[2015] UKUT 0633 (TCC)

Appeal numbers: UT/2014/0054
UT/2014/0052

INCOME TAX – deduction of tax at source – whether "interest arising in the United Kingdom" – ITA 2007, s 874 – source of interest - test to be applied – whether a multi-factorial test, a test of nationality of the loan document or a place of credit test – National Bank of Greece considered – appeals dismissed

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

(1) ARDMORE CONSTRUCTION LIMITED
(2) ANDREW COLIN PERRIN **Appellants**

- and -

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

TRIBUNAL: MR JUSTICE MORGAN
JUDGE ROGER BERNER

Sitting in public at The Royal Courts of Justice, The Rolls Building, Fetter Lane, London EC4 on 19 and 20 October 2015

Patrick Way QC, instructed by BDO LLP and Blackstar (Europe) Limited, for the Appellants

Richard Vallat, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. These appeals revisit some familiar territory. They concern the question whether interest paid on certain loans arose in the UK, such that the payer was under an obligation to deduct UK tax when making the payment and to account for the tax so deducted to HMRC.

2. There are two appeals before this Tribunal which raise the same issue of law, although of course the facts are not the same in each. In each case the First-tier Tribunal ("FTT") found that the interest in question arose in the UK, and that each of the appellants, in one case a company, Ardmore Construction Limited ("Ardmore"), and in the other an individual, Mr Perrin, was liable for tax that should have been deducted.

The statutory provisions

3. The key provision is s 874 of the Income Tax Act 2007 ("ITA"), which materially provides:

> "(1) This section applies if a payment of yearly interest arising in the United Kingdom is made—
>
> (a) by a company,
>
> (b) by a local authority,
>
> (c) by or on behalf of a partnership of which a company is a member, or
>
> (d) by any person to another person whose usual place of abode is outside the United Kingdom.
>
> (2) The person by or through whom the payment is made must, on making the payment, deduct from it a sum representing income tax on it at the basic rate in force for the tax year in which it is made.
>
> (3) But see—
>
> (a) sections 875 to 888 as to circumstances in which the duty to deduct a sum under this section is disapplied …"

4. It was common ground before us that there was no distinction between the place where interest arises for the purpose of s 874, and the source of that interest. Thus, although at the Tribunal's prompting there was some debate as to the significance in that event of the exclusion from the duty to deduct for "relevant foreign income" in s 884 ITA ("relevant foreign income" being defined by s 830 of the Income Tax Trading and Other Income) Act 2005 ("ITTOIA") as being income "arising from a source outside the United Kingdom"), there is no need for us to make any finding in that respect.

5. Section 874 ITA itself derived from earlier provisions to the same effect. Its immediate predecessor was s 349 of the Income and Corporation Taxes Act 1988

("TA"), which applied to yearly interest of money chargeable to tax under Case III of Schedule D. It is from the schedular system that applied from its inception in Addington's Act of 1803 to its eventual abolition for income tax purposes from 6 April 2005, and for corporation tax from 1 April 2009, that the concept of source of income emanates. For income to be chargeable under Schedule D, Case III, it generally had to have a UK source. Other cases of Schedule D, Cases IV and V, applied to income arising from securities or possessions out of the UK. There was thus a UK source requirement inherent in interest chargeable under Case III, Schedule D, which has translated across from s 349 TA to s 874 ITA.

6. There is also a principle of territorial scope that has been relevant to judicial consideration of the concept of source. For completeness, therefore, we should refer to the material parts of s 368 ITTOIA, which sets out, in relation to savings and investment income included within Part 4 of that Act, such as interest, that territorial scope in statutory form:

> "**368 Territorial scope of Part 4 charges**
>
> (1) Income arising to a UK resident is chargeable to tax under this Part whether or not it is from a source in the United Kingdom.
>
> (2) Income arising to a non-UK resident is chargeable to tax under this Part only if it is from a source in the United Kingdom …"

The charge to tax on a UK resident is subject to special rules for relevant foreign income in Part 8 of ITTOIA, which applies the remittance basis in certain circumstances in relation to non-UK source income.

7. Finally, although there are different statutory mechanisms for collection of tax deducted, or which should have been deducted, from a relevant interest payment, depending on whether the payer is an individual or a company, those are not material to these appeals, and we need not refer to them.

The appellants' cases

8. The appellants put forward three principal grounds of appeal each of which is submitted in the alternative.

9. The first (nationality or residence of the document) is that the source of the interest should properly be found by ascertaining the "nationality" or the "residence" of the relevant loan instrument. The argument is that the FTT below in each case erred in applying instead a multi-factorial test.

10. The second (multi-factorial test) is that if, contrary to the first ground, the proper test is a multi-factorial test, the FTT in each case erred by affording too much weight to the residence of the debtor. It is submitted in this connection that the residence of the debtor is not a relevant factor at all where, as in these cases, the loan instruments in question are subject to the laws of a foreign jurisdiction. The appellants also raise supplemental points concerning the application by the FTT of the

multi-factorial test: a confusion of jurisdiction and enforcement, the place and receipt of interest payments and (in Mr Perrin's case) the fact of assets in the Isle of Man.

11. The third (place where credit is provided) is that it is the place where the credit is provided that is the source of the interest. This submission was rejected by the FTT in *Ardmore*. It was not originally a ground of appeal in *Perrin*, but HMRC had no objection to it being added as a ground in Mr Perrin's appeal to this Tribunal, and it was therefore admitted.

Discussion

12. Given the longevity of the source principle in relation to the taxation of interest, and the requirement, albeit subject to extensive exceptions, that tax be deducted at source from yearly interest having a UK source, the paucity of domestic authority is a little surprising. There is, in fact, but a single authority which is binding on this Tribunal, namely *Westminster Bank Executor and Trustee Co (Channel Islands) Ltd v National Bank of Greece SA* [1971] AC 945; (1970) 46 TC 472 ("the *Greek Bank* case"), in the House of Lords.

13. At issue in the *Greek Bank* case was the question whether the appellant (defendant), National Bank of Greece, which had become, by a process of universal succession, the guarantor of certain sterling mortgage bearer bonds issued by the National Mortgage Bank of Greece in 1927 and 1930, had been correct to deduct income tax at the then standard rate when making payments of interest on the bonds to the respondent (claimant), Westminster, which was a Channel Islands company not resident in the UK.

14. The issuer of the bonds, National Mortgage Bank of Greece, was a Greek corporation. The original guarantor, also called National Bank of Greece, was a Greek corporation as well, which had no place of business in the UK. By a Greek decree in 1953, the original guarantor was amalgamated with another company, both were dissolved, and a new company was formed as the National Bank of Greece and Athens SA. That company, a Greek corporation, was declared to be the universal successor of the original guarantor upon which it acquired, and maintained, a branch in the UK at which it carried on business. It subsequently changed its name to the National Bank of Greece.

15. The bonds were bearer bonds denominated in sterling, which were raised in London. They were secured on land and public revenues in Greece, but the liability on the guarantee was not separately secured. They bore interest which was payable half-yearly on the presentation of coupons which were attached to the bonds. Payment of interest, at least to holders not resident in Greece, was to be made in sterling at the offices of Hambros Bank Ltd or Erlangers in London or, at the option of the holder, at the National Bank of Greece in Athens, Greece, by cheque on London. It was established in separate proceedings that the proper law of the bonds and of the guarantee was English law (*National Bank of Greece and Athens SA v Metliss* [1958] AC 509), and that the English courts would enforce the guarantee against National Bank of Greece as the universal successor of the original guarantor.

16. As Lord Denning MR in the Court of Appeal in the *Greek Bank* case, at 46 TC pp 483-484, described the position, in 1941 the Germans captured Athens and occupied Greece. The result was that the principal debtor, the National Mortgage Bank of Greece, was left with nothing with which to pay the bonds. The Greek properties on which the bonds were secured were taken over or in some way disappeared, so as no longer to be available. In 1949, the Government of Greece passed a law suspending all obligations on the bonds and imposed a moratorium. In the result, as a matter of Greek law, the liability of the principal debtor and guarantor was extinguished in Greece, but the liability of the guarantor could be enforced as a matter of English law and was recoverable by execution against its assets in England.

17. It was held by the House of Lords that the source of the relevant obligation, that of making payment under the guarantee, was situated outside the UK. As such, the income was not taxable under Case III of Schedule D, and not taxable at all on a person not resident in the UK.

18. The only reasoned speech in the House of Lords was that of Lord Hailsham LC, with whom all the other law lords agreed. After reciting the facts, and the relevant provision – s 170 of the Income Tax Act 1952 - on which the claim to deduct tax was based, Lord Hailsham referred to the territorial limitation on the chargeability of non-residents in respect of income from property outside the UK, citing Lord Herschell in *Colquhoun v Brooks* (1889) 14 App Cas 493, at p 504:

> "The Income Tax Acts themselves impose a territorial limit; either that from which the taxable income is derived must be situate in the United Kingdom, or the person whose income is to be taxed must be resident there."

19. That territorial limitation, so far as it relates to interest is, as we have described above, now contained in s 368 ITTOIA.

20. Based on that territorial limitation, Lord Hailsham accepted the submission of Mr J P Warner, counsel appearing as amicus curiae, instructed by the Inland Revenue, that the question resolved itself simply into whether the source of the payments under the guarantee was or was not situated in the UK. Lord Hailsham concluded in the following terms, at 46 TC pp 493-494:

> "I have come to the conclusion that the source of the obligation in question was situated outside the United Kingdom. This obligation was undertaken by a principal debtor which was a foreign corporation. That obligation was guaranteed by another foreign corporation which, as was conceded before us, had at no time any place of business within the United Kingdom. It was secured by lands and public revenues in Greece. Payment by the principal debtor of principal or interest to residents outside Greece was to be made in sterling and either at the offices of Hambros Bank or Erlangers Ltd. or (at the option of the holder) at the National Bank of Greece in Athens, Greece, by cheque on London. Whichever method of payment was selected, it was pointed out before us that, whatever use were made of the option, discharge of the principal debtor's obligation would have involved in

> the ordinary course either a remittance from Greece to the paying agents specified in the bond or, at the option of the holder, a cheque issued within Greece though drawn on London, and presumably payable there out of funds remitted by the debtors from abroad. It was also pointed out that the bond contained no provision for payment by the guarantor at any particular place or in any particular country. The only circumstances relied on by the Appellants as supporting their contention that the obligation was located inside the United Kingdom were as follows. Although the original guarantor had no branch in the United Kingdom, the present Appellants had acquired one on their universal succession in London. Moreover, it was urged that, since discharge of the obligations under the bond in Greece had been caught by the moratorium enacted by the Greek Government, it followed that the only place at which the obligation could have been discharged or enforced was in London. Speaking for myself, I do not see how an obligation originally situated in Greece for the purposes of British income tax could change its location either by reason of the fact that one guarantor had been substituted for another, or by reason of the fact that the second guarantor so substituted subsequently acquired a London place of business, or by reason of the fact that the Government of Greece had by retrospective legislation altered by moratorium and substitution of a new guarantor for the purposes of Greek law the obligations imposed upon the principal debtor and the guarantor. The Appellants acquired no obligation different from that of the original guarantors, and that was the obligation imposed on the original guarantors by the terms of the bonds. In my view, the bond itself is a foreign document, and the obligations to pay principal and interest to which the bond gives rise were obligations whose source is to be found in this document."

21. The starting point for Mr Way's submissions was that the underlying tax liability at issue is that of the lender and not that of the borrower. It is only if the lender, as a non-UK resident, is liable to tax on the income that a liability to deduct tax arises under s 874 ITA. We agree, and this was not disputed by Mr Vallat. That follows from the approach of Lord Hailsham in the *Greek Bank* case. That approach also took as its starting point the territorial limitation on the taxation of persons not resident in the UK, which depends on the source of the income. The link between the underlying tax liability and the deduction of tax at source has, we observe, been further reinforced by the restriction that has been placed on the liability of a non-UK resident, who does not have a chargeable UK representative, in respect of (amongst others) UK source interest income to the amount of tax deducted at source (ITA, ss 811, 825 (individuals and trustees) and ss 815, 825 (companies)).

22. That principle is plain. No further assistance can be derived from the *Archer-Shee* cases (*Baker v Archer-Shee* [1927] AC 844 and *Archer-Shee v Garland* [1931] AC 212), to which we were referred by Mr Way. Those cases did not concern source, but the question of entitlement to income under a will trust created by a US testator, which turned on the nature of the interest under the trust as ascertained by reference to the foreign law of the trust. In the first of the *Archer-Shee* cases it had wrongly been assumed that the beneficiary had an absolute entitlement to the income of the trust fund; on that basis her husband was held to be taxable on the arising basis. In the

second case, evidence as to the applicable New York law having been obtained to the effect that the beneficiary had no such right, and it being accepted that the interest of the beneficiary was not a right to specific dividends and interest, but a foreign possession consisting of a chose in action against the trustees, it was held that (under the then law) the remittance basis of taxation applied.

23. We agree with Mr Vallat that the *Archer-Shee* cases do not assist in determining the question before us. Unlike the position in those cases, there is no issue in these appeals as to the nature of the creditor's right to the interest. That right is an absolute right. But, unlike in *Archer-Shee*, where the source of the income was clear whichever of the two competing analyses was adopted, the source of the income is the very issue which is in dispute in these appeals. Furthermore, there is no correlation between the position of a trustee, where the question may arise whether a beneficiary is entitled to the underlying income of the trustee or merely an interest in the trust fund, and that of a debtor, where it is self-evident that, absent special provision in the debt instrument, for example in relation to a particular fund, the creditor has no right to the underlying income of the debtor.

24. Nor do we consider that any assistance can be derived from consideration of source in other contexts, such as rental income from land.

25. We turn then to consider the ratio of the *Greek Bank* case, as described by Lord Hailsham. Mr Way's first submission is that this can be found in the final remarks of Lord Hailsham in the quotation we have referred to, that "the bond itself is a foreign document, and the obligations to pay interest to which the bond gives rise were obligations whose source is to be found in this document."

26. As Mr Way pointed out, it had been conceded for National Bank of Greece that if the claim had been against the principal debtor in respect of interest under the terms of the bond, the source of the income would have been foreign. The rights of the bondholder would have been against the bank not resident in the UK. The Bank's argument was that both the character and source of the income had changed when the only recourse that remained to a bondholder was to a guarantor with a branch and premises in the UK (see [1971] AC 943, at pp 952-953).

27. Mr Way submitted that the proper approach was therefore to step back and ask the question whether the loan document was fundamentally a UK document or a foreign document. Factors to be taken into account would include the place from which credit had been provided, the jurisdiction in which disputes could be heard and the location of any security provided under the terms of the loan.

28. The difficulty with Mr Way's argument is that, although it seeks to focus on a single criterion identified from the speech of Lord Hailsham, that of the nationality of the document, it is a criterion that must itself be determined by reference to other criteria. The nationality of a document cannot be identified save from the relevant circumstances of the document. That necessarily resolves itself into a multi-factorial question. The question then is what are the material factors and what weight should be given to each of them. Indeed, Mr Way's own argument was to this effect,

referring to the summary which Lord Hailsham had given, and which we have recited, as to the key features of the obligation, as explaining why it was that the bond was held to represent a foreign-source obligation.

29. We do not consider that the ratio of the *Greek Bank* case can be distilled into an enquiry into the nationality or residence of the debt instrument. We agree with Mr Vallat that at this point in his speech Lord Hailsham was rejecting the argument for the National Bank that the source of the obligation had, in the events that had happened, become the substituted guarantee. Lord Hailsham was emphasising that the source had not changed. The substitute guarantor had acquired no obligation different from that imposed on the original guarantor by the terms of the bonds. That, in our judgment is the sole significance of Lord Hailsham's reference to the bond being a foreign document and the source of the obligations being found in that document. Lord Hailsham's speech is, in our view, to be understood as saying, not that it is the nationality of the loan instrument that falls to be ascertained by reference to all relevant factors, but that it is the source of the obligation that must be so ascertained.

30. We are clear therefore that the ratio of the *Greek Bank* case, which is binding on us, is that the source of the obligation must be ascertained by a multi-factorial enquiry. In view of the binding nature of that authority, it is not open to us to find that, as a matter of law, the source of the interest is to be found by reference to the single factor of the place where the credit was provided.

31. Mr Way's submissions in that respect proceeded from his starting point of *Colquhoun v Brooks* and the territorial limitation on the liability to UK tax of a lender who is not resident in the UK. He argued that any tax deducted at source would be by reference to the lender's activities, and that accordingly the correct question should be: where does the lender's activity take place, or where does the lender make its profit? If, submitted Mr Way, there was no activity of the lender in the UK, then the proper conclusion should be that the source of the interest has no UK nexus.

32. Those submissions must be rejected. They are contrary to the ratio of the *Greek Bank* case, which itself proceeded from the same starting point of the territorial limitation on taxation of the lender or creditor, in that case the holders of the bonds. Although Mr Way sought to argue that the true source of the interest is the provision of the credit, because absent the credit there would be no interest, that was not the approach in the *Greek Bank* case, which looked at the proximate source of the interest, namely the debt obligation. That, after all, is the asset from which the creditor derives the interest. Furthermore, as appears from the judgment of Karminski LJ in the *Greek Bank* case in the Court of Appeal, 46 TC, at p 489, the loan in that case was raised in London. If the proper test was to ascertain where the credit was provided, the *Greek Bank* case could not have been decided in the way it was.

33. It is not, in these circumstances, necessary for us to consider in detail the Privy Council and Commonwealth authorities which Mr Way sought to rely upon in support of his argument in this respect. The circumstances in which the source issue arose in

those cases is described by the FTT in *Ardmore*, and we need not repeat what was said there. We have only the following general observations.

34. The first is that, whatever the result of the cases concerned, it is evident that the courts did not consider that a single test could be applied in all cases. Indeed, that very observation was made by Lord Nolan in the Privy Council in *Commissioner of Inland Revenue v Orion Caribbean Limited (in voluntary liquidation)* [1997] STC 923, a case concerning Hong Kong profits tax, when he said, at p 931, that the ascertainment of the actual source of income is a "practical hard matter of fact" and that "No simple, single, legal test can be employed". The test is accordingly, on any view, a multi-factorial one.

35. Secondly, it is clear from *Orion* that, in the case of a simple debt, there is no authority for a test which focuses on the place where the creditor's activities take place in providing the credit. In *Commissioner of Inland Revenue v Hang Seng Bank Limited* [1990] STC 733, at p 740, Lord Bridge had sought to contrast the position of the provision of a service or activity from which profit has been derived with profit earned by the exploitation of assets, such as lending money, remarking that in the latter such case "the profit will have arisen in or derived from the place where … the money was lent". In *Orion*, this was applied by the courts in Hong Kong to find that, where gross income was interest on a loan, the source of the income was located as a matter of law in the place where the money was advanced. That finding was, however, not accepted by the Privy Council.

36. In explaining that the remarks of Lord Bridge in *Hang Seng Bank* could not be regarded as laying down a rule of law, or as having the broad meaning as advanced by the putative taxpayer, Lord Nolan gave, in *Orion* at p 930, as an example, a simple loan by a Hong Kong corporation to a borrower in New York, remarking that there might be little difficulty in saying that the location of the source of the interest was New York. In such a case, however, there was no question of the source of the interest being determined by the place, Hong Kong, from which the creditor had undertaken the lending activity. By contrast, in a case such as *Orion* itself, where the activity constituted borrowing and on-lending for profit, and those activities had been carried on in Hong Kong by the Hong Kong corporation on behalf of its Cayman Islands subsidiary, it was that activity which constituted the source of the income, and the source was accordingly a Hong Kong source. *Orion* does not therefore support Mr Way's argument. In the case of a simple debt, it points in the opposite direction towards the place of the borrower.

37. The same pointer can be found in *Commissioner of Taxation v Spotless Services Ltd and another* (1995) 62 FCR 244, an Australian case principally notable for its analysis of a general anti-avoidance provision under the Australian tax code. A prior question, however, concerned the source of income on certain certificates of deposit issued to Australian residents in the Cook Islands by a Cook Islands company, and subsequently repaid, with interest less Cook Islands withholding tax, from the Cook Islands. The essence of the scheme was to produce income which was exempt because its source was in the Cook Islands, and consequently not in Australia.

38. In these circumstances, therefore, the debtor was the Cook Islands company, and the creditor the Australian resident. The argument of the Commissioner was that the relevant investment contract had been made in Australia when, as a pre-cursor to the transfer of monies to the Cook Islands company, the creditor companies had handed over the amount of the investment to a bank, with which the companies had accounts in Singapore, in exchange for an irrevocable letter of credit, which was a guarantee of the certificate of deposit. This argument was rejected, both at first instance and on appeal. The relevant factors were the residence and place of business of the borrower/debtor, the place from which the deposit and interest were repaid, and the legal effect of the arrangements between the parties, under which the relevant contract was not that for the letter of credit, but that for the certificate of deposit on which the creditor could have sued and would have been entitled to judgment. Considerable weight was given to the place where the contract was made and where the money was lent (the Cook Islands). The place of activity of the Australian lender/creditor was not a relevant factor.

39. Thirdly, care must be taken in seeking to translate findings which are findings of fact, and are made in the context of laws of a different jurisdiction, to the domestic context in which findings fall to be made in these cases. A number of the cases to which Mr Way referred us, including *Orion* and *Hang Seng Bank*, but also *Studebaker Corporation of Australasia Limited v Commissioner of Taxation of New South Wales* (1921) 29 CLR 225 and *Commissioner of Inland Revenue v NV Philips Gloeilampenfabrieken* [1955] NZLR 868, whilst emanating variously from Hong Kong, Australia and New Zealand, all featured, as part of the relevant facts, trading or business activities. Where the source of trading or business activity must be ascertained, an analysis as a practical hard matter of fact may give rise to a different result from the case of a simple debt.

40. Finally, it is of the nature of these cases, where no single legal test can be determinative, that different factual circumstances may give rise to different results. One such case is *Commissioner for Inland Revenue v Lever Bros and another* [1946] AD 41, a judgment of the South African appeals court. There, on the particular facts concerning the assumption by a South African company of an existing interest-bearing debt, created on a sale of certain shares and debts by a UK company to a Dutch company, the Court held that the interest on the assumed debt was not income from a South African source. The only connection that the debt had with South Africa was the residence of the substitute debtor.

41. The South African court rejected the argument that since the debt was regarded in law as located where the debtor resided, the source of the interest was South Africa. That is another example of the courts eschewing the approach of seeking to apply a single legal test. The conclusion reached in *Lever Bros* is unexceptional on its facts, which included that the South African Treasury had consented to the transaction only on the express condition that no capital or interest should be paid from any funds in South Africa. The absence of connection of the original debt with South Africa would, it seems to us, have enabled such a conclusion to have been reached on a multi-factorial assessment. The finding, in such a case, that it is not the debt that is the source of the interest, but the activities of the creditor which earned the income,

cannot be regarded as a finding of principle, applicable to all cases. Any argument that it were such would be bound to fail, in a UK context, as it would be contrary to the binding authority of the *Greek Bank* case. The South African court, in rejecting one argument that there was a legal rule determining source, was not attempting to substitute another such rule.

The multi-factorial test

42. It is not possible to distil the multi-factorial test into a convenient set of relevant factors. Even the *Greek Bank* case cannot be regarded as exhaustive of the factors that might, in particular circumstances, be relevant to the question of source.

43. It is nonetheless possible to discern from the *Greek Bank* case certain factors which were, in the circumstances of that case, considered to be relevant, and those which were not. Chief amongst these, in our judgment, is that it is, in normal cases of a simple loan, the debt which will be the source of the interest, and not any underlying activity of the creditor. That may not hold good in particular circumstances, for example where a debt arises in the course of a trade, where the trade might be regarded as the source, or in special circumstances, such as those which arose on the *Lever Bros* case, but where the case is one of a simple loan, the asset of the creditor, on which the interest arises, is the debt, and it is that debt which will be the source.

44. That was the focus of Lord Hailsham in *Greek Bank*, with whom all the other law lords concurred. Lord Hailsham was concerned with ascertaining the "source of the obligation", that is the obligation of the debtor to pay interest. Relevant factors were the residence of the debtor and the original guarantor, the location of the security originally provided, and the ultimate, or substantive, source of discharge of the debtor's obligation.

45. Factors which were either not referred to by Lord Hailsham (and which accordingly must have carried little or no weight in the circumstances) or which were known facts but did not outweigh the factors referred to by Lord Hailsham included the following:

(a) The residence of the creditor or the place of activity of the creditor.

(b) The place where credit was advanced. The original borrowing was raised in London, but that did not weigh in favour of the UK as the source.

(c) The place of payment of the interest. Under the original bonds, the place of payment was London (either by presentation to a London bank or, if presented to the original borrower in Greece, by cheque on London). This factor was rejected in favour of the ultimate source of the principal debtor's obligation, which would have involved a remittance from Greece.

(d) The fact that a moratorium has been placed on a creditor's right to sue and enforce rights of security against the debtor.

(e) The jurisdiction in which proceedings might be brought to enforce the interest obligation. In the *Greek Bank* case, it had been held that the English courts would have jurisdiction.

(f) The proper law of the contract. In *Greek Bank*, the proper law was English law.

(g) The place of business of a substitute guarantor.

46. In addition, it was accepted before us, and we consider rightly, that the legal *situs* of the debt is not a relevant factor for income tax purposes. Thus, the fact that the *situs* of a simple debt is where the debtor resides is not a factor independent of the residence of the debtor itself. That is clear from the facts of the *Greek Bank* case, where the bonds were bearer instruments, the *situs* of which would be where the bonds themselves were physically located, and the coupons for interest payment would have been required to have been detached and presented for payment in London.

47. It would follow from this that the *situs* of a specialty debt would likewise also be of no relevance. The distinction between the *situs* of a simple debt and that of a specialty debt was one of the principal reasons why the New Zealand courts in *Philips* rejected the proposition that source should be determined according to *situs*. Although *situs* is relevant in connection with certain taxes, such as stamp duty as exemplified by *English Scottish and Australian Bank v Commissioners of Inland Revenue* [1932] AC 238, it is not appropriate for source for income tax purposes to depend on whether the debt instrument is a simple contract or by deed.

48. We note, for completeness, although it is not material to our determination, that with effect in relation to any payment of interest made on or after 17 July 2013, s 874(6A) ITA provides that in determining for the purposes of s 874(1) whether a payment of interest arises in the UK, no account is to be taken of the location of any deed which records the obligation to pay the interest. Thus, the irrelevance, in relation to deduction of tax at source, of the *situs* of a specialty debt has now been confirmed by statute.

49. That the residence of the debtor is a material factor is clear from the *Greek Bank* case. There is, however, a question as to the weight which should be placed on that factor.

50. The published position of HMRC can be seen from paragraph 9090 of their Savings and Income Manual (SAIM). Under the heading Yearly Interest: UK Source: The General Rule, and after referring to the *Greek Bank* case and to their view that the most important factor in deciding whether UK interest has a UK source is the residence of the debtor and the location of the debtor's assets, HMRC say:

> "HMRC consider the residence of the debtor to be most important because this, along with the location of the debtor's assets, will influence where the creditor will sue for payment of the interest and repayment of the loan. 'Residence' in these circumstances is not the

> same as tax residence. Residence of the debtor is residence for the purposes of jurisdiction."

51. This perceived rationale for the use of the residence of the debtor as a material factor led Mr Way to submit that residence would cease to be a factor if it were the case that there was an overriding jurisdiction clause in the debt instrument. The relevant factor would then simply be the place where the parties had chosen as the jurisdiction for disputes.

52. We do not accept that submission. There is no support within the *Greek Bank* case for a link between jurisdiction and residence. Lord Hailsham referred to the Greek residence of the debtor as a material factor even though the governing law of the bonds had been held to be English law, and the English courts had jurisdiction. That was not something that Lord Hailsham regarded as material so as to affect the foreign source of the obligation. What this shows, in our judgment, is that the residence of the debtor is a factor regardless of whether that place of residence is the jurisdiction in which the parties may bring proceedings.

53. Residence is, on the other hand, only one factor, and it cannot be elevated into the most important factor, whether alone or when combined with the question of the location of the debtor's assets. The *Greek Bank* case did not determine any hierarchy of materiality or weight, and none can be inferred. The question is simply a multi-factorial one, having regard to all the circumstances and all the relevant factors.

Application of the multi-factorial test

54. We turn then to consider the application of the multi-factorial test to the facts of the cases before us. Those facts are set out in the respective FTT decisions, and we do not need to make extensive reference to them. We shall confine our consideration only to the material facts.

Perrin

55. Mr Perrin is resident and domiciled in the UK. He is the managing director of a UK resident company, Hemisphere Freight Services Limited ("Hemisphere"), which in 2009 made contributions to an Employer-Financed Retirement Benefits Scheme ("EFRBS1"). EFRBS1 transferred funds to another EFRBS ("EFRBS2"), whose trustee was an Isle of Man company. Mr Perrin was the principal beneficiary of EFRBS2.

56. A number of loans were made by EFRBS2 to Mr Perrin. All were in similar terms, and we can confine ourselves to the first such loan, and the loan agreement in that regard between the trustee and Mr Perrin, whereby EFRBS2 lent Mr Perrin £198,000, payment of which was made from the trust's Isle of Man bank account to the Isle of Man bank account of Mr Perrin.

57. The FTT, at [9] and [10], summarised the terms of the loan agreement as follows:

> "9. The loan was not guaranteed by anyone.
>
> 10. The loan agreement provided:
>
> (1) that the loan was to be unsecured;
>
> (2) interest was payable at 4.75% annually in arrears
>
> (3) that repayment should be made on 4 November 2014, the day before the fifth anniversary of the making of the loan;
>
> (4) that repayment (or prepayments) should be made to a bank account specified. Unfortunately the details of the bank account were not specified in the agreement;
>
> (5) that no variation of the agreement would be effective unless in writing and signed;
>
> (6) that the agreement would be "governed by and construed in accordance with the laws of the Isle of Man" (clause 10.1); and
>
> (7) that the parties "irrevocably submit to the jurisdiction of the Courts of the Isle of Man for the settlement of all disputes or claims" in connection with the agreement (clause 10.2)."

58. In total, EFRBS2 lent Mr Perrin some £650,000. Of that, Mr Perrin lent the most part to Hemisphere interest-free, but he also invested about £150,000 in stocks and shares and retained about £81,000 in his Isle of Man bank account. From this Mr Perrin made two interest payments, but the FTT concluded, at [12], that up to the repayment date of the loan (4 November 2014), interest for certain periods would have to have been funded from accounts other than the Isle of Man.

59. The FTT also found, at [15], that if the trustee had sought to enforce the payment of interest or capital (principal), having obtained judgment in the Isle of Man, the principal place of enforcement would have been England.

60. The FTT took the view, at [71], that the following factors were relevant:

> "(1) The proper law of the agreement. This was that of the Isle of Man. This factor however I judge to be of very little weight.
>
> (2) The place in which payment was actually made, namely, for the two payments at issue, the Isle of Man. I regard this as of little weight.
>
> (3) The jurisdiction in which judgement could be obtained, namely the Isle of Man.
>
> (4) The country in which Mr Perrin was resident, namely the UK.
>
> (5) The country from or in which Mr Perrin's obligations to pay would be contemplated to be enforced or would substantively originate, namely the UK."

61. The FTT concluded, at [72], that the interest arose in the UK and did not arise from a source outside the UK. It found that the factors of residence and the source of funds for payment or enforcement outweighed that of jurisdiction and actual payment. As regards the actual payments made by Mr Perrin from his Isle of Man bank account, this factor was discounted by the FTT on the basis that what was required by the

Greek Bank case to be ascertained was the source of the obligation and that this was the totality of the loan obligations and not simply the source of payment of the interest.

62. The jurisdiction of this Tribunal is limited to points of law arising out of a decision, other than an excluded decision (which is not relevant here) made by the FTT (s 11 of the Tribunals, Courts and Enforcement Act 2007 ("TCEA")). It is well-established, in this regard, that an appeal court should be slow to interfere with a multi-factorial assessment based on a number of primary facts, or a value judgment. Where the application of a legal standard involves no question of principle, but is simply a matter of degree, an appellate court should be very cautious in differing from the judge's evaluation. Where a decision involves the application of a not altogether precise legal standard to a combination of features of varying importance, this will fall within the class of case in which an appellate court should not reverse a judge's decision unless he has erred in principle (*Procter & Gamble UK v Revenue and Customs Commissioners* [2009] STC 1990 at [9]–[10] per Jacobs LJ; *Designers Guild Ltd v Russell Williams (Textiles) Ltd* [2001] 1 All ER 700 at 707, [2000] 1 WLR 2416 at 2423 per Lord Hoffmann).

63. Those principles have recently been considered in the Supreme Court by Lord Carnwath in *Revenue and Customs Commissioners v Pendragon plc and others* [2015] UKSC 37. That case concerned "abuse of law" within the sphere of VAT, but the concept of source of income could equally be described using the words of Lord Carnwath, at [50], as "a general principle of central importance" in its own context.

64. What Lord Carnwath emphasised in *Pendragon* was the need for such concepts to be given detailed consideration by the Upper Tribunal, with a view, where relevant, to giving detailed guidance for future cases. But it is only if, having done so, the Tribunal finds errors in the approach of the FTT that it may go on to re-make the decision (using its power to do so under s 12 TCEA) and make factual and legal judgments as necessary in that regard.

65. The question for us is whether we find any error in the approach of the FTT in *Perrin*. We can identify no material error. In our judgment, the FTT was correct to adopt a multi-factorial approach. In applying that approach, of the features which the FTT found to be of little weight, we agree that the proper law of the agreement and the jurisdiction in which judgment could be obtained, along with the place where payment was made (as opposed to the true and substantive source of the payments), are factors of limited, if any, weight, having regard to their lack of significance in the conclusions reached in the *Greek Bank* case.

66. We consider, for the reasons we have set out above, that the FTT was correct to have given weight to the residence of the debtor, Mr Perrin, and to the source of funds for payment and enforcement. We have found that, as a matter of principle and authority, the place where the credit was provided to Mr Perrin is not a relevant factor, and we reject therefore Mr Way's submission that the place where the money was lent should be regarded as the "commercial source" and that the FTT should have

given weight to the fact that the loan was made to Mr Perrin by means of a transfer from the Isle of Man bank account of EFRBS2 to Mr Perrin's Isle of Man account.

67. Nor do we consider that, as submitted by Mr Way, weight should have been given to the place of receipt of the interest (which was the Isle of Man), or the fact that certain interest payments were made out of Mr Perrin's Isle of Man bank account. The place at which payments are received cannot be relevant to a question of source, and the place from which payments are made is of little or no significance, as the *Greek Bank* case illustrates, compared to the substantive or ultimate source of payment in respect of the obligations associated with the debt. The absence of security over UK assets, although relied upon by Mr Way, is a neutral factor. There was no security over any assets, whether in the UK, Isle of Man or elsewhere, and this could not therefore be a relevant factor. In summary, therefore, the FTT was, in our view, fully entitled on the evidence to find that the substantive source in Mr Perrin's case was in the UK.

68. Mr Perrin's appeal must accordingly be dismissed.

Ardmore

69. The facts relating to Ardmore's case were set out in an extensive statement of agreed facts which the FTT reproduced at [4] of its decision. We can confine ourselves to a few material features.

70. Ardmore is a UK incorporated and tax-resident company, owned by two brothers, Mr Cormac Byrne and Mr Patrick Byrne. Each of the Messrs Byrne established trusts, governed by Gibraltar law, the trustee of which was a Gibraltar incorporated and tax-resident company. Each of the trusts was resident in Gibraltar for tax purposes.

71. Each of the trusts acquired the whole of the ordinary share capital of a company incorporated in the British Virgin Islands, but with its administrative office in Gibraltar. Two of the directors were Gibraltar residents; the third was a resident of Spain. The trust for Mr Cormac Byrne acquired Zeus Developments Limited ("Zeus") and that for Mr Patrick Byrne acquired Halmyre Services Limited ("Halmyre").

72. Ardmore subscribed for one A Redeemable Share in each of Zeus and Halmyre at a subscription price of £4m, of which £1,000 was paid up on issue. The A Redeemable Shares became Deferred Shares under their terms of issue, as a result of which the right to repayment of capital on a winding-up or dissolution was restricted to the nominal value of the share (1p each).

73. Shortly afterwards, Ardmore paid £1.35m to each of Zeus and Halmyre in part payment of the outstanding premium on the Deferred Shares. Subsequently, on 16 June 2005, at the request of the Messrs Byrne, each of their respective trusts entered into facility agreements with Ardmore in respect of loans of £1.35m by the trusts to

Ardmore. Those loans, which had been funded by payments made by the Zeus and Halmyre to the respective trusts, were drawn down by Ardmore on 20 June 2005.

74. Further similar facility agreements were entered into between Ardmore and the trusts on 5 July 2005 and 29 July 2005, in consequence of which each trust lent to Ardmore £1.35m on 12 July 2005 and £1.3m on 2 August 2005.

75. Following a further subscription by Ardmore for A Redeemable Shares in each of Zeus and Halmyre, and conversion of those shares into Deferred Shares, as a result of which the outstanding premium due from Ardmore to each company amounted to £1,594,474, on 22 May 2007 Ardmore and each of Zeus and Halmyre entered into loan agreements for loans of £1,594,474 from the companies to Ardmore to be offset against the unpaid premiums.

76. Subsequently, although not of relevance to this appeal, agreements were entered into between Ardmore and the trusts and BVI companies varying the terms of the facility and loan agreements so as to enable Ardmore to pre-pay interest on the loans.

77. The FTT recorded, at [4](19), the main terms of the June 2005 facility agreements (those between Ardmore and the trusts) as follows:

> "(a) Each loan was for £1,350,000.
>
> (b) The loan was stated to be for general business purposes.
>
> (c) After the first 12 months, the loan was repayable on 30 days' notice but repayment by Ardmore could be made at any time on 7 days' notice.
>
> (d) The loan bore interest at 2% above the base rate of the Bank of England, compounded yearly.
>
> (e) Interest was payable on receipt of a written demand from the lender, but Ardmore was permitted at any time to pay interest already accrued. On repayment of the loan all accrued interest became immediately repayable.
>
> (f) The Agreements provided: "All payments under this Facility are to be made in Gibraltar to the account of the Lender at Nat West Offshore Ltd or other such bank in Gibraltar as notified to the Borrower in writing from time to time and all such payments including without limitation payments of interest shall be made from a source outside the United Kingdom."
>
> (g) By contractual choice of law and jurisdiction clause, each Agreement was governed by the laws of Gibraltar and the parties submitted to the exclusive jurisdiction of the Gibraltar Courts."

78. In addition, it was recorded at [4](21) that the facility agreements provided that: "This facility shall not be supported by any form of security over assets in the United Kingdom", and that none of the loans concerned in the appeal were secured loans.

79. The June 2005 facility agreements were representative of the terms of the other facility agreements entered into between Ardmore and the trusts. The terms of the

May 2007 loan agreements between Ardmore and the BVI companies were also similar to those of the June 2005 agreements save for the differences noted at [4](44):

> "(a) The interest rate was 1.5% above the Bank of England base rate;
>
> (b) There was no reference to the loan being made for any particular purpose;
>
> (c) Each loan was repayable within 30 days of receipt by Ardmore of a written demand from the Lender (the relevant BVI company), and Ardmore was not permitted to prepay the loan within the period of 365 days after the date when the loan was advanced to it; and
>
> (d) The advance to Ardmore was to be satisfied by way of offset against the outstanding sum due from Ardmore under the November 2005 share subscriptions."

80. Despite the provision, in both the facility agreements with the trusts and the loan agreements with the BVI companies, to the effect that payments of interest were only to be made from a source outside the UK, in every case such payments were made from Ardmore's bank account in the UK, funded from the income of Ardmore's UK trading activities.

81. Apart from a peripheral issue concerning the propriety of the citation of unpublished decisions of the former special commissioners, with which we are not concerned in these appeals, the FTT in *Ardmore* focused on the question of the nature of the test to be applied in determining the location of the source of interest. It was argued for Ardmore, as before us, that the multi-factorial approach was wrong, and that the source of interest is located in that place where credit is provided.

82. The FTT rejected that argument, finding in favour of the multi-factorial approach. In accordance with our own analysis we consider it was right to do so. No error of law can be found in the FTT's decision in this respect.

83. The consequence for Ardmore of the FTT's conclusion on the question of principle was that the appeal failed. As the FTT said, at [43], it had been accepted by Ardmore that if a multi-factorial approach were to be adopted, Ardmore's appeal could not succeed.

84. That raises the question whether at this stage it is open to Ardmore to argue that the FTT made an error of law in dismissing Ardmore's appeal on that basis. Mr Vallat submitted that, if we were to find – as we have – that the multi-factorial approach was the proper one to take, there would be no basis for us to interfere with the FTT's conclusion. In particular, in the absence of an error of law, there would be no basis for this Tribunal to revisit the facts under s 12 TCEA.

85. The concession made on behalf of Ardmore before the FTT, which Mr Way submitted had been wrongly made, means that permission of this Tribunal is required before the concession may be withdrawn. The principles to be applied are those set out by Peter Gibson LJ in *Jones v MBNA International Bank* [2000] EWCA Civ 514, at [38]:

> "It is not in dispute that to withdraw a concession or take a point not argued in the lower court requires the leave of this court. In general the court expects each party to advance his whole case at the trial. In the interests of fairness to the other party this court should be slow to allow new points, which were available to be taken at the trial but were not taken, to be advanced for the first time in this court. That consideration is the weightier if further evidence might have been adduced at the trial, had the point been taken then, or if the decision on the point requires an evaluation of all the evidence and could be affected by the impression which the trial judge receives from seeing and hearing the witnesses. Indeed it is hard to see how, if those circumstances obtained, this court, having regard to the overriding objective of dealing with cases justly, could allow that new point to be taken."

86. In considering whether to give permission, we have taken into account the fact that all the relevant facts were agreed and that accordingly no further factual enquiry is necessary, that although the FTT noted the concession at [43] of its decision it had already, at [42], applied the multi-factorial approach and found that the interest had arisen in the UK, that this ground was included in Ardmore's application for permission to appeal to the FTT and notice of appeal to this Tribunal and that its admission was not disputed in HMRC's response to the notice of appeal. In light of those factors, we consider that we should permit Ardmore to withdraw the concession made before the FTT. We proceed, accordingly, to consider the application of the multi-factorial approach in Ardmore's case.

87. At [42], the FTT set out its conclusions on application of the multi-factorial test. It referred in particular to the fact that Ardmore was resident in the UK and to the fact that, although it recognised that it was not determinative, the *situs* of the debt was located where Ardmore was resident. It also found that the UK, as well as being the source or origin of the funds for payment, would be the place of enforcement of the debt.

88. As we have noted earlier, the parties agree that *situs* is not a relevant factor. Apart from that, the question is whether, in its application of the multi-factorial test, the FTT made any error of law.

89. Mr Way sought to persuade us that the application of the multi-factorial approach led to a different result from that found by the FTT. He pointed to the place of credit, which he argued was in Gibraltar, the exclusive jurisdiction afforded to the courts of Gibraltar and the absence of UK security. He argued that greater weight should be afforded to place of credit and place of jurisdiction.

90. We do not accept those submissions. They do not accord with the law as authoritatively established in the *Greek Bank* case, as we have described. The FTT was right to give weight to the residence of the debtor, Ardmore, which was in the UK. It was right to have regard to the substantive, and in this case actual, source of the payments, which derived from Ardmore's UK trading activities. For the reasons we have described, we agree with Mr Vallat that the residence of the lender and the place from which the money was lent (the place of credit) are not relevant.

Jurisdiction and the proper law of the contract are factors of little or no weight having regard to *Greek Bank*. The absence of security is a neutral factor; the fact that the agreements specified that there should be no UK security is immaterial.

91. We find, accordingly, that the FTT made no error of law in finding that the correct approach was the multi-factorial approach, or in its application of that approach to the facts. The FTT was fully entitled on the evidence to find that the interest in question arose in the UK.

92. Ardmore's appeal is accordingly dismissed.

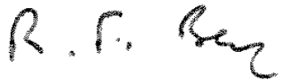
Decision

93. For the reasons we have given we dismiss both Mr Perrin's and Ardmore's appeals.

Costs

94. Any application for costs should be made not later than 14 days after the date of release of this decision. As any order will be for detailed assessment, if costs are not agreed, it will not be necessary for the application to be accompanied by a schedule of costs.

MR JUSTICE MORGAN



UPPER TRIBUNAL JUDGE ROGER BERNER

RELEASE DATE: 20 November 2015