CORPORATION TAX – whether interest paid by a UK resident company out of assets situated in the United Kingdom under a debt which, if enforced, would be enforced against assets situated in the United Kingdom had a UK source regardless of where the credit giving rise to the debt was extended and notwithstanding provisions in the loan agreement requiring the interest to be paid outside the United Kingdom, specifying that the governing law was to be that of a jurisdiction outside the United Kingdom and specifying that that non-UK jurisdiction was to be the exclusive jurisdiction for enforcement – yes – whether interest on short-term loans which were repaid within a year out of the proceeds of new loans from the same lenders in circumstances where, on the balance of probabilities, the series of loans were intended to provide long-term funding for the borrower was yearly in nature – yes – whether the Appellant could rely on the "industrial or commercial profits" paragraph in the UK/Guernsey double tax treaty to make interest payments to a Guernsey resident company without withholding – no – whether the Appellant could rely on the exemption from withholding tax for interest to which a UK resident company was beneficially entitled when the recipient acquired the interest only just before the interest payment was made and did so for no purpose other than availing itself of the exemption – except to the (de minimis) extent that an interest payment received exceeded the amount paid for the right to receive that interest payment, no– IRC v McGuckian applied

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2019/04625

BETWEEN

HARGREAVES PROPERTY HOLDINGS LIMITED **Appellant**

-and-

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

TRIBUNAL: JUDGE TONY BEARE

The hearing took place on 5, 6, 11 and 12 October 2021. The form of the hearing was V (video) on Teams. A face-to-face hearing was not held because of the COVID pandemic. The documents to which I was referred were a documents bundle of 2,964 pages (the "DB") and an authorities bundle of 873 pages.

Prior notice of the hearing had been published on the gov.uk website, with information about how representatives of the media or members of the public could apply to join the hearing remotely in order to observe the proceedings. As such, the hearing was held in public.

Mr Patrick Way QC and Ms Dilpreet Dhanoa, counsel, instructed by BDO LLP, for the Appellant

Mr Richard Vallat QC and Ms Calypso Blaj, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

INTRODUCTION

1. This decision relates to assessments to income tax made by the Respondents in respect of interest which was paid by the Appellant over the period between October 2010 and March 2015. The Respondents submit that the Appellant should have withheld income tax when paying that interest and accounted for the income tax to the Respondents. The Appellant submits that no such obligation arose.

2. I will explain in due course how that difference of view has arisen but, in the first instance, I should say that the aggregate amount of tax in dispute is £2,794,829.60, made up as follows:

Return period start date	Return period end date	Interest paid (£)	Tax assessed (£)
1 October 2010	24 December 2010	2,455,066.00	491,013.20
1 October 2011	24 December 2011	705,000.00	141,000.00
1 January 2012	31 March 2012	420,000.00	84,000.00
1 October 2012	24 December 2012	755,772.00	151,154.40
1 January 2013	31 March 2013	5,126,309.00	1,025,261.80
1 January 2014	31 March 2014	1,514,682.00	302,936.40
1 January 2015	31 March 2015	2,997,319.00	599,463.80

3. The figures of £705,000.00 and £141,000.00 set out in relation to the second return period mentioned above are estimates, based on the Respondents' best judgment.

4. In terms of the process leading to the present decision:

(1) the Appellant appealed against each assessment shortly after it was raised;

(2) on 3 August 2018, the Appellant accepted the Respondents' offer of a review;

(3) on 12 June 2019, the Respondents' review officer upheld the assessments; and

(4) on 4 July 2019, the Appellant notified the First-tier Tribunal of its appeal against the assessments.

THE LEGISLATION

The obligation to withhold

5. Before outlining the background and facts which are relevant to, and the issues which are at stake in, this appeal, I should set out the relevant provisions of the legislation. They are contained in Chapters 3, 11 and 15 of Part 15 of the Income Tax Act 2007 (the "ITA") and are as follows.

6. Sections 874(1) and 874(2) of the ITA provide that, if a payment of "yearly" interest arising in the United Kingdom is made by a company, then the company, or the person 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.

7. Section 874(6) of the ITA provides that the obligation does not apply where the company is making the payment in a fiduciary or representative capacity and Section 874(3) of the ITA refers to provisions elsewhere in the ITA in which the obligation is disapplied.

8. Chapter 15 of Part 15 of the ITA sets out the machinery whereby a company is required to account to the Respondents for the income tax it withholds. Broadly, a company with

accounting periods is required to file returns and account for the tax on a quarterly basis, with the relevant return and the tax in question due within 14 days of the end of the quarter.

Exclusion for interest to which a UK resident company is beneficially entitled

9. One of the circumstances in which the obligation to withhold is disapplied as mentioned in paragraph 7 above is where "the person beneficially entitled to the income in respect of which the payment is made is a UK resident company" (see Section 933 of the ITA).

Double tax relief

10. Article 3(2) of the Agreement between His Majesty's Government and the States of Guernsey for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income, which came into force on 24 June 1952 and was in force throughout the period to which the assessments relate (the "Guernsey Treaty") provided as follows:

"(2) The industrial or commercial profits of a Guernsey enterprise shall not be subject to United Kingdom tax unless the enterprise is engaged in trade or business in the United Kingdom through a permanent establishment situated therein. If it is so engaged, tax may be imposed on those profits by the United Kingdom, but only on so much of them as is attributable to that permanent establishment."

11. The Guernsey Treaty became part of UK domestic law pursuant to the terms of a statutory instrument (The Double Taxation Relief (Taxes on Income) (Guernsey) Order 1952 (SI 1952/1215)), which was enacted pursuant to the predecessor of what is now Section 6 of the Taxation (International and Other Provisions) Act 2010 (the "TIOPA"). The relevant parts of Section 6 of the TIOPA stated as follows during the period which is relevant to this appeal:

"6 The effect given by section 2 to double taxation arrangements

(1) Subject to this Part and Part 18 of ICTA, double taxation arrangements have effect in accordance with subsections (2) to (4) despite anything in any enactment.

(2) Double taxation arrangements have effect in relation to income tax and corporation tax so far as the arrangements provide—

(a) for relief from income tax or corporation tax,

(b) for taxing income of non-UK resident persons that arises from sources in the United Kingdom,

(c) for taxing chargeable gains accruing to non-UK resident persons on the disposal of assets in the United Kingdom,

(d) for determining the income or chargeable gains to be attributed to non-UK resident persons,

(e) for determining the income or chargeable gains to be attributed to agencies, branches or establishments in the United Kingdom of non-UK resident persons,

….

(6) Relief under subsection (2)(a) … requires a claim."

12. Finally in relation to the relevant legislation, I should mention The Double Taxation Relief (Taxes on Income) (General) Regulations 1970 (SI 1970/488) which were enacted pursuant to what is now Section 7 of the TIOPA (the "DTR Regulations"). The following provisions of the DTR Regulations are of some relevance to this appeal:

"2(1) The following provisions of these Regulations shall have effect where, under arrangements having effect under section 497 of the Income and Corporation Taxes Act 1970 [now Section 6 of the TIOPA], persons resident in the territory with the Government of which the arrangements are made are entitled to exemption or partial relief from United Kingdom income tax in respect of any income from which deduction of tax is authorised or required by the Income Tax Acts.

(2) Any person who pays any such income (referred to in these Regulations as "the United Kingdom payer") to a person in the said territory who is beneficially entitled to the income (such person being referred to in these Regulations as "the non-resident") may be directed by a notice in writing given by or on behalf of the Board that in paying any such income specified in the notice to the treaty resident he shall…not deduct tax…and where such notice is given, any income to which the notice refers, being income for a year for which the arrangements have effect, which the United Kingdom payer pays after the date of the notice to the non-resident named therein shall, subject to the following provisions of these Regulations, be paid as directed in the notice:….

5. The United Kingdom payer shall not, in respect of any payment, be charged with or liable to account for any tax which, but for a notice given under Regulation 2(2), he would have been required by the Income Tax Acts to deduct and account for on making the payment but in compliance with the notice has not deducted.

6. Where in compliance with a notice given under Regulation 2(2) a company makes the payment without deducting tax which, but for the notice, it would have been required to deduct in accordance with section 53 or 54 of the Income and Corporation Taxes Act 1970, the payment shall be treated for the purposes of section 248(4) of that Act (which prohibits certain payments from being treated as charges on income for corporation tax) as if the company had deducted that tax in accordance with the said section 53 or 54 and had accounted for it under Part XI of that Act….

8. Any notice given under Regulation 2(2) may be expressed to become ineffective if certain specified events happen, or, whether so expressed or not, may be cancelled by a notice of cancellation given by or on behalf of the Board, and if to the knowledge of the United Kingdom payer any of those events happens or if such notice of cancellation is given, any payment made to the non-resident by the United Kingdom payer after the happening of that event becomes known to the United Kingdom payer or after the receipt of that notice, as the case may be, shall be subject to deduction of tax in accordance with the Income Tax Acts.

9. If it is discovered after a notice has been given under Regulation 2(2) that the non-resident is not entitled to exemption or partial relief from tax in respect of income referred to in the notice, any tax which, but for the notice, would have been deductible from any payment made to the non-resident by the United Kingdom payer but in compliance with the notice has not been so deducted—

(a) may be assessed on the non-resident under Case VI of Schedule D by an Inspector, or

(b) shall, if a direction to that effect is given by or on behalf of the Board, be deducted by the United Kingdom payer out of so much of the first payment made to the non-resident after the date of the direction as remains after the deduction of any tax deductible therefrom under the Income Tax Acts, and any balance which cannot be deducted out of the first such payment shall be deducted, subject to the same limitation, out of the next such payment. and so on until the whole of the tax (the amount of which shall be specified in the direction) has been deducted….

11. Regulations 2(2) and 8 shall not apply to payments in respect of coupons for any interest. but any such payments may, under arrangements approved by the Board, be made without deduction of tax or with tax deducted at a rate specified in the arrangements, if the non-resident or any person acting on his behalf makes a claim to the United Kingdom payer to that effect in such form as may be prescribed by the Board, and in the case of any payments so made Regulations 3 to 7 inclusive and Regulation 9 shall, with any necessary modifications, apply as if the claim were a notice given under Regulation 2(2)."

Summary

13. In summary, in the case of interest paid by a UK resident company during the period relevant to this appeal:

(1) there was an obligation on the part of the payer to withhold, and account to the Respondents for, income tax only if the interest in question was "yearly interest" and "[arose] in the United Kingdom" – which is to say, had a United Kingdom source; and

(2) even then, there was no such obligation if the person "beneficially entitled" to the interest was a UK resident company.

Moreover, if the interest formed part of the "industrial and commercial profits" of a Guernsey resident company, there is a question as to whether the terms of paragraph 3(2) of the Guernsey Treaty, the TIOPA and the DTR Regulations meant that the obligation to withhold and account for income tax did not arise.

THE BACKGROUND AND FACTS

General

14. During the period to which this decision relates, the Appellant was the ultimate parent of a group of companies which was engaged in property investment, development and construction. The group was founded by the late Mr Neville Andrew ("NA") and the directors of the Appellant during the period to which this decision relates included NA, his wife, Mrs Ruth Andrew ("RUA"), and his son, Mr Richard Andrew ("RA"). The directors also included Mr John Hazelwood, who was unrelated to the Andrew family but had been a director of the Appellant since 1986 ("JH");

15. The following summary of the facts is taken from the documents in the DB and the witness evidence of JH, RA and Mr Mark Gill, who was, until 2010, a director of companies in the Mercator group, a group providing trust, fund, real estate and corporate administration services worldwide and which became the First Names group in July 2014 ("Mercator").

16. There is no dispute between the parties in relation to the relevant facts and they are as follows:

(1) the Appellant's group acquired property primarily for investment purposes – which is to say that its strategy was to hold the properties which it acquired for the long-term, deriving its profits from the rent which they produced and profit on eventual re-sale. The group did not acquire properties for the purposes of selling them in the short-term and therefore did not carry on a trade of dealing in property. Crucially,

although the group has very recently made acquisitions outside the United Kingdom, during the period to which this decision relates and in the period prior to that, all of the properties held by the group were in the United Kingdom and therefore all of the income and capital gains of the group were made in the United Kingdom;

(2) as a group holding its property for investment purposes and expanding as it made its acquisitions, the Appellant's group had a continuous and growing requirement for loan funding. That funding took a variety of forms ranging from institutional secured funding to unsecured borrowings from persons connected with the group, such as the directors of the Appellant, members of the Andrew family, trusts of which members of the Andrew family were settlors and/or beneficiaries and the group's funded unapproved retirement benefit scheme (the "FURBS");

(3) it is to certain of the latter category of loans to which the present proceedings relate – loans made to the Appellant by RA, NA, two Gibraltar resident Andrew family trusts managed by STM Fidecs Trust Company Limited - The Richard Andrew 2003 No 2 Settlement (the "RAS") and The Neville Andrew 2003 No 2 Settlement (the "NAS") - JH, RUA (both directly and through a separate account, the Ruth Andrew No 2 Account ("RUA2")), the FURBS and RA's sister, Mrs Charlotte Langmead ("CL") (together, the "Lenders" and, each, a "Lender");

(4) more specifically, the question which has arisen is whether, when it paid the interest described in the table set out in paragraph 2 above on those loans between 1 October 2010 and 31 March 2015, the Appellant should have withheld income tax from the payments of interest and accounted for that income tax to the Respondents;

(5) as noted in paragraph 16(2) above, the Appellant had an ongoing need for borrowings to finance its property investment business. It was the practice of NA and RA to meet at the end of each calendar year in order to discuss the group's funding requirements for the following year. The various Lenders mentioned in paragraph 16(3) above provided part of that funding. Exactly how that funding was provided lies at the heart of this appeal and therefore requires some detailed explanation;

(6) prior to 2004, the funding from the Lenders tended to be provided somewhat informally. On many occasions it was undocumented and, even when it was documented, the relevant agreement contained little more than the relevant interest rate and the terms governing the timing of repayment (including some limited events of default). In general, in the absence of default, the loans were repayable on short notice by either party. The written agreements did not have provisions relating to matters such as the governing law, the jurisdiction of enforcement and the place in which payments would be made. At the hearing, I was referred to a typical example of the practice at that time in the form of an agreement executed on 16 February 2001 between Hargreaves Construction Company Limited, an affiliate of the Appellant ("HCC"), and the FURBS set out at pages 1397 and 1398 of the DB. That agreement recorded the fact that three loans had been made by the FURBS to HCC in 1998, that interest at a rate equal to the Barclays Bank base rate plus 3% was payable on those loans and that, in the absence of an occurrence of one of the limited events of default, each loan would be repayable on four weeks' notice by either party;

(7) in November 2004, the group took the advice of BDO LLP ("BDO") and Rex Bretten QC with a view to achieving a more advantageous tax position in relation to the funding from the Lenders. The planning was intended to achieve the position whereby the group companies continued to get relief for the interest payments which they made

but that interest was not subject to UK tax. In the first instance, this entailed the following steps:

(a) documenting the undocumented loans and amending the terms of the existing documented loans, in each case in a manner which was intended to ensure that the interest under the relevant loan ceased to have a UK source by virtue of the fact that all payments under the relevant loan were to be made outside the United Kingdom, the relevant loan would be governed by the laws of a jurisdiction other than a jurisdiction within the United Kingdom and that alternative jurisdiction would have the sole and exclusive jurisdiction in relation to the relevant loan;

(b) arranging for the relevant Lender to assign the right to the interest under the relevant loan to a Guernsey resident company run by Mercator, called Storrier Investments Limited (which was subsequently re-named Storrier Trading Limited) ("Storrier") shortly before the interest was paid;

(c) simultaneously arranging for the Lender to assign the principal of the relevant loan to a group company other than the borrowing company;

(d) arranging for the interest and principal under the relevant loan to be paid or repaid very shortly – a matter of no more than one or two days - after the assignments referred to in paragraphs 16(7)(b) and 16(7)(c) above; and

(e) arranging for the relevant Lender to advance an amount which was generally at least as large as the principal amount of the original loan in order to fund that payment and repayment.

In the rest of this decision, I will refer to the general process described above of assignment, followed by repayment by the Appellant and re-advance by the original Lender, as the "refinancing structure";

(8) as outlined in an email of 17 December 2004 from JH to the trustee of the RAS and the NAS, which was included at page 798 of the DB, "[the] advantage resulting from this transaction to the Trust is that the consideration received by the Trust in respect of the interest will be capable of distribution to the beneficiaries without them incurring any tax liability thereon". In their oral evidence at the hearing, both JH and RA frankly admitted that, whilst there was a commercial benefit to the Appellant in having access to unsecured finance from the Lenders for the purposes of its property business, the sole purpose of the refinancing structure itself was to ensure that the interest accruing on the loans fell out of account for tax purposes for the Lenders whilst the borrower's corporation tax deduction remained intact and that there was no commercial purpose to the refinancing structure itself other than that tax advantage. Prior to taking the tax advice recorded above and implementing the refinancing structure, the loans made by the Lenders had simply remained outstanding and the cycle of assignment, repayment and re-advance did not occur;

(9) the refinancing structure described in paragraph 16(7) above continued from 2004 onwards, and throughout the period to which this appeal relates, although subject to the following adjustments:

(a) from 2009 onwards, which is to say, throughout the period to which this appeal relates, in order to accommodate a technical change in UK law, the assignments by the Lenders on each implementation of the refinancing structure involved assignments to Storrier of both the right to the interest and the principal on the relevant loans, and not just the right to the interest. In other words, there

were no assignments of the principal on the loans to the group company which had been the assignee prior to that date;

(b) in relation to the interest payments made in 2012 and thereafter, after Storrier acquired the right to the interest and the principal on a loan from a Lender, it assigned the right to the interest on that loan to a UK resident company which was also managed by Mercator, called Houmet Trading Limited ("Houmet") shortly before the interest payment was made, with the result that the Appellant was required to make its interest payment to Houmet instead of Storrier shortly after the relevant loan had been assigned by the Lender to Storrier; and

(c) in relation to four of the loans made in March 2013, the role of Storrier as acquirer of the right to the interest and the principal on a loan and the on-seller to Houmet of the right to the interest on that loan was instead played by one of two Guernsey resident trusts also managed by Mercator called The Longton Settlement and The Longstone Settlement (together, the "Guernsey Trusts" and, each, a "Guernsey Trust");

(10) it may be seen that, after taking into account the adjustments to the refinancing structure described in paragraph 16(9) above, during the period to which this appeal relates, the refinancing structure meant that, on an annual basis, or sometimes at longer intervals, a loan made by a Lender, together with the right to the interest thereon, would be assigned to Storrier or a Guernsey Trust and then, in a matter of no more than two or three days, the principal on that loan, together with the interest on that loan, would be repaid by the Appellant, funded by way of a new loan made to the Appellant by the Lender out of the proceeds of the assignment. The new loan was almost invariably larger than the original loan, to enable the Appellant to pay the interest on the original loan. However, there were a limited number of cases where the Appellant used its own resources to fund part of the repayment, with the result that the principal amount of the new loan was slightly lower than the original loan. After the change made in 2012 described in paragraph 16(9)(b) above, Storrier or the relevant Guernsey Trust would assign to Houmet, in the period between its acquisition of a loan and the repayment of that loan, the right to the interest on that loan, with the result that, when the repayment occurred, the principal amount would be paid by the Appellant to Storrier or the relevant Guernsey Trust and the interest amount would be paid to Houmet;

(11) the documentation used to achieve these steps was in standard form, as noted in the following extract from a letter from BDO to the Respondents of 30 June 2021 set out at page 1272 of the DB:

"The loan assignments with which you are concerned have a long history, the first having been made in December 2004, and in accordance with the assignors' expectations following on at yearly or shorter intervals up to and beyond 6 April 2013, when there were worthwhile loan and accrued interest balances to assign. The pricing of the assignments agreed in 2004 was adjusted only once (in 2009) prior to the introduction of the disguised interest rules. Throughout the entire period with which you are concerned the loan assignment documentation was in very substantially the same form and on the same terms. In effect, there was a comprehensive and long-standing understanding between the parties to the loan assignments, and all assignments whether before or after 6 April 2013, were effected pursuant to that understanding…";

(12) at the hearing, I was taken to examples of that standard documentation, the key features of which may be summarised as follows:

(a) the form of loan agreement between a Lender and the Appellant was typified by the loan from the NAS to the Appellant of 11 February 2009 set out at pages 1631 and following of the DB and the loan from the RAS to the Appellant of the same date set out at pages 1636 and following of the DB. Each loan contained the following relevant terms:

(i) it was repayable within 30 days' of notice by the Lender or at any time by the Appellant (clause 3);

(ii) all payments under the agreement were required to be made in Gibraltar from a source outside the United Kingdom (clause 4);

(iii) the loan was not secured over any assets in the United Kingdom (clause 5); and

(iv) the loan was governed by Gibraltar law and the Appellant agreed for the benefit of the Lender to submit to the exclusive jurisdiction of the Gibraltar courts (although the Lender was not similarly constrained) (clause 9);

(b) the form of revolving facility agreement between a Lender and the Appellant was typified by the revolving facility letter between the FURBS and the Appellant of 3 November 2009 set out at pages 1659 and following of the DB and the revolving facility letter between RA and the Appellant of the same date set out at pages 1663 and following of the DB. Each revolving facility letter contained the following relevant terms:

(i) there was no term within which the Appellant was entitled to call for drawdowns under the facility. As long as the Appellant was not in default, it was entitled to call for drawdowns indefinitely;

(ii) each advance under the facility was repayable on demand by the Lender and pre-payable by the Appellant at any time;

(iii) all payments under the agreement were required to be made outside the United Kingdom from a source outside the United Kingdom;

(iv) no advance was secured over any assets in the United Kingdom; and

(v) the letter was governed by Jersey law and the parties agreed to submit to the exclusive jurisdiction of the Jersey courts;

(c) the form of assignment by a Lender to Storrier or a Guernsey Trust was typified by the assignment from the FURBS to Storrier of 29 November 2010 set out at pages 1776 and following of the DB and the assignment by the RAS to Storrier of the same date set out at pages 1820 and following of the DB. Under each assignment, the relevant Lender agreed to demand repayment of the debt upon request to that effect from Storrier or the relevant Guernsey Trust and the Appellant – which was also a party to the assignment – consented to the assignment;

(d) the form of repayment request by Storrier or a Guernsey Trust was typified by the repayment request made by Storrier to the Appellant of 29 November 2010 set out at page 1780 of the DB. The only notable feature of this document is that the repayment request came from Storrier or the relevant Guernsey Trust and not the Lender, despite the provision in the assignment referred to in paragraph

16(12)(c) above suggesting that the request would instead be made by the relevant Lender at the request of Storrier or the relevant Guernsey Trust;

(e) the form of notification to the Appellant of the assignment by Storrier or the relevant Guernsey Trust to Houmet of the right to interest and the Appellant's acknowledgement and acceptance thereof was typified by the letter from Storrier to the Appellant of 12 March 2014 and the Appellant's response thereto of the same date set out at pages 2218 and 2219 of the DB. The letter from Storrier informed the Appellant that the right to the interest had been assigned to Houmet and directed the Appellant to pay the interest to Houmet or as Houmet might direct and the letter from the Appellant acknowledged and agreed to that direction; and

(f) the form of demand by Houmet to the Appellant for interest to be paid to Houmet was typified by the letter from Houmet to the Appellant of 13 March 2013 set out at page 2069 of the DB . This referred to "the letter of today's date issued to you by … Storrier and your acknowledgement thereof in connection with the assignment to us, Houmet…of the benefit in relation to the accrued interest….and all future interest on a loan of a principal sum of £1,975,000.00….advanced to you by [RA] pursuant to a revolving facility arrangement effective 19 December 2012" and requested payment of the interest under that loan.

I was not provided with a form of the typical assignment agreement between Storrier or the relevant Guernsey Trust and Houmet effecting the assignment of the right to the accrued interest;

(13) I was also taken to various documents which demonstrated the practical operation of the refinancing structure, such as the following from the end of 2010:

(a) an email of 10 November 2010 from JH to Mr Anthony Whatling of BDO which made reference to the time gaps between the various steps in the refinancing structure. It noted that, in the particular example under discussion, the assignment of principal and interest on the loan in question to Storrier would take place on day 1, with Storrier's making the payment for that assignment on either day 1 or day 2, the assignor would make the new loan to the Appellant to finance the ensuing repayment of the assigned loan on day 2 or day 3 and then repayment of the assigned loan would be made on day 3 or day 4 (see page 820 of the DB);

(b) an email of 17 November 2010 from JH to Ms Carey Mahoney, representing the trustees of the RAS and the NAS, which referred to the fact that the assignment and re-lending were planned to take place in the last week of November and asking Ms Mahoney to confirm that the trustees wished to be included in those assignments and, if so, would be willing to make fresh loans to Hargreaves immediately after each assignment (see page 813 of the DB);

(c) a response from Ms Mahoney to JH of 25 November 2010, which confirmed that the trustees would be happy to participate in the assignments and to make new loans following the assignments (see page 927 of the DB);

(d) an email of 29 November 2010 from JH to Ms Mahoney, which referred to JH's understanding that, given that the trustees were willing to make new loans to the Appellant on the same terms as their existing loans after the assignment of their existing loans had been completed, the proceeds of the assignment would be

paid to the trustees' respective client accounts with Mercator and that the new loans would be made to the Appellant out of those proceeds (see page 915 of the DB); and

(e) an email of 2 December 2010 from JH to NA, which explained that the assignment proceeds of £4,743,430.35 would be paid by Storrier to Mercator to hold to NA's order and that NA was to ask Mercator to pay £4,740,000 of that amount to the Appellant by way of a new loan from NA to the Appellant and to pay the balance to NA himself (see page 760 of the DB);

(14) the steps in relation to the refinancing structure on each occasion that it was implemented were co-ordinated by JH on behalf of the Appellant. It was JH who communicated with the Lenders and Storrier and who provided the necessary documentation for signature by the parties; and

(15) in relation to the refinancing structure:

(a) in his oral evidence at the hearing, JH testified that, although, in the case of any implementation of the refinancing structure, in theory, the Appellant could have obtained funds from someone other than the Lender under the original loan to fund the repayment of the original loan, in practice this was hypothetical and did not occur; and

(b) RA testified to the same effect in his oral evidence at the hearing. He said that, in theory, a particular Lender could have declined to make a new loan to fund the repayment of the Lender's previous loan but, in practice, this never occurred.

17. Set out below is a table listing the loans the interest on which is the subject of this appeal together, in the case of some of the Lenders, with the loan which immediately preceded the first of such loans made by that Lender and the interest on which is not part of the subject of this appeal. (Those preceding loans – numbered 1, 7, 18, 24, 30 and 36 in the first column of the table – are marked with an asterisk in the table below for the sake of clarity). This table was prepared at my request by the parties during the course of the hearing. It is not entirely complete but the parties are agreed that it provides an accurate general view of the loans which were outstanding over the period in question.

Loan number	Lender	Date of loan	Date of loan agreement	Principal amount (£)	Date of repayment
1 *	The RAS	02.04.09	02.04.09	9,500,000	08.12.09
2	The RAS	09.12.09	09.12.09	9,500,000	01.12.10
3	The RAS	01.12.10	13.03.13	6,333,333	18.03.13
4	The RAS	01.12.10	13.03.13	3,166,667	19.03.13
5	The RAS	18.03.13	18.03.13 and 19.03.13	5,593,898.35	17.03.15
6	The RAS	18.03.13	18.03.13 and 19.03.13	5,593,898.35	17.3.15
7 *	The NAS	01.04.09	01.04.09	9,000,000	09.12.09
8	The NAS	10.12.09	10.12.09	9,000,000	01.12.10

9	The NAS	01.12.10	13.03.13	6,000,000	15.03.13 (?)
10	The NAS	01.12.10	13.03.13	3,000,000	19.03.13
11	The NAS	15.03.13	15.03.13 and 19.03.13	5,273,382.68	17.03.15
12	The NAS	15.03.13	15.03.13 and 19.03.13	5,273,382.68	17.03.15
13	The FURBS	31.03.09	03.11.09	7,764,997.44	10.12.09
14	The FURBS	15.12.09	22.11.10	8,020,000	30.11.10
15	The FURBS	29.11.10	04.03.13	8,506,500	14.03.13
16	The FURBS	14.03.13	18.07.13	5,094,739.35	17.03.14
17	The FURBS	14.03.13	18.07.13	5,094,739.35	18.03.14
18 *	RA	01.04.09	03.11.09	1,225,000	14.12.09
19	RA	15.12.09	22.11.10	1,550,000	2.12.10
20	RA	2.12.10	24.11.11	1,850,000	29.11.11
21	RA	28.11.11	15.12.11	1,875,000	19.12.12
22	RA	19.12.12	19.12.12	1,975,000	13.03.13
23	RA	11.03.13	18.07.13	940,000	13.03.14
24 *	CL	08.04.09	03.11.09	880,000	14.12.09
25	CL	15.12.09	22.11.10	894,857.54	2.12.10
26	CL	2.12.10	24.11.11	838,000	29.11.11
27	CL	28.11.11	15.12.11	868,706.58	19.12.12
28	CL	19.12.12	19.12.12	951,058.05	13.03.13
29	CL	11.03.13	30.07.13	915,020.30	13.03.14
30 *	JH	31.03.09	28.10.09	562,523.74	14.12.09
31	JH	15.12.09	22.11.10	592,283.03	2.12.10
32	JH	02.12.10	24.11.11	598,969.40	28.11.11
33	JH	28.11.11	15.12.11	556,549.60	18.12.12
34	JH	18.12.12	18.12.12	635,000	13.03.13
35	JH	11.03.13	15.7.13	641,650	13.03.14
36 *	NA	01.04.09	28.10.09	3,500,000	14.12.09
37	NA	15.12.09	22.11.10	4,425,000	02.12.10
38	NA	02.12.10	24.11.11	4,250,000	29.11.11
39	NA	28.11.11	15.12.11	4,450,000	18.12.12
40	NA	18.12.12	18.12.12	4,760,000	13.03.13
41	NA	11.03.13	15.07.13	3,175,000	13.03.14

42	RUA	23.12.04	24.11.11	297,404.25	25.11.11
43	RUA	28.11.11	15.12.11	296,781.33	19.12.12
44	RUA	19.12.12	19.12.12	325,150.40	13.03.13
45	RUA	11.03.13	15.07.13	18,820.76	13.03.14
46	RUA2	25.12.09	04.03.13	230,600	13.03.13
47	RUA2	11.03.13	15.07.13	254,000	13.03.14

STORRIER

18. Before setting out the issues which I need to address in this decision, I should briefly say something about Storrier, the company which acquired most of the assigned loans from the Lenders and, in some cases, then assigned the right to the interest on those loans to Houmet. A feature of the conduct of the proceedings which I found puzzling was a dispute between the parties in relation to whether or not any member of the Andrew family had a beneficial interest in Storrier. Both parties devoted a considerable part of the submissions in their skeleton arguments and their witness evidence to that question but it was never clear to me why that question had any relevance to the issues which I was being asked to address and I believe that the parties reached a similar conclusion as the hearing progressed. They were also both agreed that the question might well become relevant to other issues in dispute between them but adopted different procedural approaches to that fact. Mr Way, on behalf of the Appellant, asked that I should make a finding of fact to the effect that no such beneficial interest existed, whilst Mr Vallat asked that I should make no finding of fact either way.

19. In light of the fact that the question has no relevance to the issues which I am asked to address, and the fact that I heard conflicting evidence on the question, I prefer to adopt Mr Vallat's approach. Accordingly, I reach no finding of fact in relation to whether any member of the Andrew family had a beneficial interest in Storrier at any time.

20. A similar debate took place between the parties at the hearing as to whether, even if no member of the Andrew family had a beneficial interest in Storrier, there was nevertheless a connection between Storrier and the Appellant which meant that transactions between them and between Storrier and the Lenders could not be said to be taking place at arm's length. Again, I suspect that this question may well become relevant to other issues in dispute between the parties but I am unable to see how it has any relevance to the issues which I have to decide. I therefore decline to make any finding of fact in relation to that question too although I would observe that it is common ground that:

(1) there was throughout the period to which this appeal relates a shareholding connection between the Appellant (and the Appellant's employee benefit trust) and Storrier in that subsidiaries of both the Appellant and the Appellant's employee benefit trust held non-voting preference shares in a Guernsey resident company called Garberdine Limited whose ordinary shares were held by Storrier and which, in turn, held non-voting preference shares in Storrier; and

(2) Storrier was acquired off the shelf by Mercator in 1997 at the request of a Mr Christopher McFadyen, who was a trustee of a trust which held ordinary shares in the Appellant, for the specific purpose of subscribing for a deep discount bond to be issued by the Appellant.

THE ISSUES

21. The Respondents submit that the interest in this case had a UK source and was "yearly" interest so that, prima facie, an obligation to withhold income tax arose. In addition, they say that:

(1) so far as the interest paid to Storrier is concerned, the withholding tax obligation was not vacated pursuant to paragraph 3(2) of the Guernsey Treaty because, inter alia:

(a) the Appellant has produced insufficient evidence to show that the interest formed part of the "industrial and commercial profits" of Storrier;

(b) in any event, Storrier has made no claim for relief from the withholding tax as it was required to do by Section 6(6) of the TIOPA if it wished to benefit from the paragraph; and

(c) in addition, the obligation to withhold tax was an obligation of the Appellant and could not be vacated unless the Appellant was directed to make gross payment by the Respondents pursuant to paragraph 2 of the DTR Regulations; and

(2) so far as the interest paid to Houmet is concerned, the withholding tax obligation was not vacated pursuant to Section 933 of the ITA because Houmet never became beneficially entitled to the interest.

22. In response, the Appellant submits that the interest in this case did not have a UK source. It adds that, even if the interest did have a UK source, much of the interest was not "yearly" in nature. Finally, it says that, even if some of the interest was UK source "yearly" interest:

(1) the Appellant was entitled to rely on paragraph 3(2) of the Guernsey Treaty to make gross payment of the interest which was paid to Storrier because:

(a) that interest was part of the "industrial and commercial profits" of Storrier;

(b) paragraph 3(2) of the Guernsey Treaty applied "despite anything in any enactment" (see Section 6(1) of the TIOPA);

(c) as that paragraph did not provide for relief from UK tax but was rather a provision attributing profits to a UK establishment of a Guernsey resident company, it fell within Section 6(2)(e) of the TIOPA and not Section 6(2)(a) of the TIOPA, with the result that it applied automatically without the need for a claim to have been made by Storrier under Section 6(6) of the TIOPA; and

(d) finally, the provisions of the DTR Regulations which dealt with obtaining directions for gross payment were permissive and not compulsory, with the result that, whilst a direction under those regulations was sufficient in order for the Appellant to be entitled to make gross payment to Storrier, it was not necessary for the Appellant to obtain such a direction before making gross payment; and

(2) the Appellant was entitled to rely on Section 933 of the ITA to make gross payment of the interest which was paid to Houmet because Houmet was beneficially entitled to that interest.

23. In its notice of appeal, the Appellant included, as an additional ground of appeal, the fact that certain of the interest paid by the Appellant in this case had been subject to tax by assessment in the hands of UK resident individual beneficiaries of the RAS and the NAS but, at the hearing, Mr Way said that the Appellant did not wish to pursue that ground of appeal any further.

24. It follows from the above summary that the questions which I need to address in this decision are as follows:

(1) did the interest paid on the loans have a UK source?

(2) if it did, was the interest paid on the loans "yearly" or short in nature?

(3) if any of the interest paid on the loans had a UK source and was "yearly" in nature, was the Appellant entitled to rely on paragraph 3(2) of the Guernsey Treaty to make gross payment of the interest which it paid to Storrier? and

(4) if any of the interest paid on the loans had a UK source and was "yearly" in nature, was the Appellant entitled to rely on Section 933 of the ITA to make gross payment of the interest which it paid to Houmet?

25. For the reasons set out in the paragraphs which follow, I have concluded that:

(1) the interest in this case did have a UK source (see paragraphs 49 to 63 below);

(2) the interest was also "yearly" in nature (see paragraphs 78 to 94 below);

(3) the Appellant was not relieved by paragraph 3(2) of the Guernsey Treaty from its obligation to withhold tax in respect of the interest which it paid to Storrier (see paragraphs 103 to 126 below); and

(4) apart from a de minimis amount, the reason for which is explained in the relevant paragraphs, the Appellant was not relieved by Section 933 of the ITA from its obligation to withhold tax in respect of the interest which it paid to Houmet (see paragraphs 140 to 157 below).

26. In the rest of this decision, I will consider each of the questions in turn, starting with a summary of the relevant law, then outlining the arguments in relation to that question made by Mr Way on behalf of the Appellant, before setting out my conclusion on the question.

27. In order not to lengthen this decision any further, I have not summarised in the paragraphs below the arguments in relation to each question which were put to me by Mr Vallat on behalf of the Respondents - except in rare instances - because I was in accord with Mr Vallat's submissions and they are reflected in my conclusions.

SOURCE OF INTEREST

The law

Bank of Greece

28. The leading case in relation to identifying the source of payments of interest is the decision of the House of Lords in *The National Bank of Greece SA v Westminster Bank Executor and Trustee Company (Channel Islands) Limited* [1971] AC 945 ("*Bank of Greece*"). In that case, the source principle had to be applied to the following critical facts. Bearer bonds subject to English law, denominated in sterling and secured (on issue) on property in Greece were issued by a Greek resident bank and were the subject of an unconditional guarantee by another Greek resident bank. Neither the original obligor nor the original guarantor had a place of business in the United Kingdom. The coupons were required to be paid by the principal debtor through paying agents in London or, at the option of the bearer of the coupons, in Greece by cheque drawn on London. Whichever means of payment was chosen, the funds to pay the interest would have to be remitted from Greece to London. In 1949, the Greek government imposed a moratorium on the bond obligations so that, for all practical purposes, the liability of the original obligor and the original guarantor were extinguished. Then, in 1953, the National Bank of Greece became the universal successor of the original guarantor. The National Bank of Greece had offices in London and carried on

business in the United Kingdom. The obligations under the bond could thus be enforced against the National Bank of Greece but only in the United Kingdom and not in Greece (as a result of the moratorium). The House of Lords held that, although the successor guarantor had a place of business in London and the only place where the obligations under the bond could be enforced following the moratorium was in the United Kingdom, the source of the interest was not in the United Kingdom.

29. In his seminal judgment, Lord Hailsham LC said as follows at pages 954H and following:

> "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 the universal succession comparatively recently 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 the fact that the second guarantor so substituted subsequently acquired a London place of business or by 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 bond. 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."

30. In the extract from his speech set out above, Lord Hailsham made it clear that, in applying these factors in any particular case, the source of an interest obligation should be identified by reference to the position which existed at the time when the obligation in question originally arose and that, as long as that obligation remained the same, the original source could not be affected by subsequent events, such as, in that case, the replacement of an original guarantor which had no connection with the United Kingdom by a new guarantor which did and the fact that the moratorium in Greece meant that the obligation in question could be enforced and discharged only in the United Kingdom. In the opinion of Lord Hailsham, neither of those facts were sufficient to change the source of the interest obligation as originally created.

31. As Arden LJ (as she then was) explained in the more recent case of *Ardmore Construction Limited v The Commissioners for Her Majesty's Revenue and Customs* [2018]

EWCA Civ 1438 ("*Ardmore CA*"), the decision in *Bank of Greece* makes it clear that identifying the source of interest involves a multi-factorial test. Moreover, as Arden LJ pointed out in *Ardmore CA* at paragraph [39], the test is "acutely fact sensitive".

Ardmore CA

32. Whilst the decision in *Bank of Greece* is inevitably the starting point in relation to any determination of source, there are two reasons why recourse solely to that decision in making that determination is insufficient.

33. The first is that *Bank of Greece* was decided on its own specific facts and the factors to be taken into account in determining the source of interest paid in other circumstances are not necessarily limited to the factors set out in that case. Indeed, in *Ardmore Construction Limited and Andrew Collin Perrin v The Commissioners for Her Majesty's Revenue and Customs* [2015] UKUT 633 (TCC) ("*Ardmore UT*" and, together with *Ardmore CA*, the "*Ardmore Cases"),* the Upper Tribunal noted that "[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" (see paragraph [42] in *Ardmore UT*).

34. In *Bank of Greece* itself, the relevant factors identified by the House of Lords were the residence of the debtor, the residence of the guarantor (if any), the location of the security for the debt (if any) and the ultimate, or substantive, source of the discharge of the debtor's obligation. In other words, the House of Lords looked to the jurisdiction from which the funds used to pay the interest emanated (Greece) and not the fact that the actual payments of interest were made in London.

35. In the *Ardmore Cases*, Ardmore sought to establish that the residence of the lender and the place where the credit was provided were the only factors to be taken into account in determining the source of interest. It referred to the existence of persuasive, non-binding authority to that effect in the New Zealand case of *Commissioner of Inland Revenue v NV Philips Gloeilampenfabrieken* [1955] NZLR 868 (NZ CA) ("*Philips*"). The New Zealand Court of Appeal in that case had held that:

(1) the originating cause of interest paid on a loan was the place where the loan was made;

(2) one had to look behind the fact that the debtor had entered into the obligation to pay the interest to the reason why it had done so – namely, the original advance; and

(3) therefore the place where the loan was made should be regarded as the source of the ensuing interest payments.

The Upper Tribunal in *Ardmore UT* emphatically rejected the proposition that the residence of the lender and the place where the credit was provided were the only factors to be taken into account in determining the source of interest, saying that *Bank of Greece* had made it clear that the test was multi-factorial in nature.

36. Indeed, in *Ardmore UT*, the Upper Tribunal went even further than that, holding that the residence of the lender and the place where the credit was provided were not even significant factors to be taken into account in making that determination. In *Ardmore UT* at paragraph [45], the Upper Tribunal said that it based that conclusion on the fact that neither the residence of the creditor nor the place of activity of the creditor nor the place where the credit was provided were mentioned by Lord Hailsham in *Bank of Greece* and that therefore those facts must have carried little or no weight in that case.

37. In *Ardmore CA*, Arden LJ agreed with that conclusion, saying that "[the] immediate search is for the source of the interest rather than a search indirectly for the source of the loan. The funds paid over as interest derived from funds generated in the UK. The activity of lending became passive once the loan was made, whereas the business of Ardmore was actively conducted to produce those funds."

38. In addition, in both *Ardmore Cases*, the relevant courts rejected Ardmore's submission that the debtor's residence was not an appropriate factor to take into account where there was an exclusive jurisdiction clause in the loan document and where no security had been given over assets situated in the United Kingdom (see *Ardmore UT* at paragraphs [51] to [53] and *Ardmore CA* at paragraphs [18] and [42]). The Upper Tribunal in *Ardmore UT* simply stated that there was no support within *Bank of Greece* for that proposition, noting that, in *Bank of Greece*, the governing law of the bonds was English law and yet that was not mentioned by Lord Hailsham in the passage set out in paragraph 29 above. In the Court of Appeal in *Ardmore CA*, Arden LJ explained that the reason why the exclusive jurisdiction and governing law clauses were of no moment was that "[there] was no default and the Gibraltarian exclusive jurisdiction and governing law clauses would only matter if there was default. The importance of those clauses is also undermined by the fact that the enforcement of any judgment following default on assets of Ardmore would be in the UK (and it is not necessary to go further than to note that all the available assets to meet the liabilities to the lender were in the UK)" (see *Ardmore CA* at paragraph [42]).

39. The second reason why the decision in *Bank of Greece* is insufficient in and of itself to provide the answer to the determination of source in all circumstances is that, whilst the case makes it clear that the test is multi-factorial, it does not explain how a particular court or tribunal is to determine source where the relevant factors point in different directions. In other words, simply stipulating that the test is multi-factorial does not assist the relevant court or tribunal in identifying which factors should be regarded as being determinative in any particular case.

40. In *Ardmore CA*, Arden LJ held that the answer to this problem was to be found in the judgment of Lord Atkin in the Privy Council decision in *Rhodesia Metals, Limited (In Liquidation) v Commissioner of Taxes* [1940] 3 All ER 422. As summarized by Arden LJ in *Ardmore CA* at paragraph [34], "Lord Atkin first made the point, which I would respectfully adopt, that great caution should be applied in adopting decisions on source from different legislative regimes, that what is the source depends to some extent on the perspective from which the question is asked, that it was not possible to provide a universal definition of "source" and, most importantly, that the question had to be resolved by applying practical sense. I refer to this below as "the practical approach"" (see *Ardmore CA* at paragraph [34]).

41. Arden LJ elaborated on this approach in paragraphs [37] to [39] in *Ardmore CA*, when she said as follows:

"37. The Privy Council's reference to matters of fact means that the correct approach to applying the multifactorial test is to ask whether a practical person would regard the source as in this jurisdiction or elsewhere. I do not see any material difference between this approach and that of Lord Hailsham in the National Bank case. Lord Hailsham applied a matter of fact approach as opposed to an approach based on legal concepts and rules.

38. Lord Atkin's approach has been impressed on us by HMRC, who have emphasised the need to have regard to "the underlying commercial reality." Those words are appropriate to this case which concerns a commercial transaction but in other types of transaction one might ask which was the source from a practical, or realistic, point of view.

39. There has been much reference to a multifactorial test. To that I would add that the correct approach is the practical approach and that it is not merely multifactorial but also acutely fact-sensitive. The court or tribunal must examine all the available facts both singly and cumulatively."

42. In the *Ardmore Cases*, Ardmore, a UK resident company, had subscribed for shares in two companies incorporated in the British Virgin Islands and then the share subscription moneys had been lent by those companies to two Gibraltar trusts before being lent by the trusts back to the appellant on an unsecured basis. The loans to Ardmore contained provisions stipulating that all payments under the loans were to be made in Gibraltar from a source outside the United Kingdom, that the loan agreements were governed by Gibraltar law and that the parties submitted to the exclusive jurisdiction of the Gibraltar courts. The interest payments were in fact made from Ardmore's bank account in the United Kingdom and funded out of the income of Ardmore's UK trading activities.

43. The Upper Tribunal held that these facts led to the conclusion that the interest paid by Ardmore to the trusts had a UK source. In reaching that conclusion, it applied the multi-factorial test in *Bank of Greece* and concluded that the UK residence of the debtor and the fact that the United Kingdom was the source or origin of the payments were factors which carried much more weight than the residence of the lender, the place where the money was lent and the governing law and exclusive jurisdiction clauses (see *Ardmore UT* at paragraphs [90] and [91]). That conclusion was upheld by the Court of Appeal, who considered that, on the basis of the facts in that case, "the underlying commercial reality" was that the source of the interest was the United Kingdom. In reaching its conclusion, the Court of Appeal attached great weight to the fact that the funds used to pay the interest had been generated in the United Kingdom. It said that the importance of the exclusive jurisdiction and governing law clauses were undermined by the fact that the enforcement of any judgment following a default on the assets of Ardmore would be in the United Kingdom and it noted that, relative to the links with the United Kingdom, the links with Gibraltar were insubstantial.

The arguments of the Appellant

Distinguishing Ardmore CA

44. Mr Way accepted that source was to be determined by reference to a multi-factorial test and that that test was to be applied by reference to "the underlying commercial reality". However, he sought to distinguish the present facts from those in the *Ardmore Cases* by saying that:

(1) the sums lent to Ardmore had had their original provenance in the United Kingdom in that the circle of funds had started with Ardmore (the ultimate borrower) whereas, in this case, the credit provided to the Appellant at the time when the interest was paid was coming from Storrier, a non-UK resident company, or a Guernsey resident trust and had not emanated from the Appellant; and

(2) in the *Ardmore Cases*, some of the facts – for example the addition of the clauses relating to the location of payments made under the loan agreements, the governing law and exclusive jurisdiction – were contrived and had been included specifically and artificially to turn the interest into non-UK source interest whereas, in this case, there was no such contrivance.

45. Mr Way emphasised that the practical person hypothesised by Arden LJ in *Ardmore CA* would take into account all the relevant facts apart from those which were contrived. In doing so, that person would note that the funds used to make the loans in respect of which the interest was paid in this case did not emanate from the Appellant itself. He or she would also note that the loans were made in order to meet a genuine funding requirement on the part of the Appellant.

The relevant factors

46. That person would then note that, whilst the debtor was a UK resident company, the loans were not secured on assets situated in the United Kingdom and that there were numerous factors which pointed toward a non-UK source. Those factors were:

(1) the creditor at the time when the interest was paid was not UK resident;

(2) the loan could be enforced only in a jurisdiction outside the United Kingdom;

(3) payments of interest and principal were required to be made outside the United Kingdom; and

(4) the law governing the loan agreement was the law of a jurisdiction outside the United Kingdom.

47. Mr Way submitted that the significance of the residence of the debtor as a factor to be taken into account in the determination of source was significantly reduced in circumstances, such as those in the present case, where the loan agreement had an exclusive jurisdiction clause. This was because the creditor would not sue in the United Kingdom if it wished to enforce the relevant loan. In his view, the residence of the debtor was a relevant factor in many cases principally only because that was the place where the debt would be enforced. If, by contrast, there was an exclusive jurisdiction clause, the residence of the debtor was much less significant.

48. In contrast, the factors mentioned in paragraphs 46(1) to 46(4) above all pointed toward a non-UK source and, with the possible exception of the governing law – which he accepted had little significance – those factors were material. In particular, the fact that a non-UK resident was the creditor at the time when the interest was paid was a highly significant factor. He referred to the decision in *Philips* as supporting the proposition that the place where the credit giving rise to the debt had been provided was an important factor to be taken into account.

Conclusion

Introduction

49. I agree with Mr Way that the test to determine source is multi-factorial in nature and that, as the loans in this case arose from commercial transactions, the source of the interest is to be identified by what the practical person would regard as "the underlying commercial reality". However, I do not agree with his submissions on the weight to be attached to the various factors in this context or what the practical person would have considered "the underlying commercial reality" to be. It seems to me that his analysis in that regard is not consistent with the judgments in *Bank of Greece* or the *Ardmore Cases* as set out in paragraphs 28 to 43 above. In my view, for the reasons which follow, the practical person would consider "the underlying commercial reality" in this case to be that the interest had a UK source.

The various factors

50. I would start by noting that the only relevant factors which point to a non-UK source for the interest are that:

(1) payments under the loans were required to be made outside the United Kingdom;

(2) any proceedings to enforce the debts were required to be brought in a jurisdiction outside the United Kingdom; and

(3) the loan agreements were governed by the laws of a jurisdiction outside the United Kingdom.

51. For reasons to which I will shortly revert, I do not accept that any weight should be attached to the non-UK residence of the creditor at the time when the interest was paid.

52. The first two of the factors referred to in paragraph 50 above are in my view outweighed by the fact that the debtor – i.e. the Appellant - was a UK resident company and carried on its business exclusively in the United Kingdom. This meant that, regardless of the fact that the interest payments were required to be made outside the United Kingdom, those interest payments were necessarily funded out of assets situated in, and the profits of activities conducted in, the United Kingdom. It also meant that, even though any proceedings in relation to the debt would have had to be taken in a jurisdiction outside the United Kingdom, any judgment obtained pursuant to those proceedings would necessarily have had to be enforced against assets situated in, and the profits of activities conducted in, the United Kingdom. In my view, therefore, the commercial substance of the arrangements – "the underlying commercial reality", as it were - was that this interest was always going to be paid by a UK resident debtor out of its assets situated in, and the profits of activities conducted in, the United Kingdom. The provisions described in paragraphs 50(1) and 50(2) above could never negate or detract from that "underlying commercial reality". In this respect, the facts in the present case are similar to the situation pertaining in *Bank of Greece*, where the coupons were paid through paying agents in London or in Greece by cheque drawn on London but the funds to pay the interest had to be remitted from Greece to London. In *Bank of Greece*, it was the fact that the interest ultimately came from Greece that mattered more than the fact that the interest would physically be paid in London and the same principle applies in this case to render the foreign payment and enforcement requirements of little relevance.

53. As regards the third factor referred to in paragraph 50 above, I agree with Mr Way that very little weight should be attached to it.

54. Support for the conclusion I have reached above is to be found in the *Ardmore Cases*. With the exception of the fact that the funding for the loans in the *Ardmore Cases* started in the United Kingdom, the disposition of the factors in those cases was virtually identical to the disposition of the factors in the present case. In both cases, the debtor was resident in the United Kingdom, the obligations under each loan were to be discharged out of assets located in the United Kingdom and the relevant loan, if it were to be enforced, would ultimately have had to be enforced against assets located in the United Kingdom. Similarly, in both cases, the provisions of the relevant loan agreement required that the payments of interest would be made outside the United Kingdom, that the loan would be governed exclusively by the laws of a jurisdiction outside the United Kingdom and that the loan could be enforced only in that jurisdiction. The conclusion of the litigation in the *Ardmore Cases* was that, based on that disposition of factors, the interest in question had a UK source. In effect, the Upper Tribunal and Court of Appeal considered that the factors to which the greatest weight should be accorded - the residence of the debtor, the location of the assets out of which the interest would be paid and the location of the assets against which any judgment would be enforced – all pointed toward the United Kingdom and very little, if any, weight should be accorded to the factors which pointed away from the United Kingdom – the provisions stipulating where the interest payments should be made and the governing law and exclusive jurisdiction clauses.

55. I do not see any meaningful distinction between the facts of the *Ardmore Cases* and the facts in this case in those respects.

The relevance of the location of the creditor

56. Mr Way sought to distinguish this case from the *Ardmore Cases* by saying that, in the *Ardmore Cases*, "the underlying commercial reality" was that the funds which had been used to make the relevant loans had initially derived from the United Kingdom. He explained that, in the *Ardmore Cases*, the flow of funds from Ardmore to the two companies incorporated in the British Virgin Islands and from those companies to the two Gibraltar trusts, before being

lent by the trusts back to Ardmore, meant that "the underlying commercial reality" in the *Ardmore Cases* was that the funding for the loans in respect of which the interest was paid ultimately came from Ardmore in the United Kingdom. In contrast, he said, "the underlying commercial reality" in this case was that the funding for the loans in respect of which the interest was paid ultimately came from Storrier, a non-UK resident company acting from outside the United Kingdom, or the relevant Guernsey Trust, a trust which was managed outside the United Kingdom, because it was Storrier or the relevant Guernsey Trust which was the creditor of each loan at the time when the interest was paid.

57. I cannot accept that proposition, founded as it is on the basis that the residence of the creditor under the loans at the time when the interest was paid is of any relevance in determining the source of the interest. With respect to Mr Way, it seems to me that his argument in this respect is indistinguishable from the one he made unsuccessfully on behalf of Ardmore in the *Ardmore Cases*, to the effect that the residence of the creditor and the place where the loan is made has either determinative or material significance in determining the source of the interest payments made under the loan. Both the Upper Tribunal and the Court of Appeal in the *Ardmore Cases* were emphatic in their rejection of that proposition. In their view, source was to be determined by reference to the nature of the obligations which arose from the loan and the manner in which those obligations were discharged. It was not to be determined by reference to the circumstances giving rise to the loan – see *Ardmore CA* at paragraph [42]. Focusing on the source of the funding used to make the relevant loan is in my view no different from focusing on the residence of the creditor or the place where the credit was provided. In both cases, the focus is directed at the position of the creditor and the circumstances giving rise to the loan, as opposed to the nature of the obligations which arose from the making of the loan and the manner in which those obligations were discharged. The logic of the *Ardmore Cases* compels the conclusion that, in the determination of the source of interest payments under a loan, little or no weight is to be accorded to the derivation of the funds giving rise to the loan. Instead, factors such as the residence of the debtor and the location of the assets out of which the interest is discharged are the material factors to be taken into account and, in that regard, "the underlying commercial reality" in this case is identical to that in the *Ardmore Cases*. Thus, I believe that I am bound by the reasoning in *Ardmore CA* to reject Mr Way's proposition.

58. For completeness, I should add that, even if Mr Way were to be correct in saying that the source of the funds used to create each loan was a material factor to be taken into account in determining the source of the interest payments under the loan, it would in my view be the source of the funds for the original Lender which would be the relevant factor in this context and not the source of the funds used, in order to take an assignment of the loan after the loan was made, by the person who happened to be the creditor in respect of that loan at the time when the interest was paid.

59. This follows inexorably from the logic set out in both *Philips* and *Bank of Greece*. In *Philips*, the reason why the residence of the creditor and the place where the credit was provided could be a relevant factor in determining the source of an interest payment was because the original loan could be seen as the ultimate source of the eventual interest payment. Based on that logic, the fact that the relevant loan was assigned to a different creditor after it was made would not change the location of the original funding for the loan. A similar approach was adopted by Lord Hailsham in *Bank of Greece* – albeit, in that context, in relation to the obligor under the debt - where he held that it was the residence of the original debtor and the original guarantor which mattered in determining the source of the interest payments and not the residence of the entity which had assumed the obligation of the original debtor. Applying similar reasoning to that of Lord Hailsham in the case of the

creditor instead of the debtor, it would be the source of the funds used by the original Lender to make the advance which mattered and not the source of the funds used by a subsequent creditor to take an assignment of the loan after it was made and who happened to be the creditor at the time when the interest was paid.

60. In that regard, the Appellant has not provided any evidence to the effect that the source of the funds used by the original Lenders to make the loans in this case came from outside the United Kingdom. On the contrary, such evidence as has been presented to me suggests that a significant part of those funds ultimately derived from the United Kingdom and, in particular, from the business of the Appellant's group carried on in the United Kingdom. Certainly, most of the loans were made by UK resident individuals who were directors of, and shareholders in, the Appellant or from settlements created by such persons and it therefore seems likely that much of the funding that was used to make the loans will have originally have emanated from the Appellant by way of fees and dividends.

61. I would add that, even if the funding used by Storrier or the relevant Guernsey Trust to acquire the loans were to be of any relevance in this regard, in my view that funding was in any case derived by Storrier or the relevant Guernsey Trust from the Appellant in the United Kingdom because the circular flows of funds which took place on the occasion that each loan was assigned meant that Storrier or the relevant Guernsey Trust was reliant on the payments made to it by the Appellant shortly after it acquired each loan in order to finance its acquisition of the relevant loan from the original Lender. In his oral evidence at the hearing, JH accepted that, although Storrier was a lender to the Appellant in another context – the deep discount bond held by Storrier in the Appellant – the refinancing transactions themselves did not involve the provision of any new funding by Storrier to the Appellant and the same reasoning would apply in the case of the Guernsey Trusts.

Conclusion

62. For the reasons set out above, I have concluded that the interest in this case arose in the United Kingdom.

63. That conclusion means that it is necessary for me to address the question of whether the interest paid on the loans in this case was "yearly" interest.

YEARLY INTEREST

The law

Introduction

64. The most recent authority in relation to the definition of "yearly" interest is the Supreme Court decision in *The Commissioners for Her Majesty's Revenue and Customs v The Joint Administrators of Lehman Brothers International* [2019] STC 661 ("*Lehman*"). The issue in *Lehman* was whether statutory interest which became payable in respect of the surplus remaining after the payment of debts proved in a distributing administration was "yearly" or "short" in nature, the importance of the issue's being that, in the former case, the administrators were required to withhold income tax before paying the interest to creditors.

65. Statutory interest of the kind which was payable in *Lehman* differs from the interest which was payable on the loans in this case in that it did not accrue from day-to-day on a prospective basis over the period to which it related. Instead, it was payable as statutory compensation for the loss suffered by the creditors in being kept out of their money during the period of the administration (see *Lehman* at paragraphs [6] and [7]). The Supreme Court adverted to this difference in dividing its summary of the prior authorities into two – those addressing the question of whether interest which accrues over time is properly to be categorised as "yearly" and those addressing the question of whether an entitlement to money

described as interest, but which does not accrue over time, can properly be regarded as "yearly" interest, or indeed "interest" at all. Lehman was ultimately decided on the basis of the second group of cases but it is the first group of cases which is of primary relevance to the issue in the present appeal.

Identifying "yearly" interest

66. On the basis of the summary of that first group of cases by Lord Briggs in *Lehman*, the prior authorities have established the following principles in relation to the question of whether interest which accrues over time is properly to be categorised as "yearly":

(1) interest is not "yearly" merely because it is calculated by reference to a rate per annum – *Goslings and Sharpe v Blake (Surveyor of Taxes)* 2 TC 450 ("*Goslings*");

(2) interest can be "yearly" even if it is payable more than once a year – *Re Cooper* [1911] 2 KB 550 ("*Re Cooper*");

(3) interest on a debt which is expected to last for a year or more, or which is of a type that has the "propensity" to last for a year or more, is "yearly" interest – *Bebb v Bunny* [1854] 69 ER 436 ("*Bebb*");

(4) the expected or habitual duration of a debt as referred to in paragraph 66(3) above is to be established by way of a business-like assessment as opposed to a dry legal assessment of the terms of the document giving rise to the debt – *Goslings*;

(5) if a debt is expected to last for less than a year but, in the event, it lasts for a year or longer, that does not make the interest on that debt "yearly" – *Gateshead Corporation v Lumsden* [1914] 2 KB 883 ("*Gateshead*"); and

(6) in order for interest to be "yearly", the debt in respect of which it is paid must have a measure of permanence or a "tract of future time" and be in the nature of an investment – *Re Cooper*, *Garston Overseers v Carlisle (Surveyor of Taxes)* 6 TC 659 ("*Garston*") and *Scottish North American Trust Limited* 1910 Session Cases 966.

67. In *Inland Revenue Commissioners v Hay* 8 TC 636 ("*Hay*"), Lord Anderson in the Inner House (Second Division) of the Court of Session attempted to reduce the prior jurisprudence in this area to a concrete set of useful propositions as follows:

"Now the authorities referred to by Crown Counsel seem to me to establish these propositions, five in number: - (First), that interest payable in respect of a short loan is not yearly interest (Goslings …). … (Second) that in order that interest payable may be held to be yearly interest in the sense of the Income Tax Acts, the loan in respect of which interest is paid must have a measure of permanence. (Third), that the loan must be of the nature - and this is pretty well expressing the second proposition in another form - that the loan must be of the nature of an investment (Garston Overseers). (Fourth), That the loan must not be one repayable on demand (Gateshead Corpn …). And (fifth) that the loan must have a 'tract of future time' (per Lord Johnston in Scottish North American Trust Ltd, 1910 Session Cases 966, 973). These propositions are perhaps one proposition expressed in different forms, but they are the result of the authorities."

68. In *Lehman*, Lord Briggs said that the tests outlined by Lord Anderson "remain the best convenient summary of the jurisprudence about the meaning of yearly interest, in the context of interest which accrues due over time, whether purely contractual or statutory in origin."

69. Whilst that may be true, those tests cannot be applied slavishly for the simple reason that the various propositions are not always internally consistent. Lord Briggs referred in *Lehman* at paragraphs [32] and [33] to one such inconsistency, an inconsistency between, on the one hand, the second and fifth propositions and, on the other hand, the third proposition, as revealed by the decision in *Cairns v MacDiarmid* 56 TC 556 ("*Cairns*"). In *Cairns*, Sir John Donaldson MR said:

"I would personally wish to avoid the use of the term "investment" as providing any sort of test in the context of whether interest is annual interest…., because it is possible to have a short term and indeed a very short term investment, eg overnight deposits, and such an investment does not involve any annual interest, regardless of whether the interest is calculated at an annual rate."

70. In other words, interest on a loan which is a short-term investment and thus satisfies the third proposition will nevertheless not be "yearly" because the loan does not satisfy the second and fifth propositions (as it does not have a measure of permanence and does not have a "tract of future time"). Lord Briggs explained this anomaly in *Lehman* at paragraph [33] by reference to changes, over the period between the two cases, in what the financial world regards as an investment, as opposed to any change in the applicable principles.

71. However, the same explanation cannot be proffered for another inconsistency between the various propositions in *Hay* – that between, on the one hand, the second, third and fifth propositions and, on the other hand, the fourth proposition – and this inconsistency is of greater relevance to the present decision (albeit by way of an analogy). In other words, it is possible for a loan to be made on terms that it is technically repayable on demand but which the parties nevertheless intend and expect to last for a considerable period of time or which has a propensity to last for a considerable period of time, such that the loan has a measure of permanence, is in the nature of an investment and has a "tract of future time". In those circumstances, the prior case law shows that the interest on the loan is clearly "yearly" in nature. In effect, the position is indistinguishable from interest on a loan with a fixed repayment date falling within a year but which the parties intended and expected to last for a much longer period, such as the examples given in the cases of *Bebb* and *Goslings*.

72. Indeed, Lord Denning MR referred expressly to this anomaly when he said the following in *Corinthian Securities Limited v Cato* [1970] 1 QB 377 and 382-383 ("*Cato*"):

"Interest is "yearly interest of money" whenever it is paid on a loan which is in the nature of an investment no matter whether it is repayable on demand or not….Looking at the agreement in this case, it is plain to me that this loan was made as an investment. Although payable on demand, it was unlikely that any demand would be made so long as the interest payments were kept up. It was a loan on the security of property, indistinguishable in principle from an ordinary loan or mortgage. The interest was "yearly interest of money"."

The arguments of the Appellant

The long-term loans

73. Mr Way accepted that the interest which was paid on certain of the loans – those where the period between the making of the advance and the date of repayment was well in excess of a year – was "yearly" in nature. By reference to the table set out in paragraph 17 above, that comprised the interest paid on loans numbered 3, 4, 5, 6, 9, 10, 11, 12,15, 42 and 46. However, he submitted that the remaining interest was "short" in nature, as it was payable on loans which had a period between the date of the advance and the date of repayment of either less than a year or just a little over a year.

Reasons why the remaining interest was "short"

74. His starting point in this regard was that the loans arose as a result of the annual funding review which was conducted at the end of each year by NA and RA. He said that this, together with the fact that the Lender could call for repayment on short notice and that each loan had in fact lasted for less than, or only just a little over, a year, showed that each loan was always intended to be short-term funding. It lacked the requisite propensity to run for more than a year which had been noted as a requirement for "yearly' interest by Lord Briggs in *Lehman* at paragraph [22] in his summary of the decision in *Bebb*. (In this respect, he regarded loans which remained outstanding for a little more than a year as being indistinguishable from loans which remained outstanding for less than a year. In both cases, he said, the intention was that

the loans would be outstanding for only a short period and it did not matter that, in some cases, the parties had inadvertently allowed the funding to continue to a date which fell slightly after the first anniversary of the date of the advance.)

75. Mr Way said that, adopting the business-like approach required by *Goslings*, the facts showed that these loans were not intended to last for more than a year and lacked the characteristics noted by Lord Anderson in *Hay* to be necessary to give rise to "yearly" interest. Applying the first *Hay* test, the loans were short, applying the second *Hay* test, the loans lacked a measure of permanence, applying the third *Hay* test, the loans were not in the nature of an investment for the relevant Lender, applying the fourth *Hay* test, the loans were repayable on demand, and, applying the fifth Hay test, the loans did not have "a tract of future time".

76. He added that the pre-eminent test in this regard was the third *Hay* test, as noted by Lord Denning MR in the extract from *Cato* which I have set out in paragraph 72 above. In this case, each loan in question was merely a temporary financial accommodation to assist the Appellant to meet its funding needs over the year in question. It was not intended to be an investment by the relevant Lender. This conclusion was supported by the fact that each loan was unsecured and was not made by a commercial institution such as a bank. There was a very real credit risk for the relevant Lender which meant that the Lender would not want the monies to be outstanding for a long time. The Lenders wanted quick and easy access to their funds and that was what the loans provided.

Recharacterisation

77. Mr Way said that the Respondents' approach in this case necessarily involved disregarding the distinct nature of each loan made by a particular Lender as a separate and distinct provision of funding from each of the other loans made by the same Lender. This, he said, was contrary to the decision in *MacNiven (HM Inspector of Taxes) v Westmoreland Investments Limited* [2001] UKHL 6 ("*Westmoreland*"). In *Westmoreland*, the House of Lords rejected the proposition made by the Respondents in that case that there had been no payments of accrued interest simply because the payments had been funded out of new advances from the same lender and the transaction had been effected for tax purposes.

Conclusion

The facts

78. I agree with Mr Way that the loans in this case fulfilled an important commercial need for the Appellant. As noted by JH in his evidence at the hearing, they were unsecured, thereby leaving the assets of the Appellant unencumbered and available to stand as security for other financing raised by the Appellant – such as that from unrelated parties like banks. In addition, as the Lenders were connected to the Appellant, the loans could be documented easily and did not involve any of the usual front-end costs or arrangement fees that the Appellant needed to incur in raising finance from its institutional lenders. It could thus be raised quickly and at minimal cost.

79. Determining the purpose of the Appellant and the relevant Lender in entering into each loan is a question of fact. In considering that question in relation to the loans which the Appellant alleges to have given rise to "short" interest in this case, I have taken into account the fact that each such loan was repayable on demand and was in fact repaid within, or very shortly after, the period of a year from the date when it was advanced. However, I am mindful of the injunction in *Goslings* to adopt a business-like approach instead of a dry legal assessment of the documents when it comes to determining the purpose of the parties to a loan. In the words of the Special Commissioner in *Minsham Properties v Price (Inspector of Taxes) and related appeal* [1990] STC 718 ("*Minsham*"), in a passage set out on page 723 which was cited

with approval by Vinelott J in that case, this involves "standing back and taking an objective view". When I do that in this case, I am forced to the conclusion that, despite the regular annual repayments of the loans made by each Lender, the loans made by that Lender were intended to form part of the longer-term funding of the Appellant and were regarded by that Lender as an investment in the Appellant, albeit an unsecured investment.

80. The starting point in the analysis is the observation that a key feature of the commercial dynamic was that, as JH testified, a property company which develops property for retention as an investment and has an expanding portfolio has an increasing demand for funding year by year. Unlike a property trader, which is able to finance future acquisitions out of the proceeds of regular sales, a property company which carries on an investment activity is reliant on external funding in order to fund its growth.

81. The obvious candidates to provide part of that finance were the Lenders – persons connected with the Appellant who were prepared to invest their surplus funds in the business without the need for security over any of the assets, complicated loan documentation or expensive arrangement fees. The evidence shows that the funding provided by the Lenders to the Appellant was an important part of the capital of the business. Far from representing a short-term accommodation to the company, each loan in this case was part of a sequence which represented the provision by the relevant Lender of part of the fixed capital of the business. That explains why, as JH explained at the hearing, the pattern was for the repayment of each loan to be funded out of the proceeds of a new advance from the same Lender.

82. The evidence of JH in this respect is confirmed when one looks at the table set out in paragraph 17 above. When one looks at the date of the advance and the date of repayment for each loan listed in that table, it becomes apparent that, ignoring the very occasional minimal gap, each Lender made a continuous provision of finance to the Appellant over a lengthy period. Moreover, the amount provided by each Lender to the Appellant tended to grow over the period in which the finance was provided because later loans were often used to pay off the accrued interest on the preceding loan as well as the principal on that loan. That is not to say that the principal amount of the monies outstanding to each Lender was always rising. There was the odd case where the principal amount owing to a particular Lender reduced following the implementation of the refinancing structure. However, the general trend was upward and, in any event, the key feature of this in my view is that the financing from each Lender had a permanency which belied the apparent short-term nature of each loan made by that Lender.

83. By way of example, starting with the loans made by the RAS, the first relevant loan to consider is loan number 2 of £9,500,000, which was advanced on 9 December 2009, a day after the repayment of loan number 1 in the same amount. That loan was repaid on 1 December 2010 but the same amount was then advanced to the Appellant on the same day (loan numbers 3 and 4). Similar points can be made about the repayment of loan numbers 3 and 4 and the advance of loans numbers 5 and 6 although the Appellant has already accepted that the interest paid on loan numbers 3, 4, 5 and 6 was "yearly" in nature. It can therefore be seen that, leaving aside the one-day gap on 8 and 9 December 2009, the RAS provided finance to the Appellant of at least £9,500,000 continuously from 2 April 2009 (when loan number 1 was made) through to 17 March 2015, when loan numbers 5 and 6 were repaid.

84. Precisely the same point can be made in relation to the finance which was provided to the Appellant by the NAS. This time, it was loan number 8 of £9,000,000 which was advanced on 10 December 2009, the day after loan number 7 in the same amount was repaid, and then that was followed by loan numbers 9 and 10, which were advanced on 1 December 2010, the same day as loan number 8 was repaid. Again, the loan profile shows that, leaving aside the

one-day gap on 9 and 10 December 2009, the NAS lent £9,000,000 to the Appellant between 1 April 2009 and 15 March 2013, approximately £13,500,000 between 15 March 2013 and 19 March 2013 and approximately £10,500,000 between 19 March 2013 and 17 March 2015.

85. Similar points can be made in relation to the loans to the Appellant from each of:

(1) the FURBS – finance provided by way of loan numbers 13 to 17 from 31 March 2009 to 18 March 2014;

(2) RA - finance provided by way of loan numbers 18 to 23 from 1 April 2009 to 13 March 2014;

(3) CL - finance provided by way of loan numbers 24 to 29 from 8 April 2009 to 13 March 2014;

(4) JH - finance provided by way of loan numbers 30 to 35 from 31 March 2009 to 13 March 2014;

(5) NA - finance provided by way of loan numbers 36 to 41 from 1 April 2009 to 13 March 2014;

(6) RUA - finance provided by way of loan numbers 42 to 45 from 23 December 2004 to 13 March 2014; and

(7) the RUA2 - finance provided by way of loan numbers 46 and 47 from 25 December 2009 to 13 March 2014.

86. In the circumstances, notwithstanding the short-term nature of each individual loan, `I consider that the only reasonable conclusion to draw from the facts is that, in practice, this funding was not temporary in nature but was instead part of the long-term funding of the Appellant. That is not to say that the funding could not easily have been brought to an end at short notice if that was what a particular Lender required. But the evidence suggests that that was not how each Lender viewed the loans. Instead, it suggests that each Lender saw the loans which it made to the Appellant as being part of the Lender's long-term capital in the Appellant's business and therefore in the nature of investments in the Appellant. Despite the fact that each individual loan was short-term in nature, the loans in this case "were something akin to long term or permanent finance" provided by persons connected with the borrowing company, as was the position in *Minsham*, which was also a case involving a property company (see the decision of the Special Commissioner in that case at page 723).

87. In reaching this conclusion, I have taken into account the fact that there was, on each occasion that the refinancing structure was implemented, an enquiry of the relevant Lender as to whether or not the Lender wished to continue providing funds to the Appellant, an example of which is recorded in paragraph 16(14) above. However, that enquiry was a formality, as JH and RA candidly admitted in their evidence and I have recorded in paragraph 16(16) above. The structure compelled each loan to be assigned before the interest was paid in order to ensure that the Lender received a payment for the accrued interest in a form which was intended to be capital in nature. The structure also compelled each loan to be repaid after it had been outstanding for around a year, in order to ensure that the interest on the loan could be said to be "short" (because the imposition of a withholding tax would have defeated the purpose of avoiding tax in the Lender's hands in respect of the interest). Those two requirements, taken together, led inexorably to a structure in which a loan was assigned and then immediately repaid. However, the repayment had to be funded. Theoretically, the funding for a repayment could have come from someone other than the same Lender. But that was never going to happen because the Lender was perfectly content to continue to fund the company, as I have concluded above. JH and RA confirmed as much in the evidence recorded in paragraph 16(16) above. In

my view, therefore, the enquiry which was made of each Lender on each occasion that the refinancing structure was implemented does not disturb the conclusion which I have reached above.

The conclusion of law

88. The finding of fact set out in paragraphs 79 to 87 above leads inexorably to the conclusion that, on the basis of the law as described in paragraphs 64 to 72 above, all of the interest in this case was "yearly" in nature. In particular, the loans made by each Lender satisfied the *Hay* tests relating to a measure of permanence, a "tract of future time" and being in the nature of an investment. I say that because, although each individual loan was short-term in nature, the loans provided by each Lender, when taken together, provided financing to the Appellant with a measure of permanence which had a "tract of future time" and that financing was in the nature of an investment for the Lender in question.

Final points

89. There are three final points which I should make in bringing this section of the decision to a close.

90. The first is that, in reaching the conclusion that the loans in this case were long-term investments in the Appellant, I am not saying that the fact that each loan was technically repaid in the short-term can be disregarded simply because the repayment was made out of the proceeds of another loan by the same Lender. In other words, I am not seeking to recharacterise, as one single long-term loan, the multiple consecutive loans which were made by each Lender. I am perfectly content to recognise the independent existence of each loan from the other loans made by the same Lender which preceded or succeeded that loan. Thus, I am not reaching a conclusion which is in any way inconsistent with the decision in *Westmoreland*. However, the fact that each loan had an independent existence and was repaid after a period of approximately one year does not mean that each loan should be viewed in isolation and with blinkers when the question of whether or not it was intended to comprise part of the long-term funding of the Appellant – and, hence, whether it gave rise to "yearly" interest - falls to be addressed. Instead, that loan needs to be examined in context and in the light of all the circumstances in which it was advanced and repaid. And, once one does that, the long-term nature of the relevant funding becomes apparent.

91. The second is that, in my view, although it has added some complexity to the facts which I am considering in this context, in answering this question, nothing turns on the various transactions comprising the refinancing structure which occurred each year. Although there might have been one or two days when a loan was owed to Storrier or a Guernsey Trust instead of a Lender and although that Lender made the new loan out of the proceeds of the assignment to Storrier or a Guernsey Trust as opposed to the proceeds of repayment, that doesn't change the essence of the arrangement from the commercial perspective. The steps involved in the refinancing structure were there to achieve a particular tax advantage but they didn't change the fact that the Appellant had a need for long-term funding from the Lenders and the Lenders were prepared to provide that funding in the form of the various consecutive loans. Accordingly, in my view, those steps have no relevance in considering this issue.

92. Finally, I should say that, even if the conclusion which I have reached on this issue were to be wrong, I do not agree with Mr Way that the category of loans giving rise to "short" interest should include not only those loans where the period between the date of the advance and the date of repayment was less than a year but also those loans where the period between the date of the advance and the date of repayment was slightly more than a year. The case law cited above shows that a loan which is intended, or has a propensity, to last for a year or more gives rise to "yearly" interest and that is the case even if that intended or habitual period is only just

over a year instead of a much longer period. The paramount importance of the one-year threshold can be seen not only in the use of the word "yearly" but also in the authorities. For example, even though the decision in *Lehman* was ultimately based on the prior case law in relation to interest which did not accrue due over time (such as statutory interest), unlike the loans in this case, the conclusion reached by Lord Briggs in that case was that that interest was "yearly" if the period over which it was calculated was a year or more.

93. Of course, that is not the same as saying that a loan which is intended, or has a propensity, to last for less than a year generates "yearly" interest simply because, through an oversight, it lasts for slightly longer than the intended or habitual period. But the Appellant has produced no evidence in the present case to demonstrate that the loans which were repaid in a little over a year were intended to be repaid earlier but remained outstanding through oversight. The facts of the present case are that there have been multiple loans, some of which have been repaid within a year of being advanced and others of which have been repaid after a year or more, in some cases well after the expiry of a year. On those facts, I can see no basis for assuming that those loans which happen to have been repaid very shortly after the first anniversary of their advance must have been intended to last for less than a year but were inadvertently allowed to run on for a brief period.

94. Accordingly, even if I were to be wrong in saying that each of the loans in this case gave rise to "yearly" interest, I would conclude that the category of loans which on their terms gave rise to "yearly" interest should include loan numbers 16, 17, 21, 23, 27, 29, 33, 35, 39, 41,43, 45 and 47.

THE GUERNSEY TREATY

The law

The Guernsey Treaty

95. The United Kingdom has entered into various double tax treaties pursuant to the provision which is now Section 6 of the TIOPA. That section provides that double tax treaties are to have effect in relation to income tax so far as the treaties provide, inter alia, for relief from income tax (Section 6(2)(a) of the TIOPA), for determining the income to be attributed to non-UK resident persons (Section 6(2)(d) of the TIOPA) and for determining the income to be attributed to establishments in the United Kingdom of non-UK resident persons (Section 6(2)(e) of the TIOPA).

96. The United Kingdom entered into the Guernsey Treaty in 1952 pursuant to a predecessor of Section 6 of the TIOPA. That treaty was still in force throughout the period in which the interest which is the subject of this appeal was paid. Paragraph 3(2) of the treaty, which is set out in paragraph 10 above, provided that the "industrial or commercial profits" of a Guernsey resident not engaged in a trade or business in the United Kingdom through a permanent establishment situated therein were not to be subject to UK tax. Although paragraph 6(5) of the Guernsey Treaty provided that items of income dealt with separately in other paragraphs of the treaty would not be affected by the terms of paragraph 3 of the treaty, it is common ground that the Guernsey Treaty contained no separate "Interest" article and that therefore the paragraph was capable of applying to interest in circumstances where that interest formed part of the "industrial or commercial profits" of a Guernsey resident company.

The DTR Regulations

97. Under the provision which is now Section 7 of the TIOPA, the Commissioners for the Respondents are empowered to make regulations for carrying out the provisions of the treaties into which the United Kingdom enters. One such set of regulations is the DTR Regulations, which make provision in relation to payments of interest by a UK resident borrower to a person resident in a jurisdiction with which the United Kingdom has concluded a treaty. The DTR

Regulations provide that, where a direction is given to that effect to a UK resident borrower by the Respondents under the regulations, the borrower is not obliged to withhold and account for tax in respect of the interest payments which it makes to a specified treaty resident.

The arguments of the Appellant

The Guernsey Treaty

98. Mr Way submitted that, as Storrier was a Guernsey resident company carrying on a financial trade, the interest which Storrier received from the Appellant following the assignment by a Lender fell squarely within the ambit of paragraph 3(2) of the Guernsey Treaty, as it formed part of the "industrial or commercial profits" of Storrier. He added that, in this respect, Storrier was in the same position as a bank resident in Guernsey and that, at the relevant time, the Respondents' International Manual at INTM 355225 (now archived) confirmed, in the context of the identically-worded provision in the double tax treaty between the United Kingdom and Jersey, that Jersey resident banks were entitled to the benefit of that language in respect of the interest which they received.

99. He added that there was no need for Storrier to have made a claim in order to benefit from the paragraph. It was true that Section 6(6) of the TIOPA required a claim to be made before reliance could be placed on a treaty provision conferring a relief from UK income tax and entered into pursuant to Section 6(2)(a) of the TIOPA but, he said, paragraph 3(2) of the Guernsey Treaty was not such a provision. Instead, it was a treaty provision which determined the income to be attributed to a Guernsey resident or a permanent establishment of a Guernsey resident and therefore fell within Sections 6(2)(d) and 6(2)(e) of the TIOPA. Similarly, the provisions in Section 19 of the TIOPA dealing with claims for relief from tax had no relevance in this context because they related to double tax relief – relief from UK tax under Section 18 of the TIOPA in respect of taxes paid outside the United Kingdom.

100. As regards whether or not Storrier was obliged to make a claim in order to benefit from the paragraph, Mr Way referred me to the decision of the Upper Tribunal in *Davies and others v The Commissioners for Her Majesty's Revenue and Customs* [2020] UKUT 0067 (TCC) ("*Davies*"). In that case, a Mauritian company was in receipt of profits arising from its activities in the United Kingdom and those profits fell within the scope of the "Business Profits" article of the double tax treaty between the United Kingdom and Mauritius. Under anti-avoidance provisions in the UK tax legislation, certain UK resident individuals were subject to UK tax on deemed income which was calculated by reference to the profits of the Mauritian company. The individuals in question failed in their attempt to rely on the article in the treaty to avoid their liabilities to UK tax on that deemed income. The Upper Tribunal held that the individuals were not entitled to rely on the article and that, in any event, if they had been so entitled, they would have had to have made a claim in order to benefit from the article. Mr Way said that *Davies* could be distinguished from the present case in two crucial respects, as follows:

(1) first, *Davies* was dealing with the ability of UK residents to rely on the treaty to avoid a tax liability on their own income (albeit calculated by reference to the profits of the treaty-resident company) whereas this case concerned the ability of the treaty resident company itself to rely on the treaty in order to avoid suffering withholding tax on its own income; and

(2) secondly, in *Davies*, the Upper Tribunal's conclusion to the effect that a claim would have had to be made by the UK residents in order for them to benefit from the treaty related to the UK residents and not the treaty resident company, whereas this case concerned whether or not the treaty resident company could rely on the treaty without having made a claim.

101. Since Storrier was entitled to the benefit of paragraph 3(2) of the Guernsey Treaty without having made a claim to that effect, Storrier was entitled to receive the interest which was paid to it by the Appellant without suffering withholding tax on that interest even if that interest arose in the United Kingdom and was "yearly" interest. Otherwise, Storrier would effectively be suffering income tax in respect of the interest and that was contrary to its entitlement under the paragraph.

The DTR Regulations

102. Moreover, the Appellant was entitled to make gross payment of the interest even though it had not received a direction from the Respondents to do so pursuant to the DTR Regulations in advance of making the payments. This was because there was no obligation for a borrower to receive a direction under the DTR Regulations before relying on a double tax treaty provision to negate a withholding tax obligation. The language in the DTR Regulations was permissive and not compulsory, as was shown by the use of the phrase "may be directed by a notice" in paragraph 2(2) of the regulations. Whilst it was common practice for borrowers to obtain a direction from the Respondents pursuant to the regulations before making gross payments of interest under a treaty, it was by no means essential and was just one way of benefitting from relief under the treaty. Moreover, the practice of obtaining an advance direction to make gross payment generally occurred in the context of the "Interest" article in a treaty and not the "Business Profits" article in that treaty, and it was the latter which was the equivalent of paragraph 3(2) of the Guernsey Treaty.

Conclusion

Storrier's ability to rely on the Guernsey Treaty

103. At the hearing, both parties spent some time in addressing the issue of whether Storrier was entitled to the benefit of paragraph 3(2) of the Guernsey Treaty in relation to the interest which it received on the loans. This involved answering two distinct questions, as follows:

(1) the first was whether the interest fell within the language set out in paragraph 3(2) of the Guernsey Treaty – in other words, did the interest in question fall within the "industrial or commercial profits" of Storrier; and

(2) the second was whether, even if the interest did fall within the ambit of that paragraph, Storrier needed to have submitted a claim to the Respondents in order to benefit from relief pursuant to the provision.

104. For reasons which will become clear, I do not think that whether Storrier was entitled to the benefit of paragraph 3(2) of the Guernsey Treaty in relation to the interest which it received on the loans is determinative of the question of whether the Appellant was entitled to make gross payment of the relevant interest to Storrier. Accordingly, I do not propose to deal with either of those questions in this decision. Instead, I propose to assume for present purposes that Storrier was entitled to the benefit of the paragraph in relation to all of the interest which it received from the Appellant.

The Appellant's ability to rely on the Guernsey Treaty

105. In my view, even if Storrier was so entitled, that did not mean that the Appellant was entitled to make gross payment of the interest to Storrier.

106. I say that because the tax to which this appeal relates was not a tax liability of Storrier at all. Instead, it was a tax liability of the Appellant. The obligation to withhold and account for tax was an obligation placed on the Appellant by Section 874 of the ITA and, unless it is possible to conclude that other provisions in the UK tax legislation operated in such a way as to remove that obligation, it was one with which the Appellant was required to comply.

107. In saying that the withholding tax liability was a liability of the Appellant and not of Storrier, I have taken into account the following passage in the decision of the Upper Tribunal in *Ardmore UT* at paragraph [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."

108. The Upper Tribunal then went on in paragraphs [21] and [22] of *Ardmore UT* to give examples of the integrated relationship between the deduction of tax at source and the recipient's tax liability.

109. I accept that, as a matter of tax policy, it makes sense to link the circumstances in which tax is required to be withheld from a payment of income and the circumstances in which the recipient is subject to tax on that income. For example, the fact that non-UK residents are generally not subject to UK tax in respect of their non-UK source income may explain why the obligation under Section 874 of the ITA is expressed to be confined to interest arising in the United Kingdom. Similarly, if tax which should have been withheld has not been withheld, it makes sense as a matter of tax policy to seek to recover that tax from the recipient by way of assessment, if possible. This approach can be seen in operation in Section 7(4) of the TIOPA and paragraph 9 of the DTR Regulations, the latter of which stipulates that, if, after a direction has been given under those regulations to make gross payment, it transpires that the recipient was not entitled to relief under the applicable treaty, the tax for which the payer should have accounted may be assessed on the recipient or may be directed to be deducted from future payments made by the payer to that recipient.

110. However, the mere fact that a link between the liability to withhold and the liability to tax of the recipient exists as a matter of tax policy does not mean that the liability to account for the withholding tax is a tax liability of the recipient of the payment. In that respect, I believe that the Upper Tribunal in *Ardmore UT* over-stated the position. As Lord Briggs noted in *Lehman* at paragraph [57]:

> "…the obligation to deduct tax from interest under s 874 does not depend at all upon the question whether the interest is taxable in the hands of the recipient. If the payment is yearly interest, and the payers (or the circumstances) qualify, for example because the payer is a company, or the usual place of abode of the recipient is offshore, then tax must be deducted."

111. It follows from the above that, even if Storrier was entitled to rely on paragraph 3(2) of the Guernsey Treaty to avoid paying tax by way of assessment on the interest income in this case, that did not mean, in and of itself, that the Appellant had no obligation to withhold and account for tax when it paid the interest. In order for the Appellant itself to have been able to rely on the paragraph to negate the obligation to withhold and account for tax, it would need to have established that the paragraph applied to relieve it from that obligation.

112. There are two reasons why I consider that that is not the case.

113. The first is that the Appellant has made no claim to that effect and the second is that the Appellant did not receive a direction to that effect under the DTR Regulations.

The need for a claim

114. The question of whether the Appellant needed to make a claim before it was able to rely on the terms of the paragraph to be relieved from the obligation to withhold and account for tax turns on whether it was seeking to rely on the paragraph in order to obtain relief from UK tax (and thus fell within Section 6(2)(a) of the TIOPA) or was instead seeking to rely on

the paragraph to determine the profits to be attributed to Storrier or to a permanent establishment of Storrier (and thus fell within Section 6(2)(d) or 6(2)(e) of the TIOPA).

115. Mr Way submitted that the latter was the case because the paragraph was dealing with the identification of which profits (if any) of Storrier could be subjected to UK tax. In contrast, Mr Vallat submitted that the language used in the opening part of paragraph 3(2) – "shall not be subject to United Kingdom tax" - made it clear that the former was the case because the Appellant was seeking to be relieved from an obligation to withhold and account for tax.

116. I have concluded that Mr Vallat is right on this point.

117. As a matter of UK domestic law, before taking into account the terms of the Guernsey Treaty, the Appellant had an obligation to withhold and account for tax. The Guernsey Treaty was capable of overriding that obligation because it formed part of UK domestic law and it was stated to "have effect…despite anything in any enactment" (see Section 6(1) of the TIOPA). However, by relying on the paragraph to override its obligation to withhold and account for UK tax, the Appellant was seeking a relief from the UK tax which the Appellant would otherwise have been required to withhold (and for which the Appellant would otherwise have been required to account). This means that, in my view, the Appellant's claim falls within Section 6(2)(a) of the TIOPA and its ability to rely on the paragraph is dependent on its having made a claim to that effect, pursuant to Section 6(6) of the TIOPA.

118. No such claim has been made by the Appellant in the present case and the time limit for making any such claim has expired.

119. The Appellant can hardly say that the language of the paragraph is apt to relieve it from the obligation to withhold and account for tax without accepting that, in applying in that manner, the paragraph is having effect to provide a relief from UK tax falling within Section 6(2)(a) of the TIOPA – namely, a relief from the Appellant's obligation to withhold and account for tax. And, as any relief from UK tax pursuant to that provision is contingent on a claim because of the requirement in Section 6(6) of the TIOPA, the absence of any claim to that effect by the Appellant in this case means that the obligation to withhold remains.

Davies

120. In passing, I would say that the above conclusion is entirely consistent with the decision of the Upper Tribunal in *Davies*. The main question at issue in *Davies* was different from the question at issue in this case in that the Upper Tribunal there had to deal with the issue of whether the UK resident appellants, who were deemed under UK law to derive income equal to the profits of a Mauritian company, were entitled to rely on the terms of the "Business Profits" article in the double tax treaty between the United Kingdom and Mauritius to avoid UK tax on that income. The Upper Tribunal held that the appellants could not do so because the deemed income of the UK residents was merely computed by reference to the profits of the Mauritian company. The appellants' deemed income was different from those profits. Since the article in the double tax treaty applied only to the profits of the Mauritian company and not to the deemed income derived by the appellants, the appellants could not rely on the article in question (see paragraph [78] of the decision). That part of the decision is distinguishable in relation to the present facts because, here, the income which is being addressed is the same income as that to which the paragraph in the treaty relates – namely, the interest income paid to the Guernsey resident recipient. In that respect, the two situations are entirely separate and distinct.

121. However, of greater relevance to the present context is the statement made by the Upper Tribunal in *Davies* to the effect that, if the appellants had been entitled to rely on the

article to avoid liability to UK tax on the profits in question, then they would have needed to make a claim for relief under the article pursuant to what is now Section 6(6) of the TIOPA (see paragraph [84] in the decision). That statement is entirely on all fours with my conclusion in paragraphs 114 to 119 above to the effect that the Appellant's ability to rely on the relevant treaty provision was dependent on its having made a claim to that effect. The appellants in that case were relying on the relevant article to claim that the income in question was not to be subject to UK tax – a claim which the Upper Tribunal said, in paragraph [84] of its decision, did not involve arguing that the relevant article determined the income to be attributed to them for the purposes of what is now Sections 6(2)(d) and 6(2)(e) of the TIOPA. Similarly, in this case, the Appellant is seeking to rely on paragraph 3(2) of the Guernsey Treaty to claim that its obligation to withhold and account for UK tax has been negated and it does not involve arguing that the paragraph determined the income to be attributed to the Appellant or a permanent establishment of the Appellant.

122. In short, although the central issue in *Davies* was whether UK residents were entitled to benefit from a treaty provision precluding the United Kingdom from taxing the specified profits of a treaty-resident company in relation to income of the UK residents which was different from, and merely calculated by reference to, those profits – which is a different issue from the one which I am here addressing - the dicta to the effect that, if they had been so entitled, their entitlement would have been subject to their having made a claim to that effect is relevant in the present circumstances and the conclusion I have reached in paragraphs 114 to 119 above is entirely consistent with the conclusion on the similar point in *Davies*.

Construction of the DTR Regulations

123. The second reason for reaching the above conclusion is that, in my view, even if the Appellant had made a claim pursuant to Section 6(6) of the TIOPA for relief from the obligation to withhold and account for tax, the language used in the DTR Regulations makes it plain that the obligation under Section 874 of the ITA to withhold tax from a payment of interest can be overridden only where the payer of the interest receives a direction to that effect from the Respondents. In that regard, I do not agree with Mr Way's proposition to the effect that the DTR Regulations are effectively voluntary and that a payer of interest can make gross payment of the interest in reliance on the terms of an applicable double tax treaty even in the absence of a direction under the DTR Regulations.

124. In my view, the only circumstance in which gross payment of interest under the terms of a treaty is permitted is where a direction to that effect has been given to the payer under the terms of the DTR Regulations. In that regard, the use of the word "may" in paragraph 2(2) of the DTR Regulations is doing no more than saying that the Respondents have the power to give a direction under the regulations. It is not saying that gross payment may be made even in circumstances where that power is not exercised. That that is the correct way of construing the DTR Regulations may be seen in the terms of various provisions in the DTR Regulations – for example:

(1) paragraph 5, which releases the payer from the obligation to account for the tax for which the payer would have been required to account in the absence of the direction under the regulations;

(2) paragraph 6, which deems the withholding to have been made for the purposes of applying the old legislation in Section 248 of the Income and Corporation Taxes Act 1970 (the "ICTA 1970") that made the deductibility of interest as a charge on income dependent on the payer's having accounted for withholding tax in respect of the interest; and

(3) paragraph 8, which provides for the obligation to account for withholding tax to revive where the direction given under the regulations becomes ineffective or is cancelled.

125. The terms of these paragraphs would make no sense if a direction under the DTR Regulations was not a prerequisite to the ability of the payer of the interest to make gross payment.

Conclusion

126. For the reasons set out in paragraphs 103 to 125 above, I have concluded that the withholding tax obligation which arose under Section 874 of the ITA in this case was not vacated by the terms of paragraph 3(2) of the Guernsey Treaty. For completeness, I would add that, if the language used in the, now archived, paragraph INTM 355225 of the Respondents' International Manual suggested that interest could be paid gross by a UK resident company to a Jersey resident bank simply in reliance on the equivalent wording, in the double tax treaty between the United Kingdom and Jersey, to the wording addressed in this part of the decision, then, in my view, that statement was concessionary in nature because it did not accord with the law, for the reasons set out above.

SECTION 933 OF THE ITA

The law

Beneficial entitlement to income

127. Section 933 of the ITA has the effect that the withholding tax obligation in Section 874 of the ITA does not apply "if the person beneficially entitled to the income in respect of which the payment is made is a UK resident company".

128. The meaning of beneficial entitlement to income in the context of tax has been considered in a number of cases. From those cases, it is apparent that determining beneficial entitlement to income can depend on the context in which the phrase appears.

129. In *Indofood International Finance Ltd v JP Morgan Chase Bank NA, London Branch* [2006] EWCA Civ 158 ("*Indofood CA*"), one of the questions in issue was how the phrase, which appeared in the double tax treaty between the Republic of Indonesia and the Netherlands, would fall to be construed as a matter of Indonesian law. Sir Andrew Morrit C held that, in addressing that question, the phrase was "to be given an international fiscal meaning not derived from the domestic laws of contracting states" (see *Indofood CA* at paragraph [42]). He then went on to hold that the fact that the person who would be receiving the relevant income was not the trustee, nominee or agent for anyone else was not conclusive in determining that it would be the beneficial owner of the income because "the concept of beneficial ownership is incompatible with that of a formal owner who does not have 'the full privilege to directly benefit from the income'" and that therefore where a person receiving income was, both as a commercial and a practical matter, bound to pay on to another person that which it received, that person could not be said to have a beneficial entitlement to the income (see I*ndofood CA* at paragraphs [42] and [44]). Chadwick LJ and Sir Peter Gibson LJJ agreed with Sir Andrew Morrit C on this point.

130. In my view, the decision in *Indofood CA* is of no relevance in determining the meaning of the phrase where it appears in Section 933 of the ITA. That is because, in that context, the phrase is to be construed as a matter of English law and not by reference to any international fiscal meaning.

131. As for the meaning of the phrase as a matter of English law, the general position is set out in the decision of Evans-Lombe J at first instance in *Indofood CA* (see *Indofood International Finance Ltd v JP Morgan Chase Bank NA, London Branch* [2006] STC 192

(*Indofood HC*")). In that decision, Evans-Lombe J held that, as long as the recipient of income is not receiving the income as a fiduciary, such as where it is acting as nominee or trustee for another person, it is the beneficial owner of the income and that that remains the case even if the recipient has a contractual obligation to pay on the income to some other person (see *Indofood HC* at paragraphs [46] and following).

McGuckian

132. However, I refer in paragraph 131 above to the general position because all statutory provisions in the United Kingdom are required to be construed in accordance with the principles which are now well-established by virtue of a line of cases starting with *Ramsay (WT) Limited v Inland Revenue Commissioners* [1981]1 All ER 865 and which has come to be known as the "Ramsay principle". That principle requires that, in the application of any statutory provision, it is necessary to adopt a purposive approach to construing the provision and then consider whether the transaction which is alleged to fall within the provision, when viewed realistically, falls within the ambit of the provision.

133. The Ramsay principle was applied by the House of Lords in *Inland Revenue Commissioners v McGuckian* [1997] 3 All ER 817 ("*McGuckian*"). In *McGuckian*, the taxpayers assigned their shares in an Irish company ("B") to a Guernsey resident settlement of which they were beneficiaries. On 23 November 1979, the trustee of that settlement ("S") transferred to a UK resident company associated with the tax consultant advising the taxpayers ("M") the right to any dividend which might be paid by B in 1979. On 27 November 1979, B declared a dividend and paid 100% of that dividend to a solicitor acting for M, who then paid 99% of the dividend to S (acting as trustee of the settlement) and the remaining 1% of the dividend, less the solicitor's fee, to M. The House of Lords held that the amount received by S as trustee of the settlement was dividend income from B and not the capital proceeds of a sale to M. In reaching that conclusion, the House of Lords accepted that the sale of the right to the dividend income was not a sham. However, although there had been no relevant finding of fact at first instance in that case, the only possible conclusion on the facts was that there was no business purpose for the assignment of the right to the dividend and the assignment was an artificial step which had been inserted solely for the purpose of gaining a tax advantage. As such, as the sale of the dividend was to be disregarded in determining the nature of the sum which had been received by S. The substance of what had occurred was that 99% of the dividend had been received by S. The House of Lords rejected the Respondents' claim to treat the remaining 1% of the dividend – which is to say, the amount which had not been received by S and had instead been paid by B to M and M's solicitor – as part of the dividend income received by S because S had not received it.

134. In his decision in *McGuckian*, Lord Cooke made the point that not all assignments of the right to receive income would be disregarded in this way. In some cases, the circumstances in which the assignment took place would mean that the proceeds of the assignment would be treated as capital in nature. However, in other cases, such as those in that case, "the circumstances surrounding the transaction may require the conclusion that the receipt is income" (see *McGuckian* at page 828c). Characterising the proceeds of the assignment as dividend income was the only reasonable answer. The assignment was the means whereby S received 99% of the dividend income (see *McGuckian* at page 829g).

Conclusion

135. It may be seen that, although the decision in *Indofood CA* is of no relevance in the present case – and the principles applied by the Court of Appeal in *Indofood CA* in determining the parameters of the "international fiscal meaning" of beneficial entitlement were

more wide-ranging than those adopted by the House of Lords in *McGuckian* in determining the nature of the payment received by S – both cases indicate, in their different ways, that there may be circumstances where:

(1) beneficial entitlement to an item of income for the purposes of the UK tax legislation is not invariably simply to be determined by reference to equitable entitlement as a matter of law; and

(2) a contractual obligation which deprives the recipient of the commercial benefits of the receipt might well also deprive the recipient of beneficial entitlement to the receipt as a matter of law.

The arguments of the Appellant

The impact of contractual obligations on beneficial entitlement

136. Mr Way accepted that the burden was on the Appellant to show that Houmet was beneficially entitled to the interest the right to which was assigned to Houmet before it was paid. However, he submitted that beneficial entitlement for that purpose was to be determined in accordance with the English law concept of equitable entitlement. In other words, he said that Houmet's obligation to pay Storrier or the relevant Guernsey Trust for the assignment of the right to receive the interest could be disregarded in that context. All that mattered was that Houmet wasn't acting as a fiduciary in receiving the interest. As long as it was not acting as a nominee or trustee for some other person – in which case that person would be entitled in equity to the interest and, hence, beneficially entitled to the interest - Houmet could be said to be beneficially entitled to the interest.

137. He added that the accounts of Houmet for its financial year ended 31 December 2015 (at pages 2498 and following of the DB) (the "Accounts") contained a statement of comprehensive income which showed:

(1) in respect of the financial year ended 31 December 2015, revenue of £2,999,403, cost of sales of £2,998,404 and a gross profit before administrative expenditure of £999; and

(2) in respect of the financial year ended 31 December 2014, revenue of £1,517,752, cost of sales of £1,513,882 and a gross profit before administrative expenditure of £3,870.

138. He then said that, when one turned to the table setting out the interest paid to Houmet on page 2769 of the DB (the "Table"), that showed that the interest paid to Houmet over the financial year ended 31 December 2015 was £2,997,319.19 and that the interest paid to Houmet over the financial year ended 31 December 2014 was £1,514,681.22. In Mr Way's view, the figures for each of those two financial years shown in the Table were sufficiently close to the figures shown as revenue in respect of the same financial years in the Accounts to show that the interest received by Houmet from the Appellant had been taken into account in the Accounts and therefore that that was evidence that Houmet was the beneficial owner of that interest.

McGuckian

139. Turning to the decision of the House of Lords in *McGuckian*, in respect of which I had asked the parties for their representations, Mr Way said that the present facts were distinguishable from those in that decision because the transactions in *McGuckian* were solely tax-motivated and generated by a tax consultant, who had overarching responsibility for the scheme as a whole, whereas the transactions in this case were not integrated in the same way. The Appellant had had no involvement in the decision by Storrier or the relevant

Guernsey Trust to transfer the interest to Houmet and the reasons for each such transfer were unknown.

Conclusion

The facts

140. It is common ground that, as a company incorporated in the United Kingdom, Houmet was resident in the United Kingdom for UK tax purposes. However, apart from that, the evidence in relation to Houmet which has been provided to me is scant. From the material provided at the hearing, it appears to have been incorporated in 2005, well before its participation in the refinancing structure, which commenced only in 2012. However, the Appellant has provided no explanation for its role in the refinancing structure. Mr Gill, the Appellant's witness from Mercator, had retired well before 2012 and so he was unable to shed any light on Houmet's involvement in the refinancing structure, as such. Similarly, JH testified that he was unaware of the reasons for the assignments to Houmet. He said that he had simply been informed by Mercator that the assignments had been made without being provided with a reason for that.

141. Given:

(1) the absence of any explanation for Houmet's involvement in the refinancing structure;

(2) the connection between Houmet, Storrier and the Guernsey Trusts in that each of them was managed by Mercator; and

(3) the fact that Houmet was invariably assigned the right to interest only a very short time before the interest was paid by the Appellant so that the commercial reasons for its participation in the refinancing structure are far from obvious,

the inescapable conclusion on the facts in my view is that the only reason for Houmet's involvement in the refinancing structure was to provide an alternative argument – this time under Section 933 of the ITA instead of paragraph 3(2) of the Guernsey Treaty - for the Appellant to be able make gross payment of the interest in the event of a failure in the Appellant's arguments to the effect that the interest did not have a UK source and did not amount to "yearly" interest.

142. I therefore find as a fact that there was no business purpose to the involvement of Houmet in the transactions comprising the refinancing structure and that the only reason for Houmet's involvement in those transactions was to ensure that a UK resident company received the interest instead of the Guernsey-resident Storrier or the relevant Guernsey Trust, in order to secure a UK tax advantage.

The conclusion of law

143. Having reached that conclusion of fact, it is necessary for me to consider whether, as a matter of law, and, more specifically, as a matter of applying Section 933 of the ITA, construed purposively, to the facts, viewed realistically, Houmet can be said to have been beneficially entitled to each payment of interest which it received. In my view, the decision in *McGuckian* compels the conclusion that, to the extent of the amount which Houmet paid to Storrier or the relevant Guernsey Trust as consideration for the assignment of the right to receive a payment of interest, it was Storrier or the relevant Guernsey Trust, and not Houmet, which was beneficially entitled to that payment of interest. Once the artificial step comprising the assignment of the right to receive the interest is identified and disregarded, the inevitable result is that, to the extent of that amount, the person beneficially entitled to the payment of interest was instead Storrier or the relevant Guernsey Trust.

144. In reaching this conclusion, I have taken into account the fact that, in *McGuckian*, the part of the dividend which was equal to the assignment consideration was paid by B to M's solicitor and then paid by M's solicitor on M's behalf to S, as the consideration for the assignment, as opposed to being paid to M itself and then paid by M to S, as consideration for the assignment. In contrast, in this case, it appears that the part of the interest which was equal to the assignment consideration was both paid by the Appellant to Houmet and paid by Houmet to Storrier or the relevant Guernsey Trust, as consideration for the assignment. However, there is nothing in the judgments in M*cGuckian* to suggest that that difference was of any significance to the decision reached by the House of Lords in that case. The key feature in M*cGuckian* was the absence of any business purpose to the assignment. The fact that the part of the dividend which was equal to the assignment proceeds did not pass through M itself was of no moment.

145. I have also taken into account the fact that *McGuckian* was a case which related to the characterisation of a receipt in the hands of the assignor. It said nothing in relation to the tax position of the assignee. However, that was because the case concerned the application of particular statutory provisions – Sections 470 and 478 of the ICTA 1970 - to the taxpayers in relation to a receipt by the assignor. It was held that the assignment should be disregarded to the extent of the 99% of the dividend which was paid to S as consideration for the assignment. The key question in this case relates to a completely different statutory provision – Section 933 of the ITA – and the question is whether the assignee, Houmet, was beneficially entitled to the interest for the purposes of that provision. However, based on the reasoning of the House of Lords in *McGuckian*, the only logical answer to that is that, to the extent that the interest received by Houmet did not exceed the consideration given by Houmet to Storrier or the relevant Guernsey Trust for the assignment of the interest, Houmet was not so beneficially entitled.

The remaining interest

146. Turning then to what remains of the interest which was paid to Houmet by the Appellant and the task of determining whether the Appellant has discharged the burden of proof of showing that, on the balance of probabilities, Houmet was beneficially entitled to that residue, I have been provided with limited evidence in relation both to:

(1) the question of whether the interest paid to Houmet might have been received by Houmet as nominee or trustee for another person; and

(2) the question of how much Houmet paid to Storrier or the relevant Guernsey Trust in respect of the right to receive that interest.

147. The evidence so provided was:

(1) the Table – which showed the interest paid to Houmet in each of its four financial years ended 31 December 2012, 31 December 2013, 31 December 2014 and 31 December 2015;

(2) the Accounts – which showed the revenue and cost of sales of Houmet in relation to each of the financial years ended 31 December 2014 and 31 December 2015; and

(3) a schedule appended to an email from Mr Gary Le Page of Mercator to Mr Edward Magrin of BDO of 5 March 2019 which was exhibit 5 to the supplementary witness statement of JH (see page 2581 of the DB) (the "Statement"), which set out receipts by Storrier from Houmet in respect of the right to receive interest assigned by Storrier to Houmet in each of the four financial years in question.

148. In terms of the evidential quality of the above information, Mr Vallat, quite reasonably, pointed out that:

(1) the Appellant had not produced any accounts in respect of the first two of the financial years in question;

(2) the Appellant had made no attempt to demonstrate that the figures appearing in the Accounts in respect of the latter two of the financial years in question were related in any way to this transaction. It was perfectly possible that those figures related to other, unrelated, transactions into which Houmet had entered during the relevant financial years; and

(3) in any event, there was not a perfect correlation between the figure shown in the Accounts as revenue in respect of each of the third and fourth financial year and the figure shown in the Table as interest received by Houmet in respect of the relevant financial year.

149. Mr Vallat added that the Appellant had not even provided me with the documents pursuant to which the rights to interest had been assigned by Storrier or the relevant Guernsey Trust to Houmet. I am not too concerned by that as the Appellant was not a party to that assignment and because the DB did contain numerous examples - at pages 2218, 2219, 2252, 2253, 2280, 2281, 2300, 2301, 2367, 2368 and 2660 to 2666 - of the notification of the assignment which was given by Storrier to the Appellant, and the Appellant's acceptance and acknowledgement of that fact.

150. I agree that it would have been highly desirable for me to have been provided with some additional evidence on this subject, preferably witness evidence from someone responsible for the affairs of Houmet at the relevant time. That evidence could have helped to confirm that the figures in respect of revenue which appeared in the Accounts and which related to the latter two of the financial years did indeed reflect the interest shown in respect of each financial year in the Table. The absence of any such evidence means that I am necessarily having to reach a conclusion on incomplete material.

151. It is of course conceivable that the figures in the Accounts reflect some completely unrelated transactions of Houmet where the numbers just happen to bear a close resemblance to the numbers in the transactions to which this appeal relates and that Houmet entered into the transactions to which this appeal relates purely as a nominee or trustee for someone else, with the result that the cash flows from these transactions did not need to be reflected in the Accounts. Nevertheless, the close correlation between the figures in respect of revenue in the Accounts and the amounts shown as having been paid as interest in respect of the two financial years in question in the Table leads me to conclude that, on the balance of probabilities, the figures for revenue and cost of sales in respect of the latter two of the financial years, as recorded in the Accounts, include the transactions to which this appeal relates.

152. That, in turn, leads me to conclude that, although the absence of any accounts for Houmet in respect of the first two of the financial years is, to say the least, sub-optimal, on the balance of probabilities, there would have been a similar degree of correlation between the revenue figures in respect of the first two financial years which would have appeared in the accounts of Houmet for the financial year ended 31 December 2013 and the amounts shown as having been paid as interest in respect of those two financial years in the Table and therefore the figures for revenue and cost of sales in respect of the first two of the financial years, as recorded in those accounts, would have included the transactions which are the subject of this appeal.

153. For the reasons set out in paragraphs 151 and 152 above, the Appellant has satisfied me that the interest paid to Houmet in all four of the financial years was not received by Houmet as nominee or trustee for any other person. That leads to my concluding that Houmet did

have a beneficial entitlement to such part of each interest payment made to Houmet in the four financial years in question as exceeded the amount paid by Houmet to Storrier or the relevant Guernsey Trust for the right to receive that interest payment.

154. I am content to leave it to the parties to calculate how much of each such interest payment that was because the figures at my disposal and the legibility of the figures in the Table and the Statement are not up to the task. However, I would note that such evidence as I have seen indicates that the amount in question is likely to be extremely small (or perhaps even nil) in the case of each interest payment. For example, the aggregate difference in each financial year other than the financial year ended 31 December 2013 appears to be £500 (£755,773.46 minus £755,273.46) in respect of the financial year ended 31 December 2012, £799 (£1,514,681.22 minus £1,513,882.22) in respect of the financial year ended 31 December 2014 and nil (£2,997,319.19 minus £2,998,403.32) in respect of the financial year ended 31 December 2015.

155. It is not possible to do the same calculation in respect of the financial year ended 31 December 2013 for two reasons, as follows:

(1) first, the Statement merely details the payments which were made by Houmet to Storrier in that financial year and does not include the payments which were made by Houmet to the two Guernsey Trusts in that financial year and I could see no evidence of the latter elsewhere in the DB; and

(2) secondly, it is apparent from the fact that the aggregate interest shown by the Table as having been received by Houmet in that financial year, leaving aside:

(a) interest the right to which was acquired from a Guernsey Trust; and

(b) the £1,693,784.25 of interest received on the loan made by the FURBS to the Appellant under the revolving credit facility of £8,506,500, which was assigned to Storrier on 14 March 2013 (see the DB at pages 2091 and 2095),

which comes in total to £187,962.82, is exactly £600 more than the amount shown on the Statement in respect of that financial year of £187,362.82, that the Statement must be erroneous in having omitted to record the consideration which was paid by Houmet to Storrier for the right to receive the interest referred to in paragraph 155(2)(b) above.

156. However, all of the other evidence in this appeal points to the likelihood that the difference between the figures in relation to the interest paid in the financial year ended 31 December 2013 will be the same de minimis amount as the difference between the figures in relation to the interest paid in the other financial years.

157. Given the incomplete nature of the figures, I would prefer to decide this issue in principle and leave the parties to do the necessary calculations.

CONCLUSION

158. Subject to the minor adjustments to the various assessments to reflect the outcome of the calculations referred to in paragraphs 154 to 157 above, the assessments are hereby upheld.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

159. 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.

TONY BEARE
TRIBUNAL JUDGE

RELEASE DATE: 2 NOVEMBER 2021

Amended and reissued on pursuant to Rule 37 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 to correct the accidental slips and omissions in paragraphs 13, 20, 52 and 144 of the original decision dated 2 November 2021.