R v DIMSEY; R v ALLEN

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I have written previously in *The Offshore and International Tax Planning Review* (Volume 9 Issue 1 pp 69-73) criticising the reasoning of the Court of Appeal (Criminal Division) in *R v Dimsey; R v Allen* [1999] STC 846. The House of Lords has now dismissed appeals from those decisions [2001] UKHL 46; [2001] STC 1520 *(R v Dimsey)* [2001] UKHL 45; [2001] STC 1537 *(R v Allen)*. It is only right, therefore, that I should consider the way in which the House came to its conclusions.

It is, fair to note first that the arguments before the House of Lords were in certain important regards different to those put before the Court of Appeal. There is nothing unusual in a certain shift in arguments as a case progresses up the appellate ladder. It is very rare that the arguments which are put before the Special Commissioners are the same as those put when the case reaches the House of Lords. It will be seen, however, that in the present appeals there was a fundamental change in the way the Crown's case was put in relation to the arguments on TA 1988 section 739. I shall deal with *R v Dimsey* first.

R v Dimsey

Dimsey was charged, inter alia, with conspiring to defraud the Revenue by failing to make full and complete disclosure of certain matters. One of those matters was the profit made by offshore companies which Chipping, a client, managed and controlled. The Crown alleged that those companies, although registered abroad, were in fact resident in the UK and so liable to UK corporation tax. The jury accepted the Crown's contentions and convicted Dimsey. However, on appeal, Dimsey argued that, even though UK resident, the companies could not be liable to corporation tax. The income of the non-resident companies arose by reason of a transfer of assets by Chipping who had "power to enjoy" that income due to owning the shares in the companies. That transfer was made in order to avoid UK tax. The companies were within section 739 because, although they were in fact UK resident, they were treated as non-resident due to being incorporated outside the UK: TA

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1988 section 742(8). The result of this was that the income of the offshore companies was deemed to be the income of Chipping by section 739(2).

In the Court of Appeal, the Crown accepted that if the income was deemed to be the income of the transferee, it could not at the same time be the income of the transferor for income tax purposes. However, it argued that this did not apply for the purposes of corporation tax. The Court of Appeal accepted this argument. It was, however, flawed for the reasons set out in my earlier article.

In the House of Lords, the Crown took a more fundamental point. It argued that section 739(2) did not have the effect that the income was deemed not to be the income of the transferee. It remained the transferee's income for all purposes. Lord Scott (with whom the other law lords agreed) accepted this argument. He was particularly impressed by the fact that section 739 was first enacted (as section 18 of the FA 1936) at the same time as what is now TA 1988 section 660B (then section 21 of the FA 1936). Section 21 provided that the income "shall ... be treated for all the purposes of the Income Tax Acts as the income of the settlor ... and not as the income of any other person". The underlined words did not appear in section 18, and still do not appear in section 739. Lord Scott put it this way [at paragraph 48]:

> *"[48] Confronted by the express words in section 21(1), 'and not as the income of any other person' it seems to me very difficult, if not impossible, to argue that those words, or something similar, which are notably absent from section 18(1) should be an implied addition to section 18(1). A comparison between section 18(1) and section 21(1) suggests strongly that the omission of any such words from section 18(1) was deliberate."*

Lord Scott also dealt with the double taxation objection. He pointed out that Parliament had expressly addressed the question of double taxation in section 743(1). If necessary he would have construed that provision as extending to corporation tax charged on the transferee. He thought that Parliament's failure to do this when corporation tax was introduced (or in the 35 years since!) was an "inadvertent oversight". In any event, he felt that section 743(1) showed "... that section 739(2) is not intended to exclude the normal tax liability that would lie on a transferee in respect of its income".

Those arguments, although far from overwhelming, are much more convincing than those put forward by the Court of Appeal. The result is clearly a sensible one. Dimsey would have been fortunate indeed to have his conviction quashed by reason of the operation of what was described by Lord Scott as a "penal" anti-avoidance provision.

Although, it appears that the human rights arguments added little, if anything, to the debate, there is a point to be noted in relation to the operation of the 1998 Act. At paragraph 61 it is recorded that:

> *"Mr Milne accepted that the 1988 Act must now be construed, so far as it is possible to do so, in a way compatible with Convention rights (see section 3 of the 1998 Act)".*

Dimsey was argued before the House of Lords, speeches in *R v Lambert* (see *R v Allen* at para 23.) Therefore, all the human rights arguments were heard 'de bene esse'. It is unlikely that Mr Milne's concession would now be made in relation to events which occurred before the 1998 Act came into force. In *R v Kensal (No 2)* [2001] UKHL 62; [2001] 3WLR 1562, Lord Hope stated that section 3(1) of the 1998 Act was not retrospective in its effect: at paras 83-4. None of the other law lords dealt with that point expressly. It is an issue which will almost certainly have to be addressed in the future.

R v Allen

The main issue in Allen was the effect of TA 1988 section 168(8). This provides that:

> *"... "director" means-*
>
> *(a) in relation to a company whose affairs are managed by a board of directors or similar body, a member of that board or similar body*
>
> ...
>
> *and includes any person in accordance with whose directions or instructions the directors of the company (as defined above) are accustomed to act."*

The argument for Allen was that this is a definition of a term ("director") used in a number of places in Chapter II of the 1988 Act. It did not have the effect of deeming the 'shadow director' to have all (or any of) the attributes of a director, in particular to have an "office". This is clearly the normal rule. For instance, "company" in the TA 1988 is defined as including an unincorporated association: TA 1988 section 832. However, no-one would suggest that the consequence of that is that an unincorporated association is to be treated, for the purposes of TA 1988, as having all the attributes of a company e.g. corporate personality, limited liability, a share capital, directors, articles of association etc. It is simply that it is to be taken as being referred to whenever the word "company" appears in the Act.

Lord Hutton rejected this argument without any reasoning at all. He simply said (at para 20):

> (8) "I am unable to accept Mr Kessler's first argument on the construction of the provisions. Under the concluding part of section 168(8) a shadow director is taken to be a director and therefore under ss.167(1)(a) *and 168(2) he is employed in the office of a director if the emoluments of* that office can be regarded as falling to be assessed under Schedule E."

There appears to be a confusion here between being employed (as a director or otherwise) and holding the office of director. Not all directors are employed. If they were, there would be no need to extend the definition of employment to include an office: see section 168(2). Whatever else it does, section 168(8) clearly does not deem a "shadow director" to be an employee.

This confusion also appears in para 19 where Lord Hutton talks about the "services provided by the shadow director." However, we are not concerned with shadow directors providing services. What they are doing is influencing or controlling the board of directors. If the shadow director was providing services, and receiving a reward (in cash or of kind), he would either be an employee (and so clearly within ss.145/6) or self-employed (in which case there is no reason for ss.145/6 to apply). In any event, in the light of the decision it now appears that we should look at definition sections as also being deeming provisions. The question presumably is how far one can take the deeming in any particular case: see e.g. *Marshall v Kerr* [1993] STC 760, 766. It is a pity that Lord Hutton did not articulate his reasoning on this point as it would have assisted practitioners in other cases.

Lord Hutton did give some reasons for rejecting the arguments on circularity and territorial scope. However, they were not particularly strong arguments. He did not, however, address the point that TA 1988 section 19(1) assumes that an office or employment will have "duties" which are performed either within or outside the UK. There are two possible approaches to the problem. First, since a shadow director has no duties, they can never be performed in the UK. Secondly, the control or influence of the board must be regarded as "duties" by taking the deeming to its logical conclusion. Therefore, one must look at where the taxpayer is when he exercises that control or influence. This is likely to be important in certain cases where the Revenue seek to apply the *Dimsey* decision.

Conclusion

The section 739(2) point was never an important point in itself. The problem was the reasoning employed by the Court of Appeal. The reasoning of the House of Lords is more satisfactory. The shadow director point is far more important in practice. We now have a clear decision, although no reasoning to guide us in applying it. In any event, the focus will now shift to the question whether the individual is in fact a shadow director. Valuable guidance on that issue can be found in the decision of the Court of Appeal in the company law case *Secretary of State for Trade and Industry v Deverell* [2001] 1 Ch 340.