation for loss of trading income was not itself trading income: he was therefore not certain that Diplock LJ and Lord Hoffman were right to say that in all circumstances compensation for the loss of a business receipt was itself a business receipt. The other lords concurred with that reservation: in other words, they declined to consider whether or not Diplock LJ and Lord Hoffman were right. They did, however, say that what Diplock LJ had said to distinguish income from capital was right in all situations.

243. In conclusion, *Attwooll* has been applied in a number of cases, and its application is to any type of income: the distinction it makes between when compensation is a capital or income receipt has been unanimously upheld in the House of Lords. One law lord also upheld as an invariable rule that compensation for a receipt of the trade would itself be a receipt of the trade: the other judges were not certain whether this was a rule to which there were no exceptions.

244. And while I recognise that Lord Browne-Wilkinson in *Deeny* indicated that compensation for loss of a trading receipt might not always be a trading receipt, that does not appear to matter in this case as HMRC do not maintain that the damages are a trading receipt: they claim they are taxable under s 979 and s 979 captures income not caught under other taxing provisions. All the judges agreed in *Deeny* that *Attwooll* gave the correct test for determining whether compensation was a capital or income receipt.

245. Damages can therefore, as explained in *Attwooll*, be taxable as income; and applying *Attwooll* damages will be income and not capital for tax purposes if paid in compensation for failure to receive a sum of money which would have been treated for tax purposes as income.

*Extinguishment of cause of action is always a capital receipt?*

246. Having said that, nevertheless it was a part of the appellant's case that compensation for giving up a cause of action was by its nature a capital receipt. The appellant relied on *Scott v Ricketts* 44 TC 303. In that case, the taxpayer entered into a contract under which he was paid a sum of money if he agreed not to pursue a claim

in respect of some real property. The issue was whether he was subject to tax on that sum, particularly as the courts doubted that the taxpayer had ever had a legally enforceable claim over the land in question

247. Lord Denning MR said that the payment for this 'moral' or 'nuisance' claim should be treated the same as a compensation payment for a valid claim: as such a payment would not have been taxable, the payment in that case was not taxable. The appellant relied on Lord Denning's reasoning that the compensation paid for giving up a valid claim was not taxable:

> '[it] is not an annual profit or gain within Case VI. It is the sale of an asset – namely, his legal claim – for a price.'

248. If taken literally, this would appear to be inconsistent with the differently constituted Court of Appeal's decision a few months earlier in *Attwooll* and per incuriam, as *Attwooll* was not cited. However, Lord Denning, and the other two judges in delivering their concurring decisions, were addressing the question of whether it made any difference to tax liability whether the compensation was paid for the compromise a good legal claim or one which was known by the recipient not to be a good legal claim: he was not addressing the question of whether compensation paid to compromise a cause of action was always to be treated as the sale of an asset (in other words, a capital matter). The example Lord Denning used was a claim for personal injury; the case before him involved real property. A payment for compromising a cause of action in respect of either would not (normally) be subject to income tax. Indeed, Lord Denning seemed to recognise that some payments for giving up a cause in action which were part of the profits of the taxpayer's trade would be subject to income tax:

> If the sum was taxable at all it was table as part of the profits of Mr Rickett's trade or profession. Once that is negatived, it becomes simply a sum received in compromise or a disputed claim; whether legal or moral makes no difference.'

249. In conclusion, I accept that an out-of-court settlement of a claim should have the same tax treatment as an award made by the court would have had had the claim not been settled. But I do not accept that damages awarded in respect of, or compensation paid in settlement of, a cause of action are necessarily payment for giving up an asset (the cause of action). That would be quite inconsistent with *Attwooll* and *Deeny v Gooda*. I do not therefore see that *Scott v Ricketts* has any relevance to the question of whether the damages paid to AMC by Wragge were capital or income: that case did not address the question of how to determine whether damages are capital or income.

250. The appellant also relied on *Zim Properties v Proctor* for the proposition that a sum received by way of damages after judgment on a cause of action is by its nature a capital sum. I have already referred to the facts of this case at §202. The decision of the court was that the receipt of the compensation was not a part disposal of the real property to which the claim related; as it had been conceded (page 102h) that the sum was a capital sum, that meant that the entirety of it was subject to corporation tax on capital gains without any deduction for acquisition costs (as there were none). But as the capital nature of the receipt was conceded in that case, the court did not consider

whether or not that concession was right. The case therefore offers no support to the appellant's contention that damages after judgment on a cause of action is by nature a capital sum: that formed no part of the court's decision in *Zim*. And had it made such a decision, it would have been inconsistent with the higher authority of *Attwooll*.

251. Lastly, in support of its case on this, I was also referred by the appellant to *Able (UK) Ltd* [2007] EWCA civ 1207. In that case, the taxpayer had lost the use of an asset for three years and by the time he recovered the use of it, the market for what he produced with it had disappeared: he claimed the compensation he was paid for the loss of use of the property was therefore a capital receipt. In *Glenboig* the taxpayer had also retained ownership of the asset for the loss of use of which it was awarded compensation, so the taxpayer in *Able* considered that, likewise, its compensation should be seen as capital in nature.

252. But Moses LJ said at [10]

> [10] The principle to be derived from such cases as *Glenboig* and *Haig's (Earl) Trustees* is that consideration received for the once and for all realisation of the capital value of an asset is capable of being a capital receipt, notwithstanding that the asset remains in existence and is the property of the recipient .... That principle may be applied to cases where an asset has the capacity to provide a number of distinct sources of income and the capital value of the asset reflects each of those sources. If one particular source is exhausted or realised, then consideration or compensation paid therefore may constitute a capital receipt if the value of the asset, which had hitherto reflected all those sources of profit to be derived from that asset, is diminished.

He ruled against the taxpayer because the compensation was for loss of income and not loss of the ability to exploit the asset: the asset remained in existence and in the taxpayer's possession; the taxpayer was still able to continue to use the asset for the same purpose as before, it was merely no longer profitable to do so.

253. I do not see this case as offering any insight relevant in this appeal other than by affirming that *Attwooll* was correctly decided: the payment of compensation to replace a source of income temporarily restricted is itself to be taxed as income.

*Attwooll not applicable after introduction of capital gains tax?*

254. My rejection of the appellant's case regarding *Scott v Rickets*, *Zim* and *Able (UK) Ltd* depends in part on the appellant's reading of those cases being inconsistent with *Attwooll*. But the appellant's case is that the rule in *Attwooll* is irrelevant because the rule's only purpose was to determine whether or not a sum was subject to tax. The appellant's point seems to be that at the time of the *Attwooll* decision, there was no tax on capital gains and so the question in that case was whether or not the compensation was subject to tax or not. In one sense, of course, that is quite true.

255. Now companies are subject to tax on capital gains so, says the appellant, the rule in *Attwooll* no longer applies. I have great difficulty in understanding the logic in this submission. *Attwooll* clearly decided that if the compensation was capital in

nature, and not replacement for a trading receipt, then it was not subject to income tax. The fact there was no tax on capital gains at that time was quite irrelevant to the decision. And it would be wrong to say that the decision is an irrelevance even now. While it is now the case that the distinction between a receipt being income or capital is less acute than in 1966 as both are taxed, they are not taxed on the same basis, and it can often make a difference to the exact liability whether the receipt is properly taxable to income or capital.

256. I entirely reject the appellant's case that the rule in *Attwooll* in some way was only applicable to determine whether a receipt was subject to tax or not: the rule was quite clearly to determine whether compensation was taxable as an income receipt. It is as valid now as in 1966, subject to the possible qualification recognised by the Lords in *Deeny v Gooda*. Indeed, if the rule in *Attwooll* was so limited, I would have expected the Lords to have said so when they considered it in *Deeny* in 1996, long after capital gains tax had been introduced. Instead of which it was approved, subject to that one qualification on one aspect of the rule.

*Attwooll not applicable at two stages removed from the income?*

257. In this case, AMC received damages from Wragge to replace the compensation it would otherwise have been entitled to receive from the Revenue, payable for being wrongfully kept out of its money for a period of time.

258. So it seems to me that I must determine whether the compensation which AMC would have received from the Revenue had its claim not been wrongfully compromised would have been an income or capital receipt, in order to determine whether the Wragge payment was itself an income or capital receipt.

259. The appellant does not agree. It says that the rule in *Attwooll* cannot be used at two places removed: the rule (if anything) says the appellant, determines whether compensation for loss of something is subject to income tax, it does not determine whether compensation for the loss of compensation for something else is subject to income tax. The point is that the *Attwooll* case and any case applying *Attwooll* have only dealt with facts where the compensation was one step removed from the source, not two steps removed from the source, as here.

260. The appellant's analysis, as I understand it is that while *Attwooll* might apply to make any compensation paid by the Revenue following *Sempra* to AMC subject to corporation tax as interest (and that is how AMC did declare such sums in its tax returns), the cause of action against Wragge was one further step removed from the ACT and the damages paid in respect of it are therefore capital.

261. I do not see the logic in this. While I accept *Attwooll* has not in practice been applied two steps removed from the source which is being compensated, I see no reason in principle why it should not apply in those circumstances. The Wragge damages were ordered to be paid to put AMC in the same position as it would have been had it received the compensation it should have received from the Revenue had it not been for Wragge's wrongdoing: it seems only logical that the damages should

be taxed in the same way that that compensation would have been taxed if received. I reject the appellant's case on this.

262. The appellant raises another defence, which, if I understand it correctly, is that *Attwooll/Glenboig* decided that compensation for a permanent loss of a source of income would be capital while compensation for a temporary deprivation of income would itself be income: therefore, says the appellant, the Wragge damages were compensation for the permanent and total loss of AMC's right to an award of compensation from the Revenue calculated on the basis of compound interest and therefore the Wragge payment falls on the *Glenboig*/capital side of the line.

263. But this is to misstate the rule: the rule in *Attwooll* was that if the sum for which compensation is paid 'would have been credited to the amount of profits (if any) arising in any year from the trade carried on by him at the time when the compensation is so received, the compensation is to be treated for income tax purposes in the same way as that sum of money would have been treated if it had been received instead of the compensation'. (Of course, as expressed there it relates only to trading profits (which were at issue in that case) but as I have said, the rule was expressed to apply to income generally in the *Raja's* case). But the point is that whether there is permanent or temporary deprivation of a source of income is relevant to the question of the nature of what is being compensated. Here, Wragge's wrongful act did deprive AMC permanently of an asset (its cause of action against the Revenue for compound interest) but that asset was not, for reasons given above a capital asset. The question is how the compensation from the Revenue would have been taxed had it been received, and under *Attwooll*, that will determine the treatment of the damages paid in lieu by Wragge.

264. It does not matter that the compensation paid by Wragge is two steps removed from the source of the claim (the ACT).

265. The appellant also says that the rule in *Attwooll* cannot convert a capital payment into an income payment and I entirely agree. But that is not what has happened here. The compensation from the Revenue to which AMC had been entitled up until Wragge's unauthorised settlement of its claim would itself have been an income payment; AMC's right to sue Wragge was therefore an income entitlement and not a capital asset.

*What were the damages paid for?*

266. Applying *Attwooll*, therefore, I must decide whether the damages from Wragges replaced what would otherwise be an income or capital receipt. This is because, as I have said, s 979 only applies to income receipts.

267. The compensation received by the appellant from the Revenue (simple interest on its pre-limitation and in-time utilised ACT claims, and compound interest on its unutilised ACT claims) had been shown as interest in AMC's accounts and declared to corporation tax in its tax returns, but AMC has made no concessions in this Tribunal with respect to the treatment of the extra compensation it would have been

entitled to receive from HMRC were it not for Wragge's unauthorised compromise of its cause of action.

268. And that means, it seems to me, that the rule in *Attwooll* must be applied to the compensation that AMC should have, but did not receive: would that compensation have replaced an income or capital receipt? The appellant again makes the points here which it made in respect of the loan relationship part of the case: it says that the sum of money which the Wragge payment replaced was not interest, but a restitutionary payment merely calculated as interest and/or the compensation was the principle amount and not ancillary to the ACT and therefore could not be interest (however calculated). I have dealt with and rejected these points above.

269. The appellant also made a new point: it said that the compensation payable by HMRC under *Sempra/DMG* was actually for damage or impairment to the capital structure of AMC's business in that it was for a restriction on AMC's right to freedom of establishment. Moreover, said the appellant, it was a once and for all realisation of its right to freedom of establishment as its capacity to obtain income from it was ended.

270. This submission must also be rejected. Firstly, even if it is right to see the appellant's right to freedom of establishment as a capital asset of its business, the levying of ACT without the right conferred on UK group companies to make a GIE was no more than an impairment of that right: the right to freedom of establishment can be exercised by doing many things, such as in choosing the place of incorporation and in carrying on business and investing money cross-border: the freedom to pay dividends to a parent company without a financial restriction that is not also imposed on other companies is simply one aspect of its right to freedom of establishment. There was no once and for all realisation of its right to freedom of establishment: AMC very much retains its right to freedom of establishment.

271. Therefore, even if it is correct to see the right to freedom of establishment as a capital asset of AMC's business, the unlawful treatment explained in *Metallgesellschaft* amounted to nothing more than an impairment of it. The mere impairment of an ability to generate income from a capital asset, as is clear from *Attwooll,* is an income receipt.

272. However, in any event, I do not think it is correct to see the right to freedom of establishment as a capital asset of the business. It was simply a legal right which could be exercised. The asset which was the subject of the legal proceedings was the money which AMC paid to the Revenue as ACT: the right to freedom of establishment was the legal right the breach of which by the Revenue gave the appellant its right to restitution of that ACT. It can be compared to *Attwooll* where the capital asset was the jetty: the right to a duty of care from the users of the jetty was the right the breach of which gave the taxpayer its rights to compensation. That duty of care was no more a capital asset that the right to freedom of establishment. They were legal rights, not capital assets.

273. As I have said, the rule in *Attwooll* must be applied to the compensation that AMC should have, but did not, receive: would that compensation have replaced an income or capital receipt? I have already determined the answer to this question above in answer to the loan relationship question. It would have been an income receipt because it would have been interest: it was damages as interest.

274. In conclusion, the compensation which the Revenue would have been liable to pay AMC but for Wragge's unauthorised settlement of its claim would itself have been taxed as interest. In turn, that means that the damages paid by Wragge in compensation for its breach of contract/negligence are income as they replace compensation that was interest.

**Are the damages within the scope of s 979?**

275. As I have said, s 979 only applies to income: and I have determined that the damages paid by Wragge were income of AMC. But there is then a second question which is whether s 979 applies to tax that income.

276. The appellant referred to cases on Schedule D Case VI (the predecessor to s 979 which charged to tax 'any annual profits or gain not falling under any of the foregoing Cases, and not charged by virtue of any other Schedule'), such as *Jones v Leaming* 30 AC 415 where Lord Dunedin said:

> 'Case VI sweeps up all sorts of annual profits and gains which have not been included in the other five heads, but it has been settled again and again that that does not mean that anything that is a profit or gain falls to be taxed....
>
> ...[profits and gains in Case VI] must mean profits and gains ejusdem generis with the profits and gains specified in the preceding five Cases....'

277. However, this case should be seen in its context which was whether a one-off sale of real property was caught by Case VI and, as the judges said, as it was a one-off it was not a venture in the nature of trade, and so it was a capital gain and outside Case VI as it was not income. So while it is right to say that some profits did not fall within Case VI, this case provides no sort of analogy with the damages received by AMC, as, while they were clearly a one-off, they were income.

278. The appellant also relied on *Scott v Ricketts* which I have discussed above in the context of rejecting the appellant's case that the compromise of a right of action must always be a capital gain. The issue in *Scott v Ricketts* specifically, however, was whether the receipt by the taxpayer of compensation for agreeing not to assert his moral claim to a piece of land was taxable under Case VI.

279. The passage by Lord Denning relied on by the appellant was devoted to explaining why it made no difference to the tax treatment of the payment in question that fact it was 'dressed up' as paid under a contract while in law the taxpayer had not had any real claim to the property: the payment to settle the claim would be taxable in the same manner as if his claim had had legal merit. As I have said, Lord Denning

was not seeking to establish a general rule that payments in compromise of a legal action were always capital: the issue did not arise in that case as the 'moral' if not legal claim related to real property and (like the example used by Lord Denning of a personal injury claim) the settlement of such a claim was clearly not income. Far from it, as I have said, Lord Denning recognised that it was possible for a settlement of a claim to amount to the profits of a trade, just that that was not applicable in that case. The same analysis could also be applied to what the other two judges said in that case.

280. So this case is not support for saying interest paid in restitution could not fall in s 979: the payment in *Scott v Ricketts* was a capital payment so by definition it could not fall within Case VI (or what is now s 979). This is also true of the payment in *Jones v Leeming*. So what income can fall within s 979?

281. HMRC relied on the decision in *Spritebeam* [2015] UKUT 1222 (on Case VI) which sought to give a definition of what would fall within Case VI:

> ...(i) the receipt must have the character of income (a word we use as an umbrella term to include the profits or gains to which Case VI refers) (ii) it must be the recipient's income; (iii) it must have a source; and (iv) there must be a sufficient link between the source and the recipient.'

But this case was really concerned with the question of whether income received but not earned by the recipient could be taxed on it. This was because at the heart of the case was a tax avoidance scheme in which the charge for a loan was irredeemable preference shares to be issued by the borrower to a company connected with lender. The crux of that case was whether a recipient could be taxed on a receipt in circumstances where it had no legal right to enforce payment of it, an issue which does not arise in this appeal. Nevertheless, applying the *Spritebeam* test, the damages paid to AMC by Wragge did have (i) the character of income. I have found that it was income. The damages certainly belonged to AMC (ii), had Wragge as its source (iii) and there was a clear link between AMC and Wragge (iv) which was the legal services contract the breach of which gave rise to Wragge's liability.

282. An application of the definition of s 979 in *Spritebeam* would lead to the receipt from Wragge falling within s 979.

*Interest is not within s 979?*

283. I have found that the Wragge damages were income paid to AMC in replacement for interest which it had been owed (up to the point of Wragge's unauthorised settlement) by the Revenue to AMC. The parties were agreed that the damages were not taxable as interest: they were taxable under the loan relationship rules or s 979 or otherwise were not taxable as income.

284. The appellant's point is that as the Wragge damages were not taxable as interest, yet on HMRC's case replace interest, *Attwooll* cannot apply to put the replacement income into the s 979 sweep up provision: *Attwooll* applies, says the

appellant, only to tax the replacement income under the same heading as the income it replaces, or not at all.

285. It is certainly true in *Attwooll* that the decision was that the compensation for the damage to the jetty was found to be taxable as profits of the trade, in the same way that the income the compensation replaced would have been taxable, and that was the rationale given by Diplock LJ:

> profits (if any) arising in any year from the trade carried on by him at the time when the compensation is so received, the compensation is to be treated for income tax purposes in the same way as that sum of money would have been treated if it had been received instead of the compensation.

286. However, it seems to me that, fundamentally, the rule in *Attwooll* determines whether a receipt was income or not. Lord Diplock clearly addressed the question of whether the sum was income or capital and explained the rule for deciding that it was income: see §§234-235. The Lords in *Deeny v Gooda* expressly approved this as right in all circumstances: §§241-243. So it seems to me that the logic of *Attwooll* is that if the sum is income because it is paid in compensation for lost income (and not for a lost capital asset), but yet can't fall into the same taxation provision as the income it replaces, then it ought to fall into the sweep up provision of s 979.

287. Indeed, in *Raja's* [1976] 2 All ER 801 the appellant was awarded damages for trespass representing the rent it would have been able to receive had it been able to re-let the property. The Privy Council appeared to accept that the damages were not themselves rent, but would be taxable as 'other profits arising from property'.

288. I also note that while the Lords in *Deeny v Gooda* were certain that in all circumstances damages which replaced income would be income, their qualification was that they were not certain Diplock LJ had been right to say that in all circumstances damages which replaced trading income would themselves be trading income. The logical resolution of this conundrum is that if the replacement income does not fall within the same type of income as the income it replaces, as income it should be taxed under the sweep up provision of s 979.

289. The appellant certainly advanced no logical explanation of why s 979 should not apply in these circumstances: if income replaces income that would itself have been taxed, then Parliament's intent behind s 979 must have been for it to be taxed. Therefore, if it does not fall under the same specific taxing provision as the original income, then the replacement income should be taxed under the sweep up provision in s 979.

*Conclusion*

290. I am satisfied that HMRC's case on this should succeed as well as its case under the loan relationship rules: the damages from Wragge were income and would fall within s 979 were they not already taxed under the loan relationship rules.

## Overall conclusion and appeal rights

291. I do not consider for the reasons I have already given that I have any jurisdiction in this matter. For that reason, the appeal should be struck out or dismissed. But if I am wrong and do have jurisdiction, I dismiss the appeal on the basis that the amendment under appeal was correct because the payment from Wragge was liable to tax under the loan relationship rules, or if I am wrong on that, under s 979.

292. 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.

**BARBARA MOSEDALE**
**TRIBUNAL JUDGE**

**RELEASE DATE: 25 SEPTEMBER 2017**