The Offshore Tax Planning Review

DOUBLE TAXATION TREATIES: THE ANTIDOTE TO ANTI-AVOIDANCE PROVISIONS?
BRICOM HOLDINGS LTD V IRC

Robert Venables QC[1]

1 The Background

1.1 The Mischief

It has long been debated to what extent a double taxation convention[2] may override an anti-avoidance provision of the municipal law of one of the contracting states. One common form of avoidance is for the taxpayer to ensure that profits arise to an entity, typically a trust or a company, which is not itself liable to tax, in circumstances where the taxpayer may nevertheless hope to enjoy the profits in due course. The strategy often takes the form of ensuring that the income arises to an entity which is not resident in the jurisdiction which imposes the tax and, on that ground, itself escapes liability to tax.

1.2 United Kingdom Legislation

United Kingdom fiscal legislation is in no way exceptional in containing a fair number of complicated provisions aimed to counteract such tax avoidance. The usual strategy is to deem the profits of the exempt entity to be that of a taxpayer for fiscal purposes. Among the more notable current examples may be mentioned the settlement provisions, contained in Taxes Act 1988 Part XV, which deem

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2 The discussion in this article in general holds good for double taxation arrangements which are not conventions or treaties. Examples are those between the United Kingdom and Jersey, Guernsey and the Isle of Man.

income arising under a settlement to be that of the settlor under certain conditions, and Part XVII, tax avoidance. Part XVII contains Chapter III, which strikes where there has been a transfer of assets abroad and income arises to a person not resident or domiciled in the United Kingdom, Chapter IV, the controlled foreign companies legislation, Chapter V, the offshore funds provisions and Chapter VI, miscellaneous. In Chapter VI are to be found section 775, sale by individual of income derived from his personal activities, and section 776, artificial transactions in land.

1.3 The Importance of Double Taxation Conventions

The principal effect of double taxation conventions[3] is that they shelter the profits of a resident of Contracting State A from a fiscal imposition by Contracting State B. If a taxpayer resident in Contracting State B has entered into an avoidance strategy which procures that income arises to an entity resident in Contracting State A, which entity has an immunity from taxation in Contracting State B, can the taxpayer rely on that immunity if he is himself assessed by Contracting State B under anti-avoidance legislation which deems the income of the entity to be his?

1.4 No General Solution

1.4.1 Relevant Considerations

In my view, the answer must depend on all the circumstances, including the true scope of the convention, the status of the convention in the municipal law of the taxing state and the scope of the anti-avoidance provision of that state.[4]

1.4.2 The Scope of the Convention

The starting point must always be the true construction of the convention. As an international treaty, the convention will fall to be construed, not according to the

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3 The term "conventions" is used in this article to include not only treaties in the strict sense but other arrangements having like effect, such as those made between different possessions of Her Britannic Majesty.

4 One United Kingdom anti-avoidance provision which can in my view clearly be circumvented in an appropriate case by the use of a double taxation convention is Taxes Act 1988 section 776, Transactions in Land: taxation of capital gains. See my article 'Double Taxation Treaties as a Defence to Taxes Act 1988 Sections 775 - 777' in Volume 4, Issue 2 of this *Review* at page 129.

traditional rules of English law, but in accordance with the Vienna Convention on the Interpretation of Treaties and the traditional rules of public international law.[5]

If the convention on its true construction provides that a resident of Contracting State B shall not be taxable in respect of certain income arising in Contracting State A, then that can clearly afford no defence to a different person, such as X, a resident of Contracting State A who is deemed by the municipal tax law of Contracting State A to be entitled to the income. Where, however, the effect of the convention is that income shall not be taxable, then the position is technically very different. There is then no *a priore* reason why X cannot rely on an immunity from taxation by Contracting State A of income which in reality belongs to a resident of Contracting State B.[6] A key question will thus always be whether or not the immunity is personal.

1.4.3 The Status of the Convention in Municipal Law

Under United Kingdom constitutional law, while the Crown has the prerogative of concluding international treaties, no such treaty has any effect in United Kingdom municipal law unless it is ratified or authorised by an Act of Parliament. Double taxation conventions concerning income tax, corporation tax and capital gains tax can become part of United Kingdom law if an Order in Council[7] is made pursuant to the power delegated by Taxes Act 1988 Part XVIII (Double Taxation Relief) section 788(1). Now a convention may arguably make provision for matters not covered by section 788. As a matter of constitutional law, the convention would to that extent not be incorporated into United Kingdom law.[8]

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[5] See the decision of Walker J in the English case of *Memec PLC v Commissioners of Inland Revenue* 24th October 1996, which, although at the time of writing unreported, will no doubt figure in STC and TC in due course. His Lordship did not simply pay lip service to the different canons of construction of the Anglo-German double taxation treaty of 28th November 1964, but gave it a purposive interpretation which would have been quite impossible if one had construed it as a United Kingdom statute.

[6] In *IRC v Commerzbank AG* [1990] STC 285 Mummery J held that a person could take advantage of a double taxation convention even though he was not a citizen, resident or corporation of either contracting party.

[7] A species of statutory instrument or delegated legislation.

[8] Although it may be that the Commissioners of Inland Revenue ought not to take the point: see 10 below.

1.5 The Need for Realism

One must never forget that even United Kingdom courts do not nowadays always decide tax cases accordingly to the technical law, especially where there has been a tax-avoidance motive. They might be impressed by the consideration that where the income of the resident of another state is not liable to United Kingdom tax in the first place, and therefore treaty relief is not needed and not available, a United Kingdom resident would have no defence to an assessment on income of the non-resident which is deemed to be his. The whole purpose of such anti-avoidance provisions is to tax United Kingdom residents on income of a non-resident which has either escaped United Kingdom altogether or, at least, United Kingdom tax at as high a rate as the resident would have paid. As a matter of common sense, therefore, it should not make one iota of difference whether the reason the non-resident escapes United Kingdom tax is because of the United Kingdom tax code standing alone or whether because of some double taxation convention.

2 *Bricom Holdings Ltd v Inland Revenue Commissioners*

2.1 Importance of the Decision

Bricom Holdings Ltd v Inland Revenue Commissioners,[9] a decision of the United Kingdom Special Commissioners for Income Tax Purposes,[10] neatly raises several points in relation to the interaction of the United Kingdom controlled foreign companies legislation[11] and the United Kingdom-Netherlands double taxation convention ("the Convention"). Oddly enough, the argument which in my opinion is conclusive in favour of the taxpayer was apparently not presented to the tribunal.

While it is true that the Special Commissioners are only the first appeal tribunal and that two further appeals[12] are available as of right and a third[13] with leave, the decision is particularly worthy of our attention. There is, so far as I am aware, no decision of any United Kingdom superior court on the issue. Although a similar point was raised before the Special Commissioners in *Willoughby v IRC*,

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[9] [1996] STC (SCD) 228.

[10] There appears to be every prospect that the case will go further.

[11] Taxes Act 1988 Part XVII Chapter IV.

[12] To the High Court, Chancery Division and to the Court of Appeal.

[13] To the House of Lords.

it was not pursued before the Court of Appeal, quite possibly for the reasons mentioned at 6.5 below.

The Special Commissioners involved in *Bricom* were the presiding Special Commissioner, His Honour Judge Oliver QC, and Mr John Avery Jones CBE. Both of these gentlemen are of enormous wisdom and experience. It is difficult to conceive of a more authoritatively constituted tribunal. The argument for the taxpayer, which they rejected, would have been impeccably presented by Mr Andrew Park QC, a leading Revenue Silk of eighteen years standing, while Mr Launcelot Henderson QC, who appeared for the Revenue, would have made the contest even-handed. The views of the Commissioners are therefore entitled to the most careful consideration.

2.2 The Issues between the Parties

The main issues were:[14]

> firstly, whether a United Kingdom resident company (Bricom) could, in so far as interest beneficially owned by a related company (Spinneys), resident in the Netherlands, was apportioned to it under the controlled foreign companies legislation, prima facie take advantage of an exemption from United Kingdom corporation tax conferred by the Convention in respect of such income. The Special Commissioners decided that it could not. Their reasoning on this point is not always clear or satisfactory. In my respectful opinion, their conclusion cannot, as a matter of abstract law, be supported. There is nonetheless a real possibility that higher courts on appeal would, for pragmatic reasons, endorse their error.
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> secondly, whether, if Bricom succeeded on the first point, the exemption from corporation tax was of no use to it because the tax to which it was being charged was not corporation tax. This point turned on the intricacies of the controlled foreign companies legislation and was arguable either way. The Special Commissioners decided in favour of the Revenue on this point.
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> thirdly, whether, if Bricom succeeded on the first point but failed on the second point, it was nevertheless protected under the terms of the Convention on the grounds that it was being charged to a tax which was "substantially similar" to corporation tax and therefore covered by the

[14] This paragraph involves a certain degree of oversimplification, especially on the first issue, which itself resolves into further sub-issues.

Convention. The Special Commissioners "inclined to the view"[15] that Bricom would have succeeded on this point. It is difficult to see how any other decision could be reached as a matter of common sense or common honesty. Applying a purposive construction, which is paramount in the interpretation of treaties, one must conclude that the broadest interpretation must be given to "substantially similar"; otherwise, either Contracting State would be able easily to wriggle out of its obligations and in effect deprive the Convention of binding force, which must be the last thing the parties intended.

fourthly, whether, as a matter of United Kingdom *constitutional* law, the incorporation of the exemption conferred by the Convention for substantially similar taxes was *intra vires* the Order in Council purporting to incorporate the whole of the Convention into United Kingdom municipal law. While the point is arguable either way, the Special Commissioners found that it was not, so that Bricom could not rely on the exemption. If that is correct, it is matter of enormous consequence, as it follows that no convention exemption from "substantially similar" United Kingdom taxes forms part of United Kingdom law. It then seems to have been assumed without argument that that was the end of the matter. I discuss below an argument which could now[16] be raised that as a matter of *administrative* law the Revenue should not be able to rely on their own inefficiency in failing to incorporate into United Kingdom law a convention they have negotiated and concluded with the taxing authorities of another state.

2.3 The Real Issue?

I would respectfully suggest that the real issue was not ventilated and that an argument could have been advanced which, in my opinion, would have shot the ground from beneath the Revenue. In essence, it is that in computing the "chargeable profits" of the foreign controlled company which form, on any view, the measure of the charge on the United Kingdom resident company, one takes into account the treaty exemption of the foreign company and thus ignores any income on which it itself is exempt from United Kingdom tax by virtue of a relevant convention.

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[15] The headnote misleadingly gives the impression that there was a categorical decision on the point.

[16] Particularly after the decision of the Court of Appeal in *R v Commissioners of Inland Revenue ex parte Unilever Plc*, which was heard around the same time as the *Bricom* hearing before the Special Commissioners.

As the argument is a purely legal one, it is still open to Bricom to take it on appeal.

3 The Background

3.1 The Facts

Bricom was a company resident in the United Kingdom, It held 100% of the shares in Spinneys International BV ("Spinneys"), a company incorporated in and resident in the Netherlands. In its three accounting periods to 31st October 1990, 1991 and 14th April 1992 Spinneys received interest from a United Kingdom resident company, which was part of the Bricom group. The United Kingdom Double Taxation Relief (Taxes on Income) (Netherlands) Order 1980, SI 1980/1961, purported to incorporate[17] the United Kingdom-Netherlands double taxation Convention of 7th November 1980 into United Kingdom law. Under Article 11(1) of the convention:

> '(1) Interest arising in one of the States which is derived and beneficially owned by a resident of the other State shall be taxable only in that other State.'

It was common ground that Spinneys was, by virtue of the Convention, not liable to United Kingdom tax on the interest paid to it by other members of the Bricom group.

3.2 The Assessments

The Revenue invoked the Controlled Foreign Companies legislation, contained in Taxes Act 1988 Part XVII Chapter IV. They served notices under Taxes Act 1988 section 747(1)b on Bricom directing that the anti-avoidance provisions relating to the use of controlled foreign companies applied and, pursuant to the notices, assessed Bricom, as sole shareholder of Spinneys, under section 747(4)(a) in a sum equal to corporation tax on the whole of Spinneys 'chargeable profits'. The amount of the chargeable profits was admittedly the amount of its total profits (excluding chargeable gains) on which corporation tax would have been chargeable on Spinneys, assuming that it had been resident in the United Kingdom and had

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[17] One of the Revenue arguments, accepted by the Commissioners, depended on the Convention not having been fully incorporated into United Kingdom domestic law.

claimed all the reliefs for corporation tax to which it would have been entitled, less the whole of its "creditable tax".[18]

3.3 The Dispute

The dispute was as to whether the assessments were correct in including in Spinneys' chargeable profits amounts attributable to the interest which had been received from the United Kingdom source and exempted under Article 11 of the Convention.

3.4 The United Kingdom Statute

3.4.1 The Text

Section 747, Imputation of chargeable profits and creditable tax of controlled foreign companies, provides, so far as is relevant:

> "(1) If the Board have reason to believe that in any accounting period a company:
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> (a) is resident outside the United Kingdom, and
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> (b) is controlled by persons resident in the United Kingdom, and
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> (c) is subject to a lower level of taxation in the territory in which it is resident,
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> and the Board so direct, the provisions of this Chapter shall apply in relation to that accounting period.
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> (2) A company which falls within paragraphs (a) to (c) of subsection (1) above is in this Chapter referred to as a "controlled foreign company".
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> (3) Where, by virtue of a direction under subsection (1) above, the provisions of this Chapter apply in relation to an accounting period of a controlled foreign company, the chargeable profits of that company for that period and its creditable tax (if any) for that period shall each be apportioned in accordance with section 752 among the persons (whether

[18] It seems to have been tacitly admitted by Bricom that Spinney would, on this hypothesis, have been chargeable to corporation tax on the interest. I argue at 12 below that this was not the case.

resident in the United Kingdom or not) who had an interest in that company at any time during that accounting period.

(4) Where, on such an apportionment of a controlled foreign company's chargeable profits for an accounting period as is referred to in subsection (3) above, an amount of those profits is apportioned to a company resident in the United Kingdom then, subject to subsection (5) below:

> (a) a sum equal to corporation tax at the appropriate rate on that apportioned amount of profits, less the portion of the controlled foreign company's creditable tax for that period (if any) which is apportioned to the resident company, shall be assessed on and recoverable from the resident company as if it were an amount of corporation tax chargeable on that company; and
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> (b) ....

and for the purposes of paragraph (a) above "the appropriate rate" means the rate of corporation tax applicable to profits of that accounting period of the resident company in which ends the accounting period of the controlled foreign company to which the direction under subsection (1) above relates or, if there is more than one such rate, the average rate over the whole of that accounting period of the resident company.

(4A) ...

(4B) ...

(5) ...

(6) In relation to a company resident outside the United Kingdom:

> (a) any reference in this Chapter to its chargeable profits for an accounting period is a reference to the amount which, on the assumptions in Schedule 24, would be the amount of the total profits of the company for that period on which, after allowing for any deductions available against those profits, corporation tax would be chargeable; and
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> (b) ..."

3.4.2 Analysis

The three key elements are thus:

(1) the ascertainment of the "chargeable profits" of the foreign resident company;

(2) the apportionment of part of those profits to persons having an interest in the company; and

(3) the assessment on and recovery from a United Kingdom resident company of "a sum equal to corporation tax" on the amount of the profits apportioned to it, less the creditable tax so apportioned "as if it were an amount of corporation tax chargeable on" that company.

The section is particularly tortuous. Its operation can be contrasted with, for example, that of Taxes Act 1988 section 739 (transfers of assets abroad, prevention of avoidance of income tax) which simply deems income of a non-United Kingdom resident to be that of a "transferor" who is ordinarily resident in the United Kingdom.

4 The Arguments

4.1 The Crown's[19] Argument

The Crown's primary argument was that Article 11(1) did not require the interest to be excluded. It is not clear from the decision how this argument was further deployed, as it is not separately reported. The Revenue appear not to have relied on any general principle that a United Kingdom resident cannot take advantage of an exemption conferred by a double taxation convention on income arising to a resident of another contracting state, which income is deemed by the municipal

[19] The United Kingdom Commissioners of Inland Revenue are technically agents of the Crown, i.e., Her Britannic Majesty. While the Crown is not in fact a party to any tax appeal, the Revenue love to stress that they are the Crown's representative and even refer to themselves as "the Crown". While this harmless conceit is indulged in by courts, law reporters and even taxpayers' counsel, it must be a source of confusion to foreigners, especially in judicial review cases, such as *R v Commissioners of Inland Revenue ex parte Unilever Plc*, referred to at 10 below, where the Crown is at least in theory, bringing proceedings against the Commissioners of Inland Revenue!

legislation of the United Kingdom to be that of the taxpayer.[20] Instead, the thrust of their argument was that the chargeable profits on which Bricom was assessed are, under section 747(4)(a), "a wholly notional amount, no part or component of which is paid to or received by anyone, whether as interest or anything else. That amount exists as a measure of profit to be apportioned under section 747."

It was contended by the Crown in the alternative that while tax under section 747 was a tax, it was not corporation tax but a sum 'equal to corporation tax' to be assessed on and recovered from the United Kingdom resident company 'as if' it were an amount of corporation tax chargeable on that company; hence it was not a tax within Article 2(1)c which was the subject of the Convention; nor was it 'substantially similar' to corporation tax so as to qualify for relief under the Convention pursuant to Article 2(2).

4.2 Bricom's Argument

The response from Bricom was that the controlled foreign company legislation does not apply to change the real nature of the interest, which is United Kingdom source interest received by a Netherlands resident; the interest retains its treaty-exempt character even when brought into the computation of chargeable profits; and the chargeable profits are not, as the Crown argues, a notional amount operating as a measure for apportionment purposes; this remains the position notwithstanding that the interest is part only of the chargeable profits; article 11 exempted the interest as a component of the controlled foreign company's chargeable profits.[21]

5 The Three-Stage Process

5.1 The Special Commissioners' Decision

The Special Commissioners held that, when the controlled foreign companies provisions come into play, the interest income which in reality is derived and beneficially owned by a resident of the Netherlands, goes through what they called a three-stage process. They stated:

> "16. First, the amount of chargeable profit of Spinneys on which corporation tax would be chargeable is computed on the various

[20] As the argument is not separately reported but is only to be gleaned from the Decision, it may be that I have misunderstood the Revenue's position.

[21] See paragraph 15 of the Decision.

assumptions contained in Sch 24; one is that Spinneys is assumed to be a United Kingdom resident company and the other is that it has claimed all the reliefs for corporation tax available to such a company. Next, those chargeable profits are apportioned to a different company, ie to Bricom Holdings. Lastly, Bricom Holdings is assessed. The assessment is not on Bricom Holdings' profits, as would have been the case if this had been a charge to corporation tax (see s 6(1) of the 1988 Act) which charges corporation tax on 'profits of companies'. Instead, Bricom Holdings is assessed to a sum equal to corporation tax on the amount of profit apportioned to it less the creditable tax apportioned to it; and the net sum is assessed on Bricom Holdings as if it were an amount of corporation tax chargeable on it.

17. Can it be said, at the end of that three-stage process, that art 11 of the Anglo-Netherlands Treaty applies to exempt that part of the net sum assessable on Bricom Holdings (ie the sum equal to corporation tax less creditable tax) which is attributable to the interest obtained by Spinneys from the Bricom Group Ltd? Put another way, is the subject matter of the s 747(4)(a) assessment recognisable as tax on that interest, or has the interest lost its original character in the process? In our view the interest has lost its character. The effect of the controlled foreign company charging code is to make the interest received by Spinneys an ingredient in the measurement of the 'sum equal to corporation tax ... on the apportioned amount' which, after deduction of creditable tax, is assessed on Bricom Holdings. The assessment appealed against by Bricom Holdings is a sui generis assessment on a notional 'sum equal to corporation tax'. The interest ingredient loses its character at the first stage of the process. By the time the assessment stage has been reached, art 11 has no application because the amount actually assessed is not 'income arising in one of the States which is beneficially owned by a resident of the other'; it is a sum equal to tax computed on the statutory assumptions and apportioned from the beneficial owner to its United Kingdom resident shareholder."

5.2 Comment on Decision

5.2.1 The First Stage

The Special Commissioners are in fact giving more than one reason for finding against the taxpayer on this point. Logically, their first point is that the interest ingredient loses its character at the first stage of the process; that is, because one is asked to ascertain the amount of the total chargeable profits of Spinneys on which corporation tax will be chargeable, computed on various assumptions, it

cannot be said that any part of that is interest. At first blush, this conclusion does not appear to be tenable. Simply because the company has, say, £3,000 of profits chargeable to corporation tax, consisting of £1,000 of interest, £1,000 of trading profits and £1,000 of rent, does not mean that the £1,000 of interest has lost its identity. Quite the contrary, it remains identifiable as a part of the whole. Indeed, it would actually be assessed to United Kingdom corporation tax under a different Schedule and Case from the rent and the trading profits.[22]

Now it is most unlikely that such experienced Commissioners made such a basic error. Possibly, their enthymematic reasoning was that the interest loses at the first stage its character as interest "derived and beneficially owned by a resident of the Netherlands", because of the hypothesis that, in this case, Spinneys is resident in the United Kingdom. If this is the learned Special Commissioners' reasoning, two comments can be made. Firstly, even on the assumption that Spinneys was resident in the United Kingdom, the interest would still have been exempt from United Kingdom tax under the terms of the Convention. See 12 below. As this point was not argued before the Commissioners, however, one can hardly criticise them for not having taken it into account. Secondly, it is irrelevant that a specific provision of United Kingdom law might deem income which is exempt from UK tax under the terms of a double tax convention to be income of a different category. A specific provision of municipal law does not alter the effect of a convention.[23] On the basis that the Convention had been incorporated into English law by statutory instrument, then it is to override express provisions of municipal law to the contrary, at least to the extent provided by Taxes Act 1988 section 788(3), which includes relief from corporation tax.[24]

5.2.2 The Second Stage

The second stage of the three-stage process is that the hypothetical chargeable profits of Spinneys are apportioned to Bricom. The Special Commissioners do not appear to place any reliance upon this stage of the process. They could, therefore,

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[22] Taxes Act 1988 section 9(3).

[23] Always assuming, of course, that the convention has been incorporated into United Kingdom law by virtue of another statutory provision which takes precedence over the former.

[24] A similar criticism is made of the Special Commissioner's decision in *Willoughby v IRC*, which the Special Commissioners in *Bricom* accepted, wrongly in my view, as good law. See 6 below.

compatibly with their reasoning *at this stage*,[25] have held that the mere fact that the income of a resident of another contracting state exempt from tax under a double taxation convention with the United Kingdom is apportioned to or deemed to be the income of a United Kingdom resident does not deprive the income of its exemption from tax. Indeed, it appears from paragraph 19 of the Decision that they remained open-minded on this fundamental point.

5.2.3 The Third Stage

It appears to be the third stage of the process upon which the Special Commissioners laid most stress. Bricom is not assessed to corporation tax on deemed profits. Instead, Bricom is assessed to a sum *equal to* corporation tax on the amount of profit apportioned to it, with a deduction for the creditable tax so apportioned. At this point, the learned Special Commissioners appear to be confusing two different arguments. One argument is that Bricom is not being charged to corporation tax at all. Yet that is the alternative argument, with which the Special Commissioners do not purport to deal at this point. Begging for one moment the question that a sum equal to corporation tax is corporation tax, the vital question *at this stage* is "corporation tax on *which* profits?" There is, in my view, no question but that the profits are the profits which have been apportioned to Bricom at stage two. The distinction between corporation tax at the appropriate rate on the apportioned profits and corporation tax at the appropriate rate on the apportioned *amount* of profits is a distinction without a difference.

Now the fact that the Special Commissioners' reasoning is somewhat contorted does not mean that it is wrong. What it is important to realise, however, is that the third stage of the process does not by itself convert that on which Bricom is being taxed from interest derived and beneficially owned by a resident of the Netherlands into income of some other variety. If the income has not been transmogrified at stage one or two, then it will not be transmogrified at stage three. If the Special Commissioners' conclusion at this point is correct it can be only because Bricom is not being charged to corporation tax on the income and in consequences no treaty exemption is available. That, however, is anticipating the next question.

5.2.4 The True Principle

Let us consider the matter from the point of view of basic principle. Standing back for one moment and ignoring the difference between corporation tax and a sum equal to corporation tax, what in substance is Bricom being taxed on? It is

[25] But see the comment on their further reasoning on the alternative point at 7 below.

as plain as a pikestaff that it is being charged to the disputed amount of corporation tax because, and only because, interest has arisen to Spinneys. If such interest had not arisen, then the Revenue would not be seeking to collect the tax in dispute. Once one has ascertained, on the true construction of the Convention, properly incorporated into United Kingdom municipal law, that such income is exempted from United Kingdom corporation tax, then it cannot, in my respectful opinion, matter one jot by what deeming provisions, by what fictions, or by what technicalities United Kingdom municipal law seeks to charge the income to tax. One looks to the substance and not to the technicality. What it is doing in substance is expressly prohibited by the Convention and therefore by section 788 of the Taxes Act which overrides, *inter alia*, section 747(4). I would therefore respectfully suggest that the learned Special Commissioners did not on this point perceive the wood for the admittedly dense and tangled thicket of trees into which Mr Henderson had snared them.

5.3 The Argument on *Hughes v Bank of New Zealand*

In distinguishing *Hughes v Bank of New Zealand* (1938) 21 TC 472, in which the House of Lords decided various statutory exemptions from income tax in respect of income from specified securities in the beneficial ownership of persons not ordinarily resident in the United Kingdom prevented the Revenue assessing a New Zealand bank which was beneficially entitled to such income on the income as part of its trading profits under Schedule D Case I as well as under Schedule C and Schedule D Case III, the Special Commissioners stated, at paragraph 18 of the Decision:

> "There the relevant question was whether the exempt gilts, owned by a non-resident bank, income tax-free in the hands of a non-ordinarily resident owner by virtue of General Rule 2(b) of Sch C, could be none the less chargeable to income tax under Case I of Sch D as forming part of the profits of the London branch of the bank. In that case the charging provision relied on by the Crown would have charged the interest to tax as the bank's income and it did not, in contrast to s 747(6)(a), require the assumption to be made that the bank, as owner, be regarded as ordinarily resident in the United Kingdom; and the charging provision did not, as here, involve any apportionment of those profits to a United Kingdom resident taxpayer. Because the bank retained its real non-ordinarily resident status for United Kingdom tax purposes, the income from the gilts retained its exempt status under Sch C. Here, however, the controlled foreign company code operates quite differently. It imports all the assumptions found in Sch 24, including that of United Kingdom residence, to the controlled foreign company; it deprives the chargeable profits of their real world status, apportions them to a different company and

assesses that company, not on the interest, but on a notional sum equal to tax."

The point made by Mr Andrew Park QC was a powerful one. An exemption was given by statute as respects the interest of certain securities. In the case of Indian Government Stock, exemption was contained in General Rules applicable to Schedule C. It was held that the Revenue could not wriggle out of the exemption by describing, quite properly, the income as something else, namely, in this case, trading profits. That was so even though the exemption was to be found in the Schedule C rules whereas trading profits were assessable under Schedule D. Mr Park QC, no doubt forcibly made the point that if income is in fact exempt from tax you do not deprive it of its exemption by calling it something else.

The Special Commissioners' argument that the provisions in *Hughes* did not require the assumption to be made that the bank, as owner, be regarded as ordinarily resident in the United Kingdom can only have any force if one once again ignores the basic principle[26] and puts the cart before the horse. If, on its true construction, the Convention makes income beneficially owned by a resident of the Netherlands exempt from United Kingdom taxes on income, then even an express provision in the Taxes Act which deemed the beneficial owner of the interest to be resident in the United Kingdom would still not bring the income into charge to United Kingdom tax.

The Special Commissioners' second point, that the charging provision did not in *Hughes*, as in *Bricom*, involve any apportionment of those profits to a United Kingdom resident taxpayer, looks a more promising ground of distinction. Yet once one ascertains that, on the true construction of the Convention, it is the interest itself which is exempt from tax and not the person who in fact beneficially owns it, then the distinction is of no relevance.

6 *IRC v Willoughby*

6.1 The Special Commissioners' Decision

The learned Special Commissioners then continued, at paragraph 19 of their Decision, with further reasoning, no doubt intended partly to elucidate and partly to expand their earlier reasoning on the supposed importance of the three-stage process:

[26] Set out at 5.2.4.

> "19. The chargeable profits on which the sum equal to corporation tax is computed are further removed from their original character as interest paid by a United Kingdom resident to a resident of the Netherlands by s 747(3) which results in their being apportioned to Bricom Holdings. If it had been the original interest which had been apportioned to Bricom Holdings as interest, this might not in itself have prevented the Treaty from applying to it. But it has already lost its character as interest before being apportioned. The situation is analogous to that found in *IRC v Willoughby* [1995] STC 143. Income which was 'industrial and commercial profits' of one person was deemed by s 739 to be income of another person, but its character as industrial and commercial profits was not preserved as it was charged to tax in the hands of the deemed recipient under Case VI of Sch D. Mr David Shirley, the Special Commissioner, found (at 168) that the double taxation arrangement with the Isle of Man could no longer be applied to the income in the hands of the deemed recipient. This part of the decision was not appealed and we respectfully agree with his reasoning."

6.2 General Comment

The first part of this paragraph is merely a reiteration of the (unsupportable), conclusion already reached: "[the interest] has already lost its character as interest before being apportioned."

The second part of paragraph 19 raises a fresh argument, the seeds of which were probably already present in paragraph 17.[27] An analogy is drawn with *IRC v Willoughby*. If *Willoughby* was right on this point, then one can see how the Special Commissioners thought the decision on the relevant point to be applicable to Bricom. The short answer, however, is that it was wrong.

6.3 The Special Commissioner's Decision in *Willoughby*

In *Willoughby v IRC*,[28] Professor Willoughby had been neither resident nor ordinarily resident in the United Kingdom since 1973. In July 1986 he took out a single premium personal portfolio bond with a company incorporated, managed, controlled and resident in the Isle of Man. He became ordinarily resident in the

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[27] See 5.1 above.

[28] [1995] STC 143 in the Court of Appeal, which contains the Special Commissioner's decision. The appeal of the Revenue from the judgment of the Court of Appeal will not be heard by the House of Lords before the spring of 1997.

United Kingdom from May 1987. The Revenue assessed him to tax on the income arising under that bond (and other bonds taken out by him later with the same insurers) for the year 1987–88 and subsequent years on the ground that he had sought to avoid income tax by the transfer of assets abroad and that Taxes Act 1988 section 739[29] therefore applied to deem the income which in reality belonged to the Manx insurer to be his for United Kingdom income tax purposes.

Robert Carnwath QC produced a whole armoury of arguments on behalf of the taxpayer, most of which proved effective with the learned Special Commissioner, Mr David Shirley. His sixth argument was that the income sought to be imputed to Professor Willoughby was exempted from taxation in the United Kingdom by art 3(2) of the Arrangement of 25th July 1955 scheduled to the Double Taxation Relief (Taxes on Income) (Isle of Man) Order 1955, SI 1955 No 1205, as being the 'industrial or commercial profits of a Manx enterprise'. It appears that it was common ground that the Manx insurer was a "Manx enterprise" as defined by article 2(1)(I) of the Arrangement and that its profits were 'industrial or commercial profits' within the meaning of article 3.

Mr Commissioner Shirley dealt with the issue in his Decision as follows:

> "14. Sixth issue
>
> This is whether art 3(2) of the Arrangement prevents s 739 applying to the industrial or commercial profits of Royal Life, an insurance company resident in the Isle of Man and not having a permanent establishment in the United Kingdom.
>
> Premiums were paid to Royal Life for the issue of policies to Professor and Mrs Willoughby. Income and gains have accrued to Royal Life, a Manx enterprise, from the investment fund attached to the bond. On redemption or surrender of a policy, Professor Willoughby or Mrs Willoughby or their respective estates are entitled only to the policy value with respect to each bond and not to the underlying investments contained in the fund attached to the bond.
>
> Article 3(2) of the Arrangement provides:
>
> > 'The industrial or commercial profits of a Manx enterprise shall not be subject to United Kingdom tax unless [as is not the case]

[29] For the first year of assessment, the relevant provision was Taxes Act 1970 section 478, which was identical to Taxes Act 1988 section 739. The argument and decision were based on the latter.

> the enterprise is engaged in trade or business in the United Kingdom through a permanent establishment situated therein ...'

A 'Manx enterprise' means 'an industrial or commercial enterprise or undertaking carried on by a resident of the Island' (art 2(1)(i)). Royal Life is such an enterprise. The term 'industrial or commercial profits' includes 'rentals in respect of cinematograph films' (art 2(1)(j)).

Mr Carnwath submits that the income and gains arising from the investments in the fund attached to the bonds accrue to Royal Life, are profits of Royal Life derived from its commercial activities and therefore are commercial profits of Royal Life, a Manx enterprise. Such profits 'shall not be subject to United Kingdom tax.' An Arrangement of this kind 'shall, notwithstanding in any enactment, have effect in relation to income tax and corporation tax in so far as [it provides]—(a) for relief from income tax, or from corporation tax in respect of income or chargeable gains ...' (s 788 (3)(a)).

Mr Carnwath argues that the exemption attaches to the profits. Section 739 attributes them (or part of them) to Professor Willoughby, a United Kingdom resident. Therefore they are exempt from United Kingdom tax. In support of this argument he cites *Padmore v IRC* [1989] STC 493[30] in which it was held that a United Kingdom resident partner of a Jersey resident partnership having no United Kingdom place of business was entitled to relief from United Kingdom tax in respect of his share of the partnership profits under an article contained in the Double Taxation Relief (Taxes on Income) (Jersey) Order 1952, SI 1952/1216, corresponding to art 3(2) of the Arrangement.

For the Crown Mr Tabbush contends that the exemption under art 3(2) is personal to the Manx enterprise: Royal Life cannot be taxed in the United Kingdom on its industrial or commercial profits. It does not follow that those profits cannot be taken as the measure of anyone else's profits. Secondly, he says that the 'investment income' of Professor Willoughby's portfolio does not form part of Royal Life's 'commercial profits' which must mean the net surplus arising from Royal Life's business of managing investments and available for distribution to Royal Life's shareholders. Only the charges and commission levied by Royal Life represent its profits. Most of the profits it is said must be kept in the funds attached to Professor Willoughby's bonds.

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[30] *Padmore* is discussed at 12 below.

> I go back to s.739(2). I ask myself what income of Royal Life has Professor Willoughby power to enjoy (now or in the future) which, if it were his income received in the United Kingdom would be chargeable to income tax? It must surely be the income arising from the investments owned by Royal Life accepted in specie as a premium or purchased with the cash paid by way of a premium. That income whether it would or would not have been chargeable to income tax apart from the provisions of s.739 is to be deemed to be income of Professor Willoughby for all the purposes of the Income Tax Acts. As part of Royal Life's income it would not have been chargeable in fact or by virtue of art 3(2), nevertheless it is to be deemed to be Professor Willoughby's income. May one apply the provisions of the Arrangement to that income deemed to be his when the actual income is not subject to United Kingdom tax for so art 3(2) provides? One cannot, as it seems to me, apply the provisions twice nor to two different people.
>
> In my opinion there is a distinction between actual income of an individual and actual income of another person which is deemed to be the income of the individual. Such income is not industrial or commercial profits of the individual nor quoad the individual is it deemed to be industrial or commercial profits or deemed to be his income as if it were such profits. I distinguish Padmore's case since Padmore has a real share in real profits of a real partnership. Professor Willoughby's income under s.739 is deemed to be his when in reality it is not his although the receipt of the actual income by Royal Life enures indirectly to some extent to his or his estate's ultimate benefit when he surrenders a policy or a policy matures.
>
> I hold therefore that the income of Royal Life deemed to be Professor Willoughby's income does not come within the provisions in art 3(2). It is not exempt from United Kingdom tax by virtue of the Arrangement."

6.4 The Revenue's First Argument in *Willoughby*

The Revenue thus adduced two separate arguments. The Commissioner found in its favour on the first argument and therefore did not go on to consider the second. The first argument is the general point of principle: is the exemption personal to the Manx enterprise? With respect, the learned Commissioner's reasoning on this aspect is defective. He stated firstly that one cannot "apply the provisions twice nor to two different people". Why not? He then went on to say that in his opinion "there is a distinction between actual income of an individual and actual income of another person which is deemed to be the income of the individual. Such income is not industrial or commercial profits of the individual nor quoad the

individual is it deemed to be industrial or commercial profits or deemed to be his income as if it were such profits."[31]

What the learned Commissioner should have done was to construe the words of the Arrangement. Do they say that a Manx enterprise is not to be taxable, in which case the exemption would clearly be a personal one, or do they say that the profits of a Manx enterprise are to be exempt from taxation in the United Kingdom, in which case the exemption would be non-personal and would *prima facie* extend to any person who would otherwise be taxable on those profits? There can to my mind be little doubt that article 3(2) is so worded as to fall into the second category.

That, however, is not conclusive, so far as the Commissioner is concerned. He reasons that, while the profits are deemed to be Professor Willoughby's, they are not in fact industrial or commercial profits of his nor deemed to be industrial or commercial profits of his. Ergo, it seems, no double taxation relief is to be allowed. With respect, this reasoning is misconceived and ignores the basic principle[32] by putting the cart before the horse. True, under section 739(2), the income of the non-resident is deemed to be that of the transferor for all purposes of the Income Tax Acts. True, it is not in fact his industrial or commercial profits nor is it deemed to be his industrial or commercial profits. What the learned Commissioner has forgotten is that the Arrangement overrides "anything in any enactment": see Taxes Act 1988 section 788(3). One must firstly determine the meaning of the Arrangement. Once one has established that, on its true construction, it exempts the profits in question from taxation and that the exemption is not a personal one, then no provision of the Income Tax Acts can withdraw that exemption. Even if section 739 expressly provided that all income of a non-resident which it deemed to be that of the transferor should also be deemed to be, say, an annual payment, that provision would not deny the transferor treaty relief. Put another way, the exemption is conferred on all profits which are in reality industrial or commercial profits of a Manx enterprise, without any restriction to those profits which United Kingdom tax law does not unilaterally deem to be profits of another description.

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[31] I agree that the Commissioner was fully entitled to distinguish *Padmore's* case, discussed at 12 below, on the basis that Mr Padmore has a real share in real profits of a real partnership

[32] See 5.2.4.

6.5 The Revenue's Second Argument in *Willoughby*

While the Special Commissioner did not adjudicate on the second argument, it is in my opinion unanswerable. My views have not changed since I wrote my article 'Personal Portfolio Bonds & Taxes Act 1988 Section 739' in Volume 3 Issue 3 page 203 of this *Review*, in which I commented on a digest of the Special Commissioner's decision. I stated, at page 209 last divide:

> "Thus there was raised, in a particularly convoluted form, a very simple point. Suppose that a wholly owned offshore company of mine is entitled to United Kingdom source interest. Under the Double Taxation Treaty between the state of the residence of the company and the United Kingdom such interest is exempted from United Kingdom tax. Is the exemption personal to the company or can I also take advantage of it if I am assessed under s.739?
>
> "In this case, the argument was far less clear-cut. It was not clear that the income from the underlying fund was at all the same thing as the industrial or commercial profits of the Manx insurer. Now "industrial or commercial profits" must mean trading profits. Yet exemption was being claimed in respect of that part of its gross receipts which would, in effect, eventually be handed over to the taxpayer and could thus form no part of its profits. One would have thought, therefore, that this argument could simply not get off the ground in this case."

6.6 Conflict between *Bricom* and *Willoughby*

While the Special Commissioners in *Bricom* purported to follow Mr Commissioner Shirley in *Willoughby*, a close examination will show that their reasoning was quite different and even inconsistent.

It will be recalled that the Special Commissioners had stated earlier in paragraph 19 of their Decision in *Bricom*: "If it had been the original interest which had been apportioned to Bricom Holdings as interest, this might not in itself have prevented the Treaty from applying to it." Now this is not at all the same reasoning as that of Mr Commissioner Shirley. His reasoning in no way depended upon industrial or commercial profits of the Manx insurer having lost their character before, during or after being apportioned. It was no part of his reasoning that those industrial and commercial profits were charged to tax in the hands of the deemed recipient under Schedule D Case VI and not under Schedule D Case I (trading profits). His point was quite simply that the income was "not industrial or commercial profits of the individual". If Mr Commissioner Shirley was right, then it would have followed that if in the case of *Bricom* "it had been the original

interest which had been apportioned to Bricom Holdings as interest", Bricom would still not have been able to take advantage of the Convention! Moreover, Mr Commissioner Shirley was right to place no reliance upon the fact that the income of the Manx insurer was chargeable in the hands of Professor Willoughby under Schedule D Case VI. As *Hughes'* case so clearly shows, if the income was in fact exempt from tax, then it mattered not under which Schedule or Case the Taxes Acts would otherwise have allowed it to be assessed.

7 Was Bricom Charged to Corporation Tax?

The Special Commissioners then went on to consider *obiter* the alternative contention of the Crown, namely that while tax under section 747 is a tax, it is not corporation tax. The sum assessed under section 747(4)(a) is a sum 'equal to' corporation tax; it is to be assessed on and recovered from the resident company 'as if' it were an amount of corporation tax chargeable on that company. Thus when the taxes that are the subject of the Convention, in art 2(1), are examined (and so far as is material these are income tax and corporation tax), the controlled foreign company charge is not covered by the Convention.

It must be admitted that this contention is one which is arguable either way. The Special Commissioners found in favour of the Crown and held that the controlled foreign company charge is not corporation tax.

8 Was Bricom Charged to a Tax "Substantially Similar" to Corporation Tax?

Now the Convention applied also to taxes "substantially similar" to corporation tax.[33] On this point, the Special Commissioners concluded that while the matter was one of degree, they inclined to the view that the differences from corporation tax are not so great as to prevent the tax from being substantially similar to corporation tax. With respect, that view was correct.

9 Is the Convention Fully Incorporated into United Kingdom Law?

It was at this point that the Crown raised the most shocking argument. If the view to which the Special Commissioners inclined was correct, then it followed that the United Kingdom was obliged, as a matter of international law, to give the relief to Bricom. It is a fundamental feature of the British constitution that a treaty does not take effect in municipal law except insofar as it is incorporated by Act of

[33] See article 2(3).

Parliament.[34] The Revenue argued that section 788(3) of the Taxes Act provides that a double taxation convention which has been incorporated into United Kingdom law, as the Convention had, is to have effect only "in relation to income tax and corporation tax insofar as they provide - (a) for relief from income tax or from corporation tax in respect of income or chargeable gains..."

Mr Andrew Park QC, raised arguments that the charge imposed under the controlled foreign companies legislation was to be included in the reference to "corporation tax" in section 788(3). That, again, was a point which was arguable both ways and on which the Special Commissioners found in favour of the Revenue.

10 Can the Revenue Plead Non-Incorporation of the Convention into United Kingdom Law?

What is quite extraordinary is that the Crown should have relied upon its own failure properly to implement the treaty into United Kingdom law. True, as a matter of constitutional law, Bricom was, if the Special Commissioners were right in rejecting Mr Park's argument on this point, not entitled to the relief. On the other hand, there is a good argument that as a matter of administrative law it was quite wrong for the Revenue to raise the point. As the Court of Appeal held in *R v Commissioners of Inland Revenue ex parte Unilever Plc*[35] the Revenue must act fairly and reasonably. They must have regard to "the spirit of fair dealing which should inspire the whole of public life". While matters of fairness and reasonableness are notoriously subjective, it is to my mind grossly unfair for the Crown to negotiate a treaty which confers an exemption from tax, to procure that such treaty is broadly enacted as part of the law of the land, but then to seek to collect tax in breach of the treaty in reliance on a loophole in the enabling Act.[36] It is particularly obnoxious where, as here, the Revenue have, by procuring the Order in Council, represented to the public that the treaty has been incorporated into United Kingdom law. The case is at least as strong as where, without just cause, they seek to resile from a published Extra-Statutory Concession or a

[34] Whether expressly or by delegated legislation duly authorised by Act of Parliament.

[35] [1996] STC 681.

[36] It would be quite different, of course, if Parliament had deliberately legislated to deny taxpayers an exemption conferred by a convention, as Blackburne J held had happened in *Boote v Banco do Brasil SA* [1996] STC 339.

statement of practice or similar public pronouncement. By reneging on their prior statement they are defeating the taxpayer's legitimate expectations.

11 The EC Treaty Point

Mr Andrew Park QC reserved the right to argue at a later stage that the manner in which the Board of Inland Revenue sought to apply section 747(4)(a) in the present circumstances was contrary to article 52 of the EC Treaty. That will indeed be an interesting argument, provided that the Crown does not prevent it from being raised on the basis that insufficient evidence has been lead before the Special Commissioners to establish a factual foundation for it.

12 The "Show Stopper"

Finally, in my view there was a complete answer to the Revenue's case. What is apportioned is a controlled foreign company's chargeable profits, namely the amount of the total profits of the company on which, on the assumptions in Schedule 24, after allowing for any deductions available against those profits, corporation tax would be chargeable. Schedule 24 paragraph 1(1) provides that the foreign company shall be assumed to be resident in the United Kingdom. Paragraph 1(2) makes it clear that nothing in sub-paragraph (1) requires it to be assumed that there is any change in the place or places at which the company carries on its activities. Paragraph 4(1) provides that, subject to two immaterial exceptions, where any relief under the Corporation Tax Acts is dependent upon the making of a claim or election, the company shall be assumed to have made that claim or election which would give the maximum amount of relief and to have made the claim or election within any time limit applicable to it.

These assumptions are deeming provisions. The Court of Appeal in *Marshall v Kerr*[37] laid down the proper approach to such deeming provisions. Peter Gibson J, with whom Simon Brown LJ and Balcombe LJ agreed, said, at page 366c:[38]

> "For my part I take the correct approach in construing a deeming provision to be to give the words used their ordinary and natural meaning, consistent so far as possible with the policy of the Act and the purposes of the provisions so far as such policy and purposes can be ascertained; but if such construction would lead to injustice or absurdity, the application of

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[37] [1993] STC 360.

[38] The House of Lords agreed with the Court of Appeal on this point: see [1994] STC 368 per Lord Browne-Wilkinson.

> the statutory fiction should be limited to the extent needed to avoid such injustice or absurdity, unless such application would clearly be within the purposes of the fiction. I further bear in mind that because one must treat as real that which is only deemed to be so, one must treat as real the consequences and incidents *inevitably*[39] flowing from or accompanying that deemed state of affairs, unless prohibited from doing so."

Although Spinneys was to be assumed to be resident in the United Kingdom, that was not inconsistent with its being also resident in the Netherlands. We are expressly told by Schedule 24 paragraph 1(2) that the mere assumption of residence in the United Kingdom does not require any further assumption that there is any change in the place or places at which the company carries on its activities. The company is thus assumed to be dual resident. Under the Convention, it is therefore deemed for the purpose of the treaty to be a resident of the Netherlands: see article 4(3) "where by reasons of the provisions of paragraph (1) a person other than an individual is a resident of both States, then it shall be deemed to be resident in the State in which its place of effective management is situated."

As a resident of the Netherlands for the purposes of the Convention, Spinneys would, even if resident in the United Kingdom as a matter of United Kingdom municipal law, have been entitled to claim relief from corporation tax on interest derived and beneficially owned by it. Schedule 24 paragraph 4(1) requires one to assume that it would have made a timeous claim for such relief. In that case, the interest would have fallen out of account in calculating its chargeable profits. Hence, the interest could not be apportioned to Bricom.

If this argument is correct, it is a complete "show stopper". In comparison with the many deep and subtle points which teased the minds of Leading Counsel and of the Special Commissioners, it is of remarkable simplicity. It may well be, of course, that there is some equally simple answer to it which I have not had the wit to discover. As matters stand, however, the only reason I have for supposing that I am wrong is that it did not occur to either of the distinguished Leading Counsel or either of the learned Special Commissioners that it might have any relevance.

13 *Padmore v IRC*

Mr Commissioner Shirley in *Willoughby* felt able to distinguish *Padmore v IRC*.[40] Rightly, in my view. *Padmore* concerned a multinational partnership, many of the

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[39] Italics supplied.

[40] [1989] STC 493.

partners of which were resident in the United Kingdom but which, because it was managed and controlled in Jersey, was deemed both under United Kingdom law and, it was assumed, Jersey law, to be resident in Jersey. It was held that it constituted a "Jersey enterprise" for the purpose of the Double Taxation Arrangement of 24th June 1952 between Jersey and the United Kingdom. Under article 2 of the Arrangement, the commercial or industrial profits of a Jersey enterprise which did not carry on business in the United Kingdom through a permanent establishment situate in the United Kingdom were exempt from United Kingdom tax. On the basis that the partnership was a Jersey enterprise, that article admittedly applied. The Revenue contended that it applied only to the profits of the partnership but not to the shares of profits of the individual partners. Under United Kingdom (and, it seems, Jersey) tax law, a partnership is fiscally transparent.[41] Partnership profits are allocated to its partners and are then taxed as part of their income in accordance with their individual circumstances. While it was true that the partnership as a whole had a reporting requirement and each of the partners was jointly and severally liable for the whole of the tax payable on the partnership profits, this did not affect the general principle.

The Court of Appeal rejected the Revenue's argument. The Arrangement expressly exempted profits of the Jersey enterprise from United Kingdom tax and if it exempted the whole of the profits it must likewise exempt shares of the profits. While that result was unexpected, it flowed inevitably from a true construction of the treaty. The only real question which arose in the litigation was whether the courts were going to decide according to the true construction of the Arrangement or were going to deprive the taxpayers of what was doubtless an unintended benefit. All four judges in the High Court and the Court of Appeal made their decision according to law and not according to prejudice. While leave to appeal to the House of Lords was refused, this was perhaps because Parliament had already intervened, at the Revenue's instigation, to withdraw the relief retrospectively in every case except the one being litigated. In any civilised country which had a more than half-decent constitution, this would, of course, have been quite impossible.[42]

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41 This must, since the decision of Walker J in *Memec PLC v Commissioners of Inland Revenue* 24th October 1996, as yet unreported, be read subject to the qualification that the position may be different if the partnership is formed under a law other than that of England.

42 The relief was withdrawn only in the case of partners of partnerships. Subject to that, *Padmore* is still good law, so that a United Kingdom domiciled, resident and ordinarily resident individual can take advantage of the Arrangement when he is entitled to profits, or a share of profits, of a "Jersey enterprise" in cases other than where both the enterprise is a partnership and he is a partner of it.

It will be readily evident that *Padmore* does nothing to help resolve the problem as to whether a person who is under municipal law *prima facie* assessable to tax on or by reference to the income of another can rely on an exemption from tax contained in a double taxation convention which exempts that other from tax.

14 Conclusion

While the Special Commissioners' decision in *Bricom* is the first authoritative United Kingdom statement on the most important question of the interrelationship between double taxation treaties and municipal anti-avoidance provisions, it is unlikely to be the last.