[2013] UKFTT 463 (TC)

TC02853

Appeal number: TC/2009/14430

INCOME TAX – Employment Income – PAYE & NIC – tax avoidance scheme – bonus –whether bonus of restricted securities under Ch 2 Part 7 ITEPA 2003 or whether excluded as "money" under s420(5)(b) ITEPA 2003 – bonus excluded from Part 7 as "money" – GAAR proposal and enactment irrelevant to interpretation of provision – change in law which required re-engineering of scheme mid-way through did not affect conclusion that there was a scheme to pay bonus in money as opposed to securities -Regulation 80 determinations and s8 decisions upheld - appeals dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

LM FERRO LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE SWAMI RAGHAVAN
LYNNETH SALISBURY

Sitting in public at 45 Bedford Square, London on 26 and 27 November 2012

Dougal Powrie, chartered accountant, for the Appellant

Tim Brennan QC, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. The appellant, LM Ferro Ltd, runs a community pharmacy shop in Cirencester. The company is owned and run by Mr Ferro, a qualified pharmacist and his wife. The business was run profitably and the company built up a sizeable amount of cash. Mr Ferro received advice on how to extract value from the company in a tax-efficient manner. He used a scheme devised by Powrie Appleby which involved the appellant subscribing for shares in another company, transfer of those shares subject to a forfeiture restriction to Mr Ferro, his transfer of the shares to another company and various other steps.

2. It is not in dispute that these arrangements amounted to a scheme designed to minimise or avoid tax or that Mr Ferro's bonus was a reward for services. The issue is whether the scheme worked. The appellant's case is that the bonus amounted to an award of securities that is not subject to income tax. The Respondents argue Mr Ferro was rewarded with money and the bonus is taxable as earnings. They say tax (under PAYE) and Class 1 National Insurance contributions are payable on a bonus of £300,000 paid by the appellant to Mr Ferro.

3. The appeal is against a determination under Regulation 80 of the Income Tax (Pay As You Earn) Regulations 2003 in the amount of £115,113.18 and a notice of decision under s8 of the Social Security (Transfer of Functions, etc) Act 1999 determining liability to pay Class 1 National Insurance contributions of £43,276.48 (the amount due being £42,263.79). The relevant tax year is 2004-5.

Scheme in brief

4. The legislative backdrop to the scheme is Part 7 of the Income Tax (Earnings and Pensions) Act 2003 ("ITEPA"). The relevant detail of Part 7 is set out below as it is necessary to be aware of the particular provisions in order to understand how the scheme sought to enter Part 7 and pass through it without being subject to a tax charge.

5. At a high level the legislation provides an exemption from income tax at the point when shares related to a person's employment are received but then seeks to charge tax later when "chargeable events", as defined, happen such as when the shares are disposed of in a certain way and to certain persons. The scheme used by the appellant sought to ensure the bonus recipient received bonus in the form of shares which were subject to this special regime but that value could be obtained for the bonus recipient without triggering a chargeable event under the regime.

Statutory provisions

6. The scope of Part 7 ITEPA 2003 is set out in s417 ITEPA as follows:

> "**417 Scope of Part 7**
>
> (1) This Part contains special rules about cases where securities, interests in securities or securities options are acquired in connection with an employment
>
> (2) The rules are contained in-
>
> Chapter 2 (restricted securities)…"

7. Before looking at Chapter 2 it is necessary to mention certain provisions in Chapter 1 which are relevant to the definitions in Chapter 2 and its scope. Section 420 ITEPA provides a definition of "securities" in s420 ITEPA which so far as material provides as follows:

> "**420 Meaning of "securities" etc.**
>
> (1) Subject to subsections (5) and (6), for the purposes of this Chapter and Chapters 2 to 5 the following are "securities"—
>
> (a) shares in any body corporate (wherever incorporated) …
>
> (b) debentures, debenture stock, loan stock, bonds, certificates of deposit and other instruments creating or acknowledging indebtedness …
>
> (5) The following are not "securities" for the purposes of this Chapter or Chapters 2 to 5—
>
> (a) cheques and other bills of exchange, bankers' drafts and letters of credit …
>
> (b) money and statements showing balances on a current, deposit or savings account, …"

8. Section 421B headed 'Application of Chapters 2 to 4', provides where relevant as follows:

> "(1) Subject as follows (and to any provision contained in Chapters 2 to 4) those Chapters apply to securities, or an interest in securities, acquired by a person where the right or opportunity to acquire the securities or interest is available by reason of an employment of that person or any other person.
>
> (2) For the purposes of subsection (1)—
>
> (a) securities are, or an interest in securities is, acquired at the time when the person acquiring the securities or interest becomes beneficially entitled to those securities or that interest (and not, if different, the time when the securities are, or interest is, conveyed or transferred) …
>
> (3) A right or opportunity to acquire securities or an interest in securities made available by a person's employer … is to be regarded

for the purposes of subsection (1) as available by reason of an employment of that person unless [certain immaterial conditions apply]

…

(8) In this Chapter and Chapters 2 to 4—

"the acquisition", in relation to employment-related securities, means the acquisition of the employment-related securities pursuant to the right or opportunity available by reason of the employment,

"the employment", in relation to employment-related securities, means the employment by reason of which the right or opportunity to acquire the employment-related securities is available … and

"employment-related securities" means securities or an interest in securities to which Chapters 2 to 4 apply …"

9. Section 422 ITEPA sets out the scope of Chapter 2 which is headed "Restricted securities":

"422 Application of this Chapter

This Chapter applies to employment-related securities if they are—

(a) restricted securities …

at the time of the acquisition."

10. Section 423 defines "restricted securities" as follows in so far is relevant:

"(1) For the purposes of this Chapter employment-related securities are restricted securities … if—

(a) there is any contract, agreement, arrangement or condition which makes provision to which any of subsections (2) to (4) applies, and

(b) the market value of the employment-related securities is less than it would be but for that provision.

(2) This subsection applies to provision under which—

(a) there will be a transfer, reversion or forfeiture of the employment-related securities … if certain circumstances arise or do not arise,

(b) as a result of the transfer, reversion or forfeiture the person by whom the employment-related securities are held will cease to be beneficially entitled to the employment-related securities, and

(c) that person will not be entitled on the transfer, reversion or forfeiture to receive in respect of the employment-related securities an amount of at least their market value (determined as if there were no provision for transfer, reversion or forfeiture) at the time of the transfer, reversion or forfeiture …"

11. Section 425 ITEPA provides that there is no charge in respect of acquisition in certain cases as follows:

"425 No charge in respect of acquisition in certain cases

(1) Subsection (2) applies if the employment-related securities—

(a) are restricted securities … by virtue of subsection (2) of section 423 (provision for transfer, reversion or forfeiture) at the time of the acquisition, and

(b) will cease to be restricted securities … by virtue of that subsection within 5 years after the acquisition …

(2) No liability to income tax arises in respect of the acquisition, except as provided by … [provisions not relevant]."

12. Section 426 imposes a charge on the occurrence of a "chargeable event" in relation to the employment-related securities. A "chargeable event" for this purpose has the meaning given by s427. The relevant chargeable events are:

"**427 Chargeable events**

(3) The events are:

'(a) the employment-related securities ceasing to be restricted securities … in circumstances in which an associated person is beneficially entitled to the employment-related securities after the event …

(c) the disposal for consideration of the employment-related securities, or any interest in them, by an associated person otherwise than to another associated person (at a time when they are still restricted securities or a restricted interest in securities)."

13. The term "associated person" is defined in s421C which provides:

"**421C Associated persons**

(1) For the purposes of this Chapter and Chapters 2 to 4 the following are "associated persons" in relation to employment-related securities—

(a) the person who acquired the employment-related securities on the acquisition,

(b) (if different) the employee, and

(c) any relevant linked person.

(2) A person is a relevant linked person if—

(a) that person (on the one hand), and

(b) either the person who acquired the employment-related securities on the acquisition or the employee (on the other),

[are or have been connected or (without being or having been connected) are or have been] members of the same household. (*the wording in square brackets replaced the words "are connected or, although not connected, are" with effect from 18 June 2004 although nothing turns on this change*)

(3) But a company which would otherwise be a relevant linked person is not if it is—

(a) the employer,

(b) the person from whom the employment-related securities were acquired,

(c) the person by whom the right or opportunity to acquire the employment-related securities was made available, or

(d) the person by whom the employment-related securities (or the securities in which they are an interest) were issued."

14. Section 429 disapplies the charge under s426 in certain circumstances. It provides where relevant as follows:

"429 Case outside charge under section 426

(1) Section 426 (charge on occurrence of chargeable event) does not apply if—

(a) the employment-related securities are shares … in a company of a class,

(b) the provision by virtue of which the employment-related securities are restricted securities … applies to all the company's shares of the class,

(c) all the company's shares of the class (other than the employment-related securities) are affected by an event similar to that which is a chargeable event in relation to the employment-related securities, and

(d) subsection (3) or (4) is satisfied.

(2) For the purposes of subsection (1)(c) shares are affected by an event similar to that which is a chargeable event in relation to the employment-related securities—

(a) in the case of a chargeable event within section 427(3)(a) (lifting of restrictions), if the provision mentioned in subsection (1)(b) ceases to apply to them,

(b) in the case of a chargeable event within section 427(3)(b) (variation of restriction), if that provision is varied in relation to them in the same way as in relation to the employment-related securities, or

(c) in the case of a chargeable event with section 427(3)(c) (disposal), if they are disposed of.

(3) This subsection is satisfied, if immediately before the event that would be a chargeable event, the company is employee-controlled by virtue of holdings of shares of the class.

(4) This subsection is satisfied if, immediately before that event, the majority of the company's shares of the class are not employment-related securities."

15. The elements of the scheme are described in outline below by reference to the relevant provisions of Part 7.

16. The appellant subscribed for new shares in a special purpose vehicle (incorporated 2 months before), Stoneygate 123 Ltd. ("SG123 Ltd.") at a substantial premium. The appellant transferred the shares to Mr Ferro.

17. The shares were subject to forfeiture for 95% of their market value in the event Mr Ferro ceased to be employed by the appellant for any reason whatsoever including death within 12 months of the date of their acquisition.

18. It is argued by the appellant that the transfer of shares constituted a reward for Mr Ferro's services and was earnings within the definition of s62 ITEPA 2003 and further that the appellant received restricted employment related securities and that there was no tax charge on their acquisition under s425 ITEPA.

19. The appellant's advisors had received advice that if employment-related securities were shares of a particular class in a company, all of the shares of that class had been acquired either for no payment or for a payment less than their market value, and the company was employee controlled by virtue of the employment-related securities then, when the restriction came to an end or was lifted, there was no income tax charge. Value in the shares could be realised, if the employee wished, by for instance selling the shares or liquidating the company, although the owner of the shares would potentially be subject to a capital gains tax charge. Thus it was sought to rely on the carve out for chargeable events set out in s429(1) ITEPA.

20. On 7 May 2004 it was announced by the government that changes would be made to Part 7 of ITEPA which would take effect from that date. The changes gave rise to concerns by the appellant's advisers that the original planning would not have the effect that had been intended. The new legislation was to include an anti-avoidance provision at s429 (1A) ITEPA which meant the exemption in s429 not be accessed if it was the case that:

> "something which affects the employment-related securities has been done…as part of a scheme or arrangement the main purpose (or one of the main purposes) of which is the avoidance of tax or national insurance contributions."

21. Following advice from counsel further steps were taken.

22. Mr Ferro transferred his shares in SG123 Ltd. to San Gabriel 108 ("SG108"), an unlimited liability company which had been incorporated 4 months before the transfer.

23. This is said to be a sale and to be a transfer to an associated company such that there was no chargeable event for the purposes of s427(3)(c) ITEPA. SG108 is said to be "relevant linked person" in that it is "connected" with Mr Ferro, (the person who acquired the employment-related securities). The meaning of "connected person" for ITEPA 2003 is given in Part 2 Schedule 1 which at the relevant time referred to s839 Taxes Act 1988. Section 839(6) provided:

> "a company is connected with another person if that person has control of it or if that person or persons connected with him together have control of it."

24. Mr Ferro is said to have control of SG108 it being a wholly owned subsidiary of the appellant, LM Ferro Ltd., a company he had control of.

25. Further it is said SG108 did not fall within any of the exceptions to the definition of "relevant linked person" set out in s421C(3). It was not a) the employer, b) the person from whom the employment-related securities were acquired, c) the person by whom the right or opportunity to acquire the employment-related securities was made available, or d) the person by whom the employment-related securities (or the securities in which they are an interest) were issued.

26. The appellant guaranteed payment of the price to Mr Ferro.

27. SG108 transfers the beneficial interest in the shares in SG123 Ltd. back to the appellant by declaration of a dividend in specie of shares in SG123 Ltd. and declares that it holds the shares in SG123 Ltd. on trust for the appellant.

28. The dividend in specie is said to not be a disposal for consideration and therefore not a chargeable event under s427(3)(c) ITEPA.

29. The appellant borrows money from SG123 Ltd. which it then uses to discharge the debt to Mr Ferro the guarantee having been triggered.

Evidence

30. On behalf of the appellant we had a witness statement from Mr Ferro and heard oral evidence from him which was subject to cross-examination. Mr Ferro was obviously uncomfortable and nervous in being subjected to cross-examination. Some answers were given rather tentatively belying our impression that he was concerned as to the implications of his answers counting against him. This meant he did not give a clear response to certain questions. We took Mr Ferro's unfamiliarity and trepidation in being involved in proceedings before the Tribunal into account in assessing his evidence. Our overall impression was that he was an honest witness.

31. There was also a statement but no oral evidence from Mr A C Cook of MacIntyre Hudson LLP concerning valuation of the securities. There were a number of points raised by the Respondents which gave us concerns about the report's reliability which we set out later in this decision at [100] to [108].

32. We had several bundles of documentary evidence comprising various board and members' meeting minutes of the appellant and the other companies used in the scheme, correspondence and telephone attendance notes recording communications between Mr Ferro, his tax advisor, and the scheme designers, and correspondence between the parties.

Facts

33. We had before us a short agreed statement of facts which were not in dispute which we have integrated into our findings of fact.

34. The appellant is a trading company which was set up in around 1998 and whose business is running a single community pharmacy shop in Cirencester.

35. The appellant's auditor and tax advisor is Mr Modi with whom the appellant meets at least annually.

36. At all relevant times the appellant was controlled by Mr Leo Ferro and owned by Mr Ferro and his wife Mrs Marta Ferro, who were the only directors of the appellant. Mr Ferro is a professional pharmacist.

37. On 27 March 2003 a meeting took place between Mr Modi and Mr Ferro. Mr Modi kept manuscript notes of what was discussed against the relevant printed agenda item. Under point 5 headed "How do we grow the business?" Mr Modi wrote:

> "May buy a 2nd branch using the money in the co.. But wait for OFT comments / DOH ruling in April '03"

38. Point 6 of Mr Modi's notes next to the heading "Extraction of monies from company through Bonus (D Powrie Scheme) >£200k in Co. bank account." records:

> "Leo did express an interest and wanted to know more. I said I would arrange a meeting at appropriate time. Will think about it but may buy a 2nd pharmacy. He will revert in due course (OFT enquiry /? New centre? An issue though.)"

39. The references to the OFT (Office of Fair Trading) and (DOH) Department of Health were explained to us by Mr Ferro as relating to an OFT enquiry that was ongoing at the time in relation to the limitation of contracts for pharmacies and which had made him think he may need to diversify the business.

40. On 25 September 2003 Mr Ferro called Mr Modi in relation to a letter Mr Modi had sent to him on 19 September 2003. Mr Modi's note records:

> "He said that when we met in March '03 we discussed a number of possibilities with the business including buying a second pharmacy and extracting a bonus in a tax-efficient manner" – second pharmacy purchase through LM Ferro difficult – worried about collapse in goodwill…went on to ask about extraction of bonus from the company so that he would re-invest the money on properties either commercial or buy to let. He however wanted a tax efficient proposal. Mr M mentions Dougal Powrie may have a scheme appropriate for his circumstances… confirmed yes we can include in 30/9/03 accounts provided that the bonus is paid by 30 June 2004 i.e. within 9 months - …said he wants to proceed on that basis for 30/9/03."

41. On 30 September 2003 the appellant's accounts for year ended 30 September 2003 which were drawn up on 12 July 2004 show under "Director's remuneration" a

director's bonus of £300,000. The accounts explain a transaction was undertaken after year end under which the company invested £300,000 in the shares of Stoneygate 123 Limited, and that the shares were transferred, subject to a restriction to Mr Ferro by way of bonus and further that the transfer would constitute earnings of the Director.

42. On 12 December 2003 Mr Powrie saw counsel about a "key strategy" that Mr Powrie had been describing to Mr Modi. This was described as follows in a letter from Mr Powrie to Mr Modi dated 15 December 2003:

> "…the aim of the strategy is to enable a director or executive of a company to take out a bonus in such a way that the company gets a full corporation tax refund on the amount paid but there is no NIC not [sic] does the executive or director suffer any personal tax. Further, he ultimately ends up with cash in his hands; there is an intermediate stage where it is an investment company but this does not need to be for terribly long and he could, if necessary, borrow some of the money."

43. On 12 February 2004 a meeting was held between Mr Powrie, Mr Modi and Mr Ferro. Mr Powrie's note of the meeting was prepared on 16 February 2004. Mr Powrie explained the various stages of what was termed the "0% bonus scheme". These were injecting money into a Newco, giving Newco shares subject to condition to Mr Ferro by way of bonus and then waiving the conditions. Once the shares with conditions in the Newco had been given to Mr Ferro and the restrictions lifted, it was explained that the next stage was that if Mr Ferro so wished, he could liquidate the new company.

44. On 13 February 2004 an application for companies house registration of SG123 Ltd. was made by Powrie Appleby (Secretaries) Limited.

45. On 17 February 2004 Stoneygate 123 Limited was incorporated.

46. On 25 February 2004 Mr Modi recorded on a copy of the above note in manuscript that:

> "£300k is a possibility as the company has excess funds of £300k which it doesn't need."

47. On 4 March 2004 Mr Ferro telephoned Mr Modi. Mr Modi's note of the conversation headed "Bonus" states:

> "he wants to proceed with specific scheme discussed…£300,000 would be about right for the reward to him for the hard work put into the business over the last few years… He is also concerned about the new contract, OFT situation and future of pharmacy business. He thought that he may need to diversify and invest the money in other business ventures or property investments. He will think about it when he has received the bonus..."

48. On 30 March 2004 Powrie Appleby wrote to Mr Ferro enclosing forms 288a and 288b, and stock transfer forms. It was explained that these were in relation to Mr Ferro's consent to act as director of SG123 Ltd. Mrs Ferro's consent to act as company secretary, and Powrie Appleby's resignation as director and company secretary. The letter included instructions to sign where indicated and to fax and post the signed forms and transfer back in order that they could be filed at Companies House.

49. On 31 March 2004, two SG123 Ltd. ordinary shares of £1 were transferred to the appellant. The forms set out above were completed.

50. On the same day a meeting of the Board of Directors of SG123 Ltd. took place. Present were Mr R. Appleby (corporate representative of Powrie Appleby Limited) and Mr D. Hannah (corporate representative of Powrie Appleby (Secretaries) Limited). The meeting approved the transfer of 1 ordinary share of £1.00 from Powrie Appleby Limited and 1 ordinary share of £1.00 Powrie Appleby (Secretaries) Limited to the appellant.

51. Resolutions were passed 1) approving the acquisition of the entire issued share capital of the SG123 Ltd. by the appellant, 2) approving the conversion of ordinary shares in the capital of SG123 Ltd. to 'A' Ordinary Shares and 'B' Ordinary Shares and 3) adopting new Articles of Association.

52. In relation to transferability of the 'B Shares, the Articles provided that where such shares were transferred to someone who was an employee, director or officer of any company who was the holder of the 'A' Ordinary Shares, the 'B' shares would be subject to forfeiture for 95% of their market value should the holder of the 'B' shares cease for any reason (including death of the holder) to be employed by the holder of the 'A' Shares during a period of one year after the transfer of the 'B' shares.

53. On 1 April 2004 Mr Ferro telephoned Alyson Kyle at Powrie Appleby saying that he had been to the bank to arrange for the new account for the company to be opened. Ms Kyle's note of the conversation records the following:

> "…he also went on to say that the bank had asked what the trading activity would be, he said he was unsure what to tell them so he said that he had presently traded as a pharmacist and this may apply to a new company. I said that normally I would say it was to assist in the remuneration of key executives but it is difficult to say what the company will do in the future. Leo said he would fax and post the signed documents back to me today."

54. What Mr Ferro said to the bank and what he meant by it is the subject of dispute between the parties. This issue is considered further at [118] to [123].

55. On 5 April 2004 Alyson Kyle at Powrie Appleby e-mailed Mr Modi to confirm that everything was in place "in respect of appointing new directors and transferring the initial two shares etc". She asked Mr Modi to let him know when the bank account was open and said she could then arrange for the "subscription and relevant

documents" to be drawn up. She also asked for confirmation of which year the bonuses were paid for.

56. On 8 April 2004 Mr Modi e-mailed Alyson Kyle to seek confirmation various forms had been filed at Companies House as the bank account would only be opened after a search at Companies House had been performed. He also asked for confirmation that "planning is under way and that you have sent the Minutes etc. to be signed". She e-mailed back the same day to say she could not proceed until the bank accounts are opened. The paperwork could be drafted but they could not send anything until funds were ready to move.

57. The correspondence between Mr Modi and Alyson Kyle makes reference to other companies using a scheme. Those other companies were also using "Stoneygate companies".

58. On 21 April 2004 Mr Modi and Alyson Kyle spoke on the telephone and agreed Mr Ferro could instruct his bank that day to subscribe for shares in the new company by asking them to transfer funds.

59. On 27 April 2004 Mr Modi e-mailed Alyson Kyle stating:

> "I am told that the bank account is now opened and £300,000 is also transferred today into Stoneygate Ltd. Can you please send him all the paperwork for signature at his home address. He is going on holiday on 15 /5/04. So it would be good to get it all signed up before then."

60. On 27 April 2004 funds of £300,000 were transferred from the appellant to SG123 Ltd.

61. A series of meetings took place and a number of documents were signed by Mr Ferro and his wife. These are set out below. We accept that the meetings did take place, however perfunctory the discussions around the agenda items were, and that the documents were signed by the person purporting to sign them. However, in relation to the dates of 27 April 2004 and 29 April 2004 which are stated on these documents it is a matter of dispute as to whether the meetings took place on these stated dates and whether documents were signed on these stated dates.

(1) A board meeting of the appellant took place. Mr and Mrs Ferro were present. They approved a proposal to make a bonus to Mr Ferro of £300,000. The minute records that having sought the advice of Powrie Appleby it transpired the most tax efficient manner for the payment of such a bonus was by means of a transfer of shares to Mr Ferro. The shares would be 'B' Ordinary shares in SG123 Ltd. and it was necessary for the appellant to acquire this company. The Board approved draft written resolutions approving the acquisition of the entire issued share capital of SG123 Ltd. and the subscription of 'B' Ordinary shares.

(2) The appellant passed written resolutions approving the acquisition and the subscription of the shares. A board meeting of SG123 Ltd. was held at which it was resolved that 998 'B' Ordinary Shares were to be allotted to the appellant.

(3) A board meeting of SG123 Ltd. approving transfer of 'B' Ordinary Shares in the company took place.

(4) A written resolution of the members of SG123 Ltd. was passed approving the transfer of 998 'B' Shares from the appellant to Mr Ferro, and special resolutions relating to the transfer.

(5) A board meeting of the appellant took place approving the transfer of 'B' ordinary shares in SG123 Ltd. to Mr Ferro, a written resolution of the members approving such transfer, and special resolutions relating to the transfer.

(6) Stock transfer forms transferring the 998 'B' Shares from the appellant to Mr Ferro were signed.

(7) A letter from the appellant to Mr Ferro was signed by Mr Ferro on behalf of the appellant. An acknowledgement of receipt of that letter was signed by Mr Ferro. The letter set out the forfeiture conditions of the 'B' Shares. It explained the transfer of shares to Mr Ferro as follows:

> "As you are aware L M Ferro Limited has made arrangements for the acquisition of the entire issued share capital of Stoneygate 123 Limited and the subscription of 998 'B' Ordinary Shares of £1 each in the capital of that company. It is intended to transfer to you all of such 'B' Ordinary Shares as a reward to you for your hard work in your duties as an employee in the year to 30 September 2003."

62. On 29 April 2004 in response to an e-mail from Mr Modi asking Alyson Kyle whether the paperwork had been sent to the appellant for signature Ms Kyle replied "LM Ferro – docs are going out in tonight's post". It was put to Mr Ferro that given this e-mail the meetings could not have taken place on the 27 April 2004 and 29 April 2004 but must have taken place later. Mr Ferro said he followed the instructions in relation to the documents sent to him and that he assumed he would have acted promptly in sending them back.

63. A telephone call took place on Tuesday 4 May 2004 between Alyson Kyle and Mr Ferro. Ms Kyle prepared a note of this call on 5 May 2004 in which she reported Mr Ferro as saying that he had sent the documents on Saturday morning by registered post. We accept from this that Mr Ferro had sent the documents back by registered post the previous Saturday morning (ie 1 May 2004). In the telephone call he asked whether the documents had been received yet. There was no evidence to suggest the documents had been faxed or e-mailed to Mr Ferro on 29 April 2004 or prior to that. If the documents had been or were going to be sent by those means we think this would have been mentioned by Ms Kyle in response to the chaser e-mail from Mr Modi. We also noted that apart from the stock transfer forms all documents had typed dates. We think it unlikely that Mr Ferro would have gone to the trouble of inserting typed dates after having received the documents and there is no evidence to suggest that this is what he did.

64. Taking into account Mr Ferro's evidence that he would have sent documents back promptly, the fact that he was concerned about the documents not having been

received and of Ms Kyle's 29 April 2004 e-mail saying the documents were going out in that night's post we find that on the balance of probabilities the documents were not received until 30 April 2004.

65. Given Mr Ferro sent them back on Saturday morning (1 May) we find that it was more likely than not the meetings took place and documents were signed on 30 April 2004. We accept that Mr Ferro followed the instructions he was given and the order of the meetings took place in the order he had been instructed to carry them out.

66. On 7 May 2004 HMRC issued a press release announcing an amendment to the Employment Related Securities legislation in Part 7 of ITEPA 2003. The amendments were introduced in the Finance Act 2004 and were effective from 7 May 2004.

67. At some point between this date and 1 June 2004 advice was sought from counsel by Powrie Appleby about the "way forward". On 1 June 2004, in response to an e-mail from Mr Modi enquiring as to what action to take for clients including LM Ferro who were "half way through under the 0% scheme", Rachel Ingham, on behalf of Powrie Appleby responded that they had spoken to counsel who had given a favourable opinion in relation to extracting a dividend from the Newco.

68. On 2 July 2004 Powrie Appleby (Secretaries) Ltd applied for registration of SG108 which was then incorporated as an unlimited company on 9 July 2004.

69. Relevant disclosures were made to the Respondents under the Disclosure of Tax Avoidance Schemes (DOTAS) regulations under the transitional rules in Finance Act 2004. The disclosure made on 28 October 2004 was allocated reference number 16613935.

70. The Appellant acquired SG108 on 8 November 2004 by purchase of the entire issued capital of two £1 ordinary shares, at par.

71. On the same day the appellant applied for and was allotted a further £1 ordinary share in SG108 at a premium of £288,965.88. The consideration was left outstanding.

72. A share acquisition agreement was executed on 8 November 2004 by Mr Ferro, SG108 and the appellant. Mr Ferro agreed to sell 998 'B' Shares of SG123 Ltd. to SG108 for the sum of £287,515.88.

73. This sum is stated in the agreement to be 95% of the market value of the shares in accordance with "restrictions" which are defined as being the various restrictions on transfer of the shares set out in the letter of 29 April 2004 from the appellant to Mr Ferro.

74. Clause 2.1 of the Share Acquisition Agreement states the consideration for the sale and purchase of the shares shall be the payment by SG108 to Mr Ferro "at any time on demand" by Mr Ferro after the date of the agreement. Under Clause 2.3 the appellant guaranteed to Mr Ferro the payment by SG108 of the purchase price in accordance with clause 2.1.

75. Payment of the consideration was left outstanding.

76. On 10 November 2004 Mr Ferro gave a power of attorney to Rachel Ingham, of Powrie Appleby, to sign stock transfer forms in relation to the sale of his shares in SG123 Ltd. to SG108.

77. On 10 November 2004 stock transfer forms transferring the SG123 Ltd. shares to SG108 were executed under power of attorney.

78. At a board meeting on 10 November 2004 SG108 resolved to convert a share premium account to distributable reserves and declared a dividend in specie of its shareholding in SG123 Ltd. The share premium account was cancelled in its entirety.

79. The meeting was held at the offices of Powrie Appleby. The Board consisted of Dougal Powrie who was Director for Powrie Appleby Corporate Services and Secretary for PA Secretaries.

80. SG108 executed a Declaration of Trust on 10 November 2004 declaring that the investment in 998 'B' ordinary shares of £1 each in the capital of SG123 Ltd. was to be held by SG108 as nominee of the appellant.

81. On 10 November DOTAS disclosure 92742840 was made to the Respondents.

82. Correspondence took place between Mr Modi and Ms Ingham at Powrie Appleby about further arrangements. On 10 December 2004 Mr Modi stated that he had thought from previous conversations with Powrie Appleby that Mr Ferro could "draw the money" within 2 weeks of sorting all the paperwork. He was concerned that it had now been some 5 weeks and they had still not got the money. Mr Modi e-mailed on 14 December 2004 asking:

> "Are you saying that I can now ask my clients to transfer the money from their Stoneygate company back to employer company and then draw out the cash, as previously advised. Or do we wait for you to sort the paperwork first and I ask my clients to do the transfers."

83. Ms Ingham replied on 16 December 2004 to Mr Modi:

> "…your clients can action the following transactions if the directors see fit i.e. they can make the payments now. In short, yes the payments can be made straightaway. The precise chain of events is as set out below so the paperwork will need to reflect this. However provided there is no objection to these steps the money can be paid immediately and the paperwork dealt with later.
>
> LM Ferro Ltd – Stoneygate 123 Ltd can loan its funds to LM Ferro Ltd (its 100% shareholder). Leo Ferro is owed by San Gabriel 108 £288,965.88. This debt can be settled with a transfer from LM Ferro Ltd (because LM Ferro Ltd owes £288,966.88 to San Gabriel 108…"

84. On 22 December 2004 SG123 Ltd. transferred £303,905.32 to the appellant.

85. On 23 December 2004 a payment of £288,965.88 was made to Mr Ferro by the appellant.

86. We have difficulty reconciling Ms Ingham's explanation for how the payment arose in view of other documents we had before us. Pursuant to the share acquisition agreement of 8 November 2004 the appellant guaranteed payment of the purchase price of £287,515.88 to Mr Ferro. Subsequent minutes and resolutions of the appellant and SG108 refer to SG108 owing money to the appellant in the amount of £287,515.88 but no explanation is offered for how the debt arose. We think the more probable explanation for the basis on which the payment was made to Mr Ferro as intended by the scheme is that £287,515.88 of the amount paid to Mr Ferro represented a payment made pursuant to the guarantee made by the appellant to Mr Ferro in the share acquisition agreement and that this gave rise to SG108, as purchaser of the shares, owing a debt to the appellant.

87. In the event the "paperwork" referred to above was dealt with some time later in November 2005.

88. On 10 November 2005 a conversation took place between James Bland at Powrie Appleby and Mr Modi in which it was discussed whether it would be possible for his clients, one of whom included Mr Ferro to make actual money transfers. Mr Bland was told that Mr Ferro had spent the money. This is at odds with Mr Ferro's evidence, which we accept, that he had not spent the money at this point in time. He did not spend it until some years later in 2007 when he used it to buy a property for his daughter.

89. On 11 November 2005 Mr Ferro was e-mailed a set of documents with detailed instructions for their completion which Mr Ferro followed. SG123 Ltd. held a board meeting as did the appellant where it was proposed SG123 Ltd. should re-register as an unlimited company. The necessary companies house forms and amended articles of association were completed and returned to Powrie Appleby. Mr Bland filed these at Companies House.

90. On 21 November 2005 Mr Bland confirmed in an e-mail to Mr Ferro that SG123 had been re-registered as an unlimited company. Mr Bland asked Mr Ferro to sign and date an attached resolution including a clause in SG123's articles of association that "the company may by special resolution reduce its share capital and any share premium account in any way" and to send this back to him. Mr Ferro signed the resolution on 22 November 2005.

91. On 24 November 2005 Mr Bland e-mailed Mr Ferro enclosing what he described as "the very final documents to finalise the bonus planning for the company" together with detailed instructions for their completion and asked that they be faxed back on the same day they were signed.

92. The instructions included details as to the sequence and to the time of the meeting to be inserted on the meeting minutes e.g. for the second meeting "Time should be 10 minutes after time of the previous meeting" and for the third, "Time

should 10 minutes after time of the previous meeting, i.e. 20 mins after the first meeting".

93. On 25 November 2005 Mr Bland sent more documents to Mr Ferro to be signed.

94. On 26 November 2005 SG123 passed a resolution authorising its directors to reduce the company's share premium account by the transfer of £299,002 to distributable reserves. The board proposed a dividend of £301.884 per share be recommended to the shareholder. The shareholders approved the proposal. Mr Ferro was authorised to proceed with payment of the dividend.

95. At a meeting of the appellant on the same day it was noted:

> "that £302,668 was presently owed to the company's subsidiary Stoneygate 123 (comprising a loan of £303,905, £2 unpaid share capital less £1,239 owed to the company in respect of the Stoneygate 123's corporation tax paid on its behalf by the company). However the company was in turn owed £301,884 by Stoneygate 123 in respect of a dividend and it was resolved that the company would immediately repay £301,884 of the loan by offsetting the dividend due from Stoneygate 123 against the debt owed to Stoneygate 123 leaving an outstanding debt of £784 and that the relevant accounting entries are made in the Company's books".

96. On 26 November 2005 the board of the appellant noted that it was owed £287,515.88 by SG108 but that it owed an equal sum to SG108 in respect of shares it had subscribed for. It was resolved that the shares be paid up in full and Mr Ferro was given authority to make the necessary arrangements.

97. On 28 November 2005 at a board meeting of SG108 it was noted that the sum of £287,515.88 was owed by SG108 to the appellant but that that sum was equal to the sum unpaid on the SG108's share capital. It was noted that the appellant wished to pay up the unpaid share capital by offsetting the debt due to it. It was resolved that the share capital was considered paid up in full and that SG108's debt to the appellant was considered to be settled in full.

98. San Gabriel 108 was dissolved on 22 August 2006.

99. On 15 May 2007 SG123 Ltd. was dissolved pursuant to s652A of the Companies Act 1985.

Evidence on market value of restricted securities

100. We had before us an Expert Report of MacIntyre Hudson LLP dated 22 August 2011. The Respondents had not called the author of the report, Mr Cook, on the basis that the errors in the report they sought to draw our attention to were so self-evident and incapable of being addressed through explanation in their view that it would have been disproportionate to call the witness to put those points to him. In the event the appellant did not take issue with the criticisms levelled at the report. Irrespective of

the report the appellant argues there is a trivial effect on market value arising from the 1 year survival condition and this is enough to get them into the definition of "restricted security".

101. However whether the shares were "restricted securities" is not directly in point as the issue this case turns on is whether the award of bonus is to be regarded as falling within the "money" exclusion to Part 7 in s420(5)(b) such that Part 7 does not apply.

102. To the extent it is relevant to find that the securities were prima facie capable of being restricted securities in order that the "money" exception was in issue we find that the 1 year survival condition had an effect however miniscule or trivial and so was capable of being a "restricted" security. We agree with the appellant that the fact that if the contingency was triggered the 5% amount would revert to the appellant company (controlled by Mr Ferro and his wife) and to "family wealth" as the Respondents put it, was irrelevant.

103. We agree with the criticisms levelled against the report by the Respondents and set these out for the sake of completeness. The errors are in our opinion fundamental and mean the report cannot be relied upon in relation to making any findings of fact as to the market value of the securities.

104. In the description of the valuation approach and the restrictions on the "B" Ordinary Shares the author states:

> "The Articles of Association contain restrictions in respect of the transfer or the B Ordinary Shares. In the circumstances of the arrangement whereby Mr Leo Ferro received the shares from LM Ferro Limited, those restrictions are considered a commercial arrangement to incentivise Mr Leo Ferro to remain with the Company."

105. We agree with the Respondents' observation that this was at complete variance with the other evidence before us. Mr Ferro and his wife owned the Company. There was simply no basis to think Mr Ferro needed incentivising to remain with the company he owned with his wife.

106. In paragraph 4.10 the report states:

> "the restrictions …meant that if Mr Ferro ceased to be employed by LM Ferro Ltd for any reason, including death for a period of 12 months from acquisition, the consideration for his shares would have been at a 95% discount…".

107. The figure of 95% is wrong. It should be 5% to open market value. This error is transposed to the "discount suffered" column in the author's assessment of the discount for the restrictions on the 'B' ordinary shares.

108. In assessing the impact of the survival condition the report makes certain obviously misconceived assumptions about life expectancy. It takes a life expectancy of 19.3 years for 65 year olds in 2007 and gives Mr Ferro, at 50, a life expectancy of

24.3 years. It then states the likelihood in year 1 of dying is 1 in 24.3. This fails to take account that by being younger a person is less likely to die in year 1 than in later years say year 24. The 4% probability figure derived from an assumption of likelihood based on 1 in 24.3 is incorrect. The incorrect figure is then used as a basis for subsequent calculations. This, together with the 95%/5% error above, means the total expected discount figure of 8.6% cannot be relied on.

Discussion

The issue for consideration – was the reward for services within the exclusion for "money" in s420(5)(b) ITEPA 2003?

109. It was not in dispute that the bonus was a reward for services. Further it was accepted by the appellant that the scheme which it had entered into was an arrangement which was designed to minimise or avoid tax.

110. Although the Respondents had previously indicated the possibility that it would argue that Part 7 ITEPA was not relevant because Mr Ferro had an entitlement to earnings at a point in time earlier than the point at which he was awarded the shares this argument was not pursued.

111. The issue between the parties was whether the bonus arrangements fell out of the scope of Part 7 ITEPA because they did not amount to a payment of "securities" (as the appellant argues) but were a payment of "money" which was excluded in s420(5)(b) from the definition of "securities" (as the Respondents argue).

General approach

112. In the words of Ribeiro PJ in *Collector of Stamp Revenue v Arrowtown Assets Ltd* [2003] HKCFA 46 at [35]:

> "The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically."

113. This was cited by Arden LJ in *Astall v Revenue and Customs Commissioners* [2009] EWCA Civ 1010 at [36]. That there must be a realistic appraisal of facts was also confirmed *Tower MCashback LLP v HMRC* [2011] UKSC 19 (Lord Walker at [80]) and by the Court of Appeal in *HMRC v PA Holdings Ltd* [2011] EWCA Civ 1414.

114. Although the general approach of a making a realistic appraisal of facts and discerning the provisions purposively is not contested, the parties part company as to what the facts are when realistically appraised, and also on the purpose of the legislative provisions.

115. The question of whether the arrangements fell within the exception for "money" in s420(5)(b) governs whether Part 7 is relevant. This question is therefore prior to the question of whether, if Part 7 applies, the steps in the scheme were successful at

enabling the appellant to negotiate its way through the detailed provisions of that code to escape a tax charge. These fall to be considered if it is determined that the "money exception does not apply. Having said that, it will be relevant in construing the "money" exception to look at the provisions in Part 7 more generally. Looking at Part 7 more widely is also relevant in considering one of the appellant's arguments to the effect that the prescriptive and complex nature of Part 7 means that it cannot be surprising if the scheme used by the appellant is successful in its object.

Realistic appraisal of facts: issues in dispute – what was the role of SG123 Ltd.?

116. Central to the issue of what the realistically appraised facts are, is the question of the role and intended role of SG123 Ltd. The shares awarded to Mr Ferro were shares in this company.

117. The appellant's case is that Mr Ferro wanted to, and could, use SG123 Ltd. as a vehicle for other business and investment interests. He had no need for the money. The Respondents disagree. Mr Ferro was the controlling and complete owner of a cash rich company and wanted to extract money from it to use for whatever purpose he wanted to apply it to. The £300,000 in SG123 Ltd. was in a "wrapper" and Mr Ferro was simply seeking to get it out without falling over tax hurdles e.g. payment of dividends, directors' fees or salary under an employment contract if he had one. It was unrealistic to think Mr Ferro would have kept the company and used it as a trading vehicle. If he had done that there would have been a chargeable event when the 12 month forfeiture restriction on the shares expired.

Mr Ferro's answer to the bank when asked what SG123 Ltd. would be used for

118. Related to above issue there was a factual issue as to what Mr Ferro had told the bank when they had asked him what SG123 Ltd. would be used for and what his intentions were in relation to it.

119. When asked what SG123 Ltd. was for, Mr Ferro is recorded in Powrie Appleby's telephone attendance note as saying that "he presently traded as a pharmacist and this may apply to a new company". When it was put to him in cross-examination that he had no intention of using it as a pharmacy business Mr Ferro's response was guarded and he did not give a clear explanation as to what his intention was. The Respondents say Mr Ferro was not dishonest but he was caught flat-footed. He knew the company was part of a scheme to extract a bonus but was embarrassed and gave a significantly inaccurate answer when asked what the trading activities of the SG123 Ltd. would be. There was no justification or commerciality for saying SG123 Ltd. was going to be used for another pharmacy business.

120. The appellant points out the manner Mr Ferro gave his answers reflected his feeling that he was doing something wrong in following through instructions as to necessary meeting procedures whereas most of the time he was doing what business men do in relation to meeting documentation and minutes which are drafted by advisers. There was confusion about long term and short-term objectives and Mr Ferro was not sure which question he was answering. It was possible for the company

to be used both for getting the money out and for further investment and there was no conflict between the two.

Discussion on role of SG123 Ltd.

121. Dealing with Mr Ferro's answer to the bank first, we accept from a note of a conversation between Mr Modi and Mr Ferro that back in April 2003 Mr Ferro was thinking at that point in time about the possibility of using the money in the appellant to buy a second branch. To that extent, the possibility of buying a second pharmacy branch was not something that was manufactured after the event for the purposes of these proceedings.

122. What we reject however is the suggestion that it was thought SG123 Ltd. would be used as a vehicle for setting up another pharmacy branch. We do not think Mr Ferro had a specific intention at the time he spoke to the bank to use SG123 Ltd. for another pharmacy business. There is no documentary evidence supporting the use of SG123 Ltd. as a pharmacy business.

123. We find that Mr Ferro did tell the bank the company "may be used" for a pharmacy business but we do not accept this statement reflected his intention at the time. We think he knew SG123 Ltd. was part of the scheme but in contrast to other steps in the scheme in relation to which he had received detailed instructions he had not been given instructions on what to say to the bank. He did not know what answer to give and therefore gave an answer, which he thought would sound plausible to the bank. He was concerned enough about having given the "right" answer such that he called Powrie Appleby to tell them about what he had said. If Mr Ferro had genuinely thought the company might be used to buy a pharmacy we think it likely that he would have thought about this before setting up the bank account and having a conversation with the bank. He would likely have mentioned the issue to his advisers and there would not then be any reason to call to tell Powrie Appleby to tell them that this was the answer he had given and to seek reassurance as to its implications.

124. We disagree with any suggestion that SG123 Ltd. would be used as a vehicle to invest in property or to make other investments. Although theoretically possible it was simply unrealistic to think that it would be used in this way for a number of reasons.

125. We note that as of 8 November 2004 Mr Ferro had agreed to sell all the SG123 Ltd. shares he had been awarded to a wholly owned subsidiary (SG108) of his company, the appellant LM Ferro Ltd. in return for cash. We do not think this is consistent with him wanting to retain an interest in SG123 Ltd. as a property or other investment vehicle to be held by him. If there was any concern about holding businesses through LM Ferro Ltd as indicated by some notes of previous consultations with Mr Modi, Mr Ferro is unlikely, we think, to have assumed, and could not reasonably have assumed, that any difficulties could be sidestepped by holding property or investments through a wholly owned subsidiary of the appellant.

126. What was realistic at the time the shares in SG123 Ltd. were awarded was borne out by the reality of what actually happened. None of Mr Ferro's subsequent actions

are consistent with him having the intention of using SG123 Ltd. as an investment vehicle or a means by which to buy another pharmacy.

127. In any case we are not persuaded why a business person in Mr Ferro's position would choose to hold investments, or property through a limited company rather than in their own name. Although it is of course possible that a company could be used in this way, there was no explanation as to why this would make sense for Mr Ferro. The claim that SG123 Ltd. was to be used in such a way is simply not credible.

128. We also note the fact that SG123 was subsequently re-registered as an unlimited company; a vehicle which as the name suggests does not limit liability to members making it even less suitable as a vehicle for trading.

129. There is a distinction between what realistically would be done with SG123 Ltd. and what was possible. It was possible to use SG123 Ltd to hold property or other investments but in our view Mr Ferro did not intend to use it in this way and there was no realistic prospect that SG123 Ltd. was to be used in this way.

What was the purpose of the statutory provisions?

130. The appellant says the result of no tax being exacted following the transactions undertaken is firmly within the purpose of the legislation. Referring to *Mayes v HMRC* [2010] STC 1 the appellant says that advantage may be taken of detailed statutory codes with the result that artificial tax avoidance may succeed. Part 7 ITEPA is such a statutory code. It sets out a complicated set of rules which do not apply a tax charge when shares are transferred to a director but only thereafter applies a tax charge when one of a number of highly prescribed events take place. The point was made by the Upper Tribunal (UT) at [165] in *UBS AG & Another v HMRC* [2012] UKUT 320 (TCC) that:

> "Chapter 2 [of Part 7] contains a very detailed and prescriptive code for dealing with restricted securities, in the context of a Part which had as one its main objectives the countering of tax avoidance. Experience has shown that advantage can sometimes be taken of detailed statutory codes of this general nature in a way that is resistant to a Ramsay analysis with the result that even the most artificial of tax avoidance schemes may succeed in their object."

131. The UT then go on to give the chargeable event regime in the context of life insurance policies and the decision in *Mayes* as an example of an instance where a scheme was successful in view of such a code.

132. The Respondents say the result of no tax being exacted is outside the purpose of the provisions and refers to the purpose as explained in the Supreme Court's decision in *Grays Timber Products v HMRC* [2010] UKSC 4. The clear purpose of Part 7 is to provide tax rules for awards of shares (generally, if not necessarily, in the employer's enterprise or a part of it) as a means of retaining and incentivising employees.

133. As set out in *Grays Timber* (Lord Walker (at [5]-[7]) and Lord Hope (at [56])), the Respondents say Part 7 reflect three different legislative purposes. First, there is Parliament's recognition that it is good for the economy and for social cohesion for employees to own shares in the company for which they work. Second, that if arrangements of this sort are to act as effective long-term incentives, the benefits which they confer have to be made contingent, in one way or another, on satisfactory performance. Third, it is the legislative purpose to eliminate opportunities for unacceptable tax avoidance. It is said that if there is any theme in Part 7 it is one of anti-avoidance and the closing down of perceived tax loop-holes.

Examination of Part 7 and the "money" exception – relevance of prescription / detail to construing purpose?

134. It is worth noting the further explanation in the Supreme Court's analysis of Part 7 at [5] that where benefits conferred are to be made contingent on satisfactory performance that this creates a problem because:

> "…it runs counter to the general principle that employee benefits are taxable as emoluments only if they can be converted into money, but that if convertible they should be taxed when first acquired…"

135. After quoting from Lord Radcliffe in *Abbot v Philbin* [1961] AC 352 Lord Walker then goes on to explain:

> "[6] The principle of taxing an employee as soon as he received a right or opportunity which might or might not prove valuable to him, depending on future events, was an uncertain exercise which might turn out to be unfair either to the individual employee or to the public purse…Parliament soon recognised that in many cases the only satisfactory solution was to wait and see, and to charge tax on some "chargeable event"(an expression which recurs through Pt 7 either instead of , or in addition to, a charge on the employee's original acquisition of rights.
>
> [7] That inevitably led to opportunities for tax avoidance. The ingenuity of lawyers and accountants made full use of the "wait and see" principle embodied in these changes in order to find ways of avoiding or reducing the tax charge on a chargeable event, which might be the occasion on which an employees's shares became freely disposable (Ch 2)…"

136. In relation to the appellant's reliance on *Mayes* it is correct that the Court of Appeal makes the point that prescriptive and detailed legislation may be prone to exploitation. But, the basis for this is not that prescription and detail in itself means there is no purpose but that the prescriptive code points in different directions making it difficult to discern a purpose. It is not sufficient in our view to point to a code being prescriptive and then assume it therefore has no purpose.

137. Examining the statutory provisions we note the following in the light of the above purposes as set out by the Supreme Court. An exhaustive definition of "securities" is provided which includes "shares". However, "money" is excluded.

That exclusion is consistent with the purposes outlined by the Supreme Court. In particular, where an employee is awarded "money" the value will not on the face of it depend on future events. There is no reason to wait and to charge tax instead of or in addition to a charge on the acquisition of money.

138. Chapter 2 applies to securities which are "employment-related securities". These according to s421B ITEPA are securities which are acquired by a person where the right or opportunity to acquire securities is available by reason of an employment of that person or any other person. This provision coupled with the definition of "restricted securities" is consistent with the purpose set out by the Supreme Court that benefits in order to be effective may have to be made contingent on performance.

139. The chargeable events set out in s427 ITEPA of restrictions being lifted, varied or of the shares being disposed of are all consistent with the idea that there are points in time at which value can be said to pass. In terms of the "wait and see" principle referred to by the Supreme Court they are when it becomes necessary to "see" having done the waiting.

140. Section 429 provides exemption for situations where all the company's shares of the class (other than the employment-related securities) are affected by an event similar to that which is a chargeable event in relation to the employment-related securities. This means that where e.g. those securities are disposed of as a part of a wider transaction whose purpose is therefore unlikely to be about realising value from the employment related securities a chargeable event does not arise. Exempting disposals where they arise for reasons unrelated to employment is consistent with a regime focussed on employment-related securities.

141. Beyond referring us to statements that Part 7 is complex and technical the appellant has not pointed us to any statutory provisions which would suggest that Lord Walker's analysis in *Grays Timber* as to the underlying purposes of Part 7 is not to be accorded its due weight.

142. We therefore prefer the Respondents' interpretation of purpose. While, as highlighted by Lord Hope's judgment in *Grays Timber* at [56], there are difficulties in drawing conclusions as to how the charging provisions in each Chapter are to applied if the overall aim is consistency in particular in relation to the meaning of "market value" Lord Hope's suggested approach was to not to try to draw conclusions from the application of that term in other parts of Part 7. Any difficulties arising from a consistent interpretation of "market value" are in any case not on point on the issue of ascertaining the purpose underlying the exclusion of "money" from Part 7. In contrast to *Mayes* it has not been shown to us that the code has provisions which point in different directions making it impossible to discern a purpose.

143. The statements of the UT in *UBS* set out above must also be read in the light of their earlier statements in [162] (quoted below) which make it clear that the UT contemplated that there would be certain schemes (described as "money in - money out") which would not be successful in falling outside the "money" exception. Their

observations about Chapter 2 cannot be taken to mean that contrived and artificial schemes will necessarily succeed because of the complexity of the statutory code.

Relevance of GAAR proposal?

144. The appellant also made an argument along the lines that the proposals for a GAAR (General Anti-Abuse Rule) would be irrelevant if *Ramsay* type arguments could apply to a device which enabled a director to be remunerated at the cost of only a comparatively small capital gains tax charge.

145. Proposals are simply that and do not have force of law. The argument did not go anywhere at the time it was made. But, since the hearing a general anti-abuse rule has been enacted in the Finance Act 2013 with effect from Royal Assent (17 July 2013) in relation to arrangements entered into after that date. The significance of that was understandably not addressed in the parties' submissions. Nevertheless, even if the appellant's argument is applied across to the enactment of the proposal rather than the proposal we think it is misconceived. First, this is because the general anti-abuse rule is not a rule of interpretation. Rather, it provides for a system of counter measures that may or may not be taken by HMRC to counteract abusive tax schemes. That there is now such a system cannot in our view affect the Tribunal's views as to what the statutory purpose of particular legislation is. Second, even if the rule was capable of colouring the Tribunal's interpretation of the statutory purpose of particular provisions, it could not, we think, assist the appellant in relation to how legislation which was in place prior to enactment of the GAAR proposal should be interpreted and applied to arrangements which were not capable of being covered by the enacted proposal.

Construing the "money" exception - the authorities

The UT's decision in UBS

146. The statutory construction of the "money" exception was considered by the UT in *UBS and another*. Both parties made reference to this case and it is worth setting out some background to the decision before going to the UT's views on statutory construction.

147. *UBS and another* concerned a tax avoidance scheme which was designed to enable the appellant banks (UBS and Deutsche Bank) to provide substantial bonuses to employees in the tax year 2003/04 in a way that would escape liability to income tax and national insurance contributions through an award of redeemable shares (in the case of UBS these were termed Non-Voting Shares ("NVS")) in a special purpose offshore company set up to participate in the scheme. It was intended the shares would be "restricted securities" subject to the special taxation regime contained in Chapter 2 of Part 7 ITEPA. As described by the UT on appeal at [6], the issues in the two appeals could be grouped under three headings.

148. First, whether the employees became entitled to be paid their bonuses in money before the sums allocated to them were applied in acquiring shares under the scheme.

Apart from in relation to a guaranteed element of bonus in relation to 10 or so employees the FTT found that no entitlement crystallised before the scheme was set in motion. The UT agreed there was no entitlement but also held that was the case for the employees with a guaranteed element of bonus.

149. Second, if the answer to the first issue was no, whether the shares were "restricted securities" as defined in s423 ITEPA, and if so whether the employees were entitled to an exemption under s429 ITEPA on the happening of a chargeable event when the shares ceased to be subject to the relevant restriction. The FTT held the shares were not "restricted securities" on materially different factual grounds in both appeals, but that if they were wrong on that point the s429 exemption (on materially different facts) would be available for both appeals. The UT disagreed that the exemption under s429 was available in relation to Deutsche Bank.

150. Third, in the alternative, could it be concluded by application of the *Ramsay* principle that on a realistic appraisal of the facts the scheme fell outside the scope of Chapter 2 altogether? The FTT concluded in both appeals that it could. The UT held in both appeals the scheme could not be characterised in this way.

151. In this case the Respondents are not pursuing an argument on entitlement and it is the UT's discussion on the third strand which is most relevant to the issue in this case.

152. The appellant referred us in particular to the following passages in which the UT set out their view on any argument that the *UBS* scheme fell within the "money" exception. At [162] the UT explained:

> "Unless all the FTT meant was that the securities were not restricted securities, in other words merely stating other reasons for their earlier conclusion, the only plausible basis for such a contention, in our judgment, would be if, on a realistic appraisal of the facts, the scheme was not one which provided securities (in the form of the NVS) to employees, but one which provided them with money. By virtue of ITEPA, s 420(5)(b), 'money' is excluded from the definition of 'securities' which applies for the purposes of Chs 1 to 5. We readily accept that, in an appropriate case, it might well be possible to construe 'money' in this context purposively, and to treat the exception as applying to arrangements which, viewed realistically, are no more than disguised or artificially contrived methods of paying money to employees. There is plenty of authority for applying a Ramsay approach (in the sense explained by Arden LJ in Astall to 'money in, money out' schemes of that kind: see, for example, NMB Holdings Ltd v Secretary of State for Social Security (2000) 73 TC 85 (payment of bonuses by the purchase and immediate sale of platinum sponge) and DTE Financial Services Ltd v Wilson (Inspector of Taxes) [2001] EWCA Civ 455, [2001] STC 777, 74 TC 14 (payment of bonuses through artificial trust arrangements which ended with the falling in of a contingent reversionary interest a few days after the scheme was set in motion). However, caution is needed because everything always depends on a careful scrutiny of the particular statutory provisions in

> issue, and it is impossible to generalise from instances where such an analysis is appropriate to a broad proposition that any tax avoidance scheme designed to turn an otherwise taxable bonus into something else, and to leave the employee at the end of the day with money in his pocket, will necessarily fail in its object. It also needs to be remembered that the mere existence of a tax avoidance motive is, in itself, irrelevant, although it may of course throw light on matters such as the commerciality of the arrangements made, or the likelihood of pre-planned events occurring."

153. At [163] the UT sounded a note of caution in interpreting the exception too broadly:

> "The need for caution in attributing too broad a meaning to the 'money' exception in s 420(5)(b) is reinforced by the fact that the definition of 'securities' in s 420(1) includes debentures and other instruments creating or acknowledging indebtedness, while s 424(1)(c) makes it clear that redeemable shares are also included. Thus securities which are convertible into money, and a wide range of securities which create, evidence or secure indebtedness, plainly fall within the scope of Pt 7. Moreover, since one of the legislative purposes of Pt 7 is, as Lord Walker said in Gray's Timber ([2010] STC 782 at [7], [2010] 1 WLR 497 at [7]), to eliminate opportunities for unacceptable tax avoidance, including in particular Chs 3A, 3B, 3C and 3D, one naturally expects the definition of 'securities' for the purposes of (among others) those chapters to be a wide one, and the exceptions to it to be relatively narrow."

154. The UT went on at [164] to consider the money exception in the light of the particular facts of the case:

> "Wherever the precise boundary of the 'money' exception should be drawn, it is in our opinion clear that the facts of the present case fall well outside it, and that the NVS are therefore within the definition of 'securities'. The real and enduring nature of the NVS, combined with the fact that nearly half of them were not redeemed for two years, makes it impossible to ignore them, or to regard them as a mere vehicle for the transfer of money. It is true that over half of the NVS were redeemed at the first opportunity, in March 2004, and it was plainly intended that this opportunity would be taken by those employees who would not in practice be liable to CGT on a disposal of the shares. But even in their case the shares were held for a period of almost two months, and because of the investment in UBS shares the amount received on redemption bore no necessary relation to the initial amount of the bonus. Furthermore, HMRC have never sought to argue that those employees who redeemed their shares at the first opportunity should be taxed differently from those who held their shares until 2006."

155. Both parties referred us to the above passage; the appellant for the views expressed on purpose and of a narrow construction of the "money" exception being

taken, the Respondents for the acknowledgement that there may be disguised and artificial schemes which fall within the exception. For the Respondents, Mr Brennan made it clear he was not however seeking a generalisation to the effect that a scheme which was disguised or artificial must fail.

156. Where does that leave us? It is not enough to say Part 7 is complicated, therefore artificial schemes must succeed. It is not enough to say that because a scheme is artificial it will inevitably fail. It means that a scheme will not fail because it is artificial but there are some artificial schemes in particular those of the "money in- money out" variety which do fail in their object.

157. Further, for the reasons explained by the UT the exception is to be construed narrowly in the sense that it is not enough that what a person receives may be treated as "money" because it can be converted to money in the hand of the recipient. There are items described in the provisions which plainly can be converted but are nevertheless intended to be captured within Part 7.

158. In assessing the scope of the "money" exception we think the following points are relevant too.

159. As observed by the appellant, the UT does not in its decision refer to the Court of Appeal case of *HMRC v PA Holdings Ltd* [2011] EWCA Civ. There, the Court of Appeal explains an approach of statutory construction whereby the question is asked whether a legislative act is intended to apply to one act or whether it can apply in relation to a series of transactions or a part of a composite transaction (see [54] to [56] Moses LJ). Although the UT's decision in UBS did not mention *PA Holdings* we note that their acknowledgement that there may be "money in-money out" schemes which fall within the exception is consistent with the "money" exception being able to apply to particular series of transactions or composite transactions.

160. We also note that part of the UT's analysis on "money" being construed narrowly is based on the presence of anti-avoidance provisions in Part 7 in particular Chapters 3A, 3B, 3C and 3D. i.e. if a wide interpretation encompassing anti-avoidance is adopted what role would there be for these chapters to play? We note that at least some of these chapters do not exclusively target schemes involving employment related securities where it is clear at the outset that the scheme has an avoidance purpose. It appears that Chapters 3A and 3B could also have a role in relation to employment-related securities that may not have been part of an avoidance scheme at the outset but where subsequently something else is done involving avoidance. We note for instance s446A ITEPA (the application provision for Chapter 3A which deals with securities with artificially depressed market value) applies the chapter where the market value of employment-related securities is "reduced by things done" otherwise than for genuine commercial purposes. This is broad enough to capture situations where employment-related securities were not part of a scheme when they were acquired but where their market value is subsequently reduced for an avoidance purpose. Section 446K provides a similar formulation in relation to Chapter 3B which deals with securities with artificially enhanced market value. In this regard at least, giving an anti-avoidance role to "money" does not mean Chapters 3A and 3B

are redundant. It also cannot be the case that "money" has no anti-avoidance role given that the UT says that "money in-money out" schemes may be caught.

161. We conclude the "money" exception is not to be interpreted in an overly broad way but equally it is not to be restricted to single acts but may apply to a series of transactions or part of a composite transaction. The exception can bring within its scope some, but not necessarily all, artificial and contrived tax avoidance schemes, which brings us to the question of how it applies to the facts of this particular scheme.

162. *UBS* gave the example of "money in – money out" schemes of the type considered in *NMB Holdings* and *DTE*.

163. The appellant argues the scheme in this case is not a "money in money out scheme". It was not inevitable money would be paid out. Mr Ferro had no need for the cash, he could use SG123 Ltd., a company which he controlled through the shares he was awarded, as a private investment vehicle.

164. The Respondents say this is an "old-fashioned" scheme which ignores the decisions in *NMB* and *DTE*. They say it is a disguised or artificial way of paying money to employees. The minutes, resolutions, alterations to share capital, to the company's articles were all with one purpose; money in, money out. It is precisely the sort of "disguised or artificially contrived method of paying money to employees" which was referred to in *UBS*.

165. Before continuing it is necessary to briefly outline *NMB* and *DTE*.

NMB holdings

166. In *NMB* the High Court considered whether the transfer of platinum sponge to directors as a bonus was 'earnings' and not 'payments in kind' for the purposes of the Social Security (Contributions) Regulations 1979, SI 1979/591. The court looked at the substance of the transaction. There were arrangements whereby the directors could immediately sell the platinum sponge for cash, to the bank which held the sponge. The bonuses were not 'payments in kind' exempt from the Social Security legislation (The court's approach and conclusion were endorsed by Lord Hoffmann in *MacNiven* [2001] STC 237 at [68], [2003] 1 AC 311 at [68]).

DTE

167. *DTE* concerned a composite transaction consisted of three stages, the purchase by an employer of a contingent reversionary interest in a trust fund in a sum equivalent to the intended bonus, the assignment of that interest to the employee and the payment of the cash sum by the trustee when the interest fell into possession. Viewed, as Jonathan Parker LJ put it, 'through *Ramsay* eyes', the company decided that its employee should have a £40,000 bonus and the employee got that bonus. ([2001] STC 777 at [41], 74 TC 14 at [41]).

PA Holdings Ltd.

168. We were also referred by the Respondents to *PA Holdings* for the proposition that it is important not to confuse the nature of the reward with the manner of its delivery.

169. The facts concerned a taxpayer company with a discretionary bonus scheme under which certain employees received dividends from preference shares in a third party company.

170. There, as highlighted by the Respondents, the award of money was distinguished from the mechanism for its delivery. The award of shares and the declaration of dividend were, in reality not separate steps but the process for delivery of the bonuses. The court held a court is not to be restricted to the legal form of the source of the payment but must focus on the character of the receipt in the hand of the recipient. A *Ramsay* approach is not even necessary. The scheme was a process for delivering a cash bonus not an award of shares.

171. The appellant refers us to the finding in *UBS* that the FTT had no basis for ejecting the scheme from Part 7. It says the same is true here. Here there is no machinery to turn what was in the company SG123 Ltd. into cash. It says *NMB* can be distinguished and so can *DTE* and *PA Holdings* for the following reasons.

172. In *NMB* it was clear there was never any intention of physically transferring the platinum sponge to a director or of doing anything with it other than having it purchased by the company, transferred to the director, and then sold back. It remained in the custody of a bank in Hong Kong and there was no ready market so practically it had to go back to the original vendor. Platinum sponge was alien to the directors' knowledge or to any use they may have for it. In the current appeal there was no trading mechanism. Shares in an investment company were transferred to Mr Ferro and there was a variety of ways Mr Ferro could exploit those shares. An investment company is clearly a vehicle with which businessmen are familiar. Whereas in *NMB* the purchase and sale of platinum sponges were simply machinery, there was no such machinery here.

173. *DTE* can be distinguished too. It was a simple structure into which cash went in and then went out ending up in the hands of the employees

174. The appellant says *PA Holdings* is also distinguishable. It was not agreed that what was paid was income and the bonus recipients only had a minority interest in the third party company which meant it was not attractive as an investment vehicle in the way that the shares in this appeal were. Mr Ferro had the controlling interest in the company. There were many other things he could have done with the company; he could have continued to operate the company perhaps buying investments in it and running it for his long term benefit. The appellant says *PA Holdings* is a decision about source of income: Is it Schedule F or is it income tax? It is not a blanket authority to say rewards from corporate body to executive are subject to PAYE. If it was there would be no point to Part 7.

175. The appellant's riposte to the Respondents' remark that this case had an "old fashioned" feel to it was to note that in *UBS*,a case where UBS succeeded also concerned the tax year 2003/4.

Tribunal's views

Similar or different to NMB / DTE?

176. We are not persuaded that *NMB* is irrelevant because there the bonuses were in platinum sponge, an unfamiliar subject matter whereas here what was paid were SG123 Ltd. shares with which Mr Ferro could have done a variety of things apart from turning them to cash.

177. The relevance of the unfamiliarity of platinum sponge in *NMB* was in the context of the Secretary of State's consideration (at [6(22)] and endorsed as "impeccable reasoning" by Langley J) of whether, once started, the scheme would proceed through the various steps to the end. The unusual nature of platinum sponge from a private individual's point of view meant that practically the only thing a private individual can do is to sell it. However the fact that the assets here were shares in SG123 Ltd. and that such shares were of a less unusual nature does not prevent the conclusion being reached that the scheme would proceed to its end if that is what the particular circumstances of this case point towards.

178. In this case it seems clear to us that the receipt of shares was not the end of the scheme but one of the steps in the scheme. We note for instance Mr Ferro's adviser's indication prior to 1 June 2004 describing his client as "half-way through under the 0% scheme".

179. The approach in *NMB* (consistent with a realistic appraisal) is to take account of what practically an individual could do with what they received in order to throw light on whether the scheme would be followed through. The fact that there is a theoretical possibility that others might use SG123 Ltd. for other purposes does not get round the fact that realistically that was not what Mr Ferro was going to do with them.

Lack of "machinery" to turn shares to cash?

180. In relation to the appellant's argument that a lack of machinery to turn shares to cash means (in contrast to the "machinery" for selling the platinum sponge) that their scheme is not a "money in – money out" scheme we consider this fails to take account of the different nature of the asset involved. The appellant accepted Mr Ferro was in control of SG123Ltd. The company had £300,000 in its bank account. It is not surprising that there were not the same kinds of arrangements put in place to turn the shares to cash as compared with the arrangements for turning platinum sponge to cash. In any case, as mentioned above, the scheme was not complete at the stage of the award of shares. More steps were to follow. The detail of these was to change because of changes in legislation, so in the event, the step which was taken and part of

the machinery of the scheme was to enter into an agreement under which the appellant guaranteed to pay a purchase price for the shares to Mr Ferro.

181. In relation to *DTE* the appellant says the arrangement there was some distance away from the facts here. *DTE*, say the appellant was a simple structure in which case went out and cash ended up in the hands of the employees.

182. But, to call the structure simple, and contrast this with the facts here is not comparing like with like in the sense that the cash in cash out depiction arises after looking at the matter through *Ramsay* eyes. The scheme comprised a number of steps: the creation of an off shore discretionary settlement of a sum of cash (borrowed by the settlor) under which the settlor becomes entitled (by virtue of an appointment made by the trustee) to a sum equal to the intended bonus plus a sum in respect of costs. The contingent reversionary interest amounts to a right to a specified sum of cash on a specified date. The employer takes an assignment of the contingent reversionary interest for consideration and then assigns it to the employee. The interest is non-assignable and on the specified date the employee receives a cash payment equal to the amount of his intended bonus. The scheme the appellant used also comprised a number of steps and we disagree that *DTE* is distinguishable on the ground the appellant suggests.

Distinguishable from PA Holdings?

183. As considered above we reject, on a realistic appraisal of the facts that there was any role for SG123 Ltd for holding investments or properties. The contrast the appellant highlights between Mr Ferro's control of SG123 Ltd and the bonus recipients' minority interests in *PA Holdings* is not a basis on which to disregard the approach and observations set out in *PA Holdings*.

184. Having dismissed the appellant's reasons for why *DTE* and *NMB* and *PA Holdings* are not relevant we do take into account that each of those cases concerned different legislation and different schemes. Their relevance lies in their support for an approach of looking at a series of transactions as a whole and in considering whether, given the purpose of the relevant legislative provisions at issue, the transaction was with the legislation's scope.

185. The Respondents' arguments caution against getting confused between what is delivered and the means by which it is delivered. There are references in the case law variously to steps in a scheme being "vehicles" (*UBS)* or "machinery" or a "process for delivery" (*PA Holdings Ltd*). While all of those concepts helpfully describe the character of steps which are found to be intermediate steps in transactions we are conscious that if it were to simply be asserted in this case that the award of shares was a vehicle, or a process for delivery, or machinery, this would beg the question of what the outcome to which the process, vehicle, or machinery was directed towards. As shown by the decision of the UT in *UBS* it may also be the case that something which is ostensibly a "vehicle" in a contrived avoidance scheme turns out not to be upon further examination.

186. In *UBS* the facts also concerned an artificial scheme and there was specific consideration of the "money" / "securities" dividing line. We need to return there to look at the reasons why the scheme was successful in its object. In that case there was a vehicle / machinery but the UT found it could not be ignored.

"Vehicle" which can't be ignored? Real and Enduring nature of shares

187. The Respondents say *UBS* is factually distinguishable because there the Non-Voting Shares "NVS" which were awarded were of a "real and enduring nature". It is to be noted that nearly half of them were not redeemed for two years making it "impossible to ignore them or regard them as a mere vehicle for transfer of money." In this case the 998 'B' Shares awarded to the appellant were not comparable to the NVS. They were held for only 6 months and that was largely because of the press release of May 2004 announcing the legislative changes to Part 7 ITEPA. There was, also a particular fiscal reason for why half the shares were not redeemed.

188. The appellant points to the fact that in *UBS* the other half of the shares were redeemed within a couple of months. The 998 'B' Shares were ordinary real shares which could vote dividends and which had restrictions. They continued to exist until the company was dissolved. They were real from 29 April 2004 until 15 May 2007. Shares do not stop being real because they are transferred. The shares were in a company which gave Mr Ferro virtually all control and the company had £300,000 in its bank account. It could be used for any commercial purpose.

Tribunal's views

189. It is worth recalling [164] of the UT's decision (extracted above at [154]). It shows there were several strands to the UT's view as to why the facts of the UBS case fell well outside of the money exception one of which was the "real and enduring nature of the NVS". It was not this fact alone though but that it was "combined with the fact that nearly half of them were not redeemed for two years". Further the point is made that even where shares were held for only 2 months the amount received on redemption bore no necessary relation to the initial amount of the bonus.

190. The 998 'B' Shares were real and enduring in the sense they were real shares – they carried voting rights, rights to dividends and distribution of surplus assets on a winding up. They did not vanish. They existed until SG123 was dissolved. The NVS in *UBS* entitled the holders to receive dividends and surplus assets on a winding-up (see [46] of UT decision).

191. But, the UT also thought it relevant to mention the issue of when the shares were redeemed as a separate point from their "real and enduring" nature. In the context of a question before them as to whether the arrangements fell into the "money" exception, we think the separate reference to redemption means they were looking at the circumstances under which money was received. Redemption in that case happened to be the means by which the NVS could be turned to money and the length of time over which that happened was a relevant factor to consider. In a similar vein we think the length of time the shares were held for by the recipient before being

turned to money (as opposed to the length of time the shares were in existence) is relevant.

192. It was also relevant, in our view, in the context of determining whether there was a bonus of money or of shares and the role of the shares in the scheme, to consider the fact that the amount coming out upon redemption, whether 2 months later or years later, would depend on the performance of the UBS shares that the special purpose vehicle (ESIP Ltd.) was bound to invest in. There were hedging arrangements protecting against loss in value but these expired after the restriction term so there was a period at which the holders of the shares bore real risk. It was not part of the scheme that there was no risk. In this case holding the 'B' shares in SG123 Ltd. gave control of a company which held a bank deposit.

193. For these reasons in assessing whether the facts of this case mean the 998 'B' shares fall into the "money" exception, the fact the UT in *UBS* found the NVS fell well outside it does not, we think, mean that the receipt of 'B' shares in this case fall outside it too. The circumstances surrounding the 998 'B' shares and their nature mean that they cannot be viewed in the same light as the NVS were in *UBS*.

194. The UT reached a similar conclusion on the "money" exception issue in relation to the Deutsche Bank appeal as it did in the UBS appeal which was heard at the same time. In Deutsche Bank, the vehicle corresponding to ESIP Ltd was a company incorporated in the Cayman Islands called Dark Blue Investment Ltd (DBI). The relevant shares were C1 redeemable shares. It appears from [61] of the FTT's decision that the C1 shares were real shares, that it was possible for an employee to hold them for over two years and if they did so they received dividends from the sums invested in DBI and invested by it. That suggests DBI was not simply sitting on a sum of cash in its bank account.

195. It was not a foregone conclusion how much money the employee would get for the shares. Returning to the purpose underlying the legislation it could be seen there was some point to "waiting and seeing" what value emerged from holding the shares. In this case Mr Ferro received shares in a company which he controlled and which held a significant cash balance. There was no real risk or uncertainty beyond that attached to bank deposits to what Mr Ferro would get.

Relevance to change in law on 7 May 2004

196. The appellant also says there was no pre-ordainment as the law changed unexpectedly further to the 7 May 2004 announcement. The Respondents say this is a change of route but the destination remained the same. We were referred by the appellant to the FTT decision *Sloane Robinson* [2012] UKFTT 451 (TC) where the point was made that there was no authority on the point, (ie when changes to the scheme arose out of changes in law) and the FTT would need to wait for a UT decision on the matter. No authorities on the point were cited to us but the Respondents suggest that should the Tribunal find it necessary to deal with the case relying on *Ramsay* it would not be prevented and indeed ought to set out its views on the matter. Both parties agreed that as a decision of the FTT, *Sloane Robinson* could

only be persuasive at best, and that it was therefore open to the Tribunal to reach its view on the change of law point even though the Tribunal in *Sloane Robinson* did not do so.

197. We have considered the change in law argument from the point of view of whether when construing the "money" exception we can look at the steps in the scheme which were taken before the change in law on 7 May 2004, and after it as a whole. We think we can for two reasons.

198. First, as at the point of time the SG123 Ltd. shares were awarded there was a scheme whose object was to realise value in cash. The scheme did not end with the award of shares, that much is clear from Mr Modi's prompts as to what further steps needed to be taken and the need to go to counsel. If the scheme had ended with the award of shares there would have been no need for this. We do not find that there was any realistic possibility that Mr Ferro would do anything other than turn the shares to cash. SG123 Ltd. served no purpose other than as performing a part in the scheme. Mr Ferro had no reason to want to hold onto shares in a special purpose vehicle apart from as a means of extracting money from his company.

199. Second, the appellant cannot reasonably have assumed that the law would necessarily stay the same. Against that backdrop, it was we think predictable, given what the appellant was setting out to do, namely extract cash from its account and deliver this to Mr Ferro, that further steps would be carried out in order to try and achieve the objective taking account of any change in law even if it was not known until later what the exact formulation of those steps would be.

200. There was an overarching objective and it was foreseeable advice would be sought as to the further steps to be taken. At the outset there was a scheme to extract the bonus which envisaged certain steps. Some of those steps were performed, the remainder were re-engineered but the objective remained the same. The steps taken after the change took account of the planning before. It would not be realistic, given the overall objective and the linkage between the steps, to disregard the steps taken post the change in law and to regard the change in law as giving rise to two separate sets of transactions which should be examined separately. There was one set of transactions linked by a common objective.

201. We agree with the Respondents. The route may have changed but the destination was the same.

Applying the facts realistically appraised in relation to this scheme to the legislation

202. Bringing the above discussion together we make the following conclusions in relation to how the legislation purposively construed is to be applied to the realistically appraised facts of this case.

203. The appellant argues this is not a "money in money out scheme". It was not inevitable money would be paid out. Mr Ferro had no need for the cash; he could use it as a private investment vehicle.

204. Following from the findings above we disagree Stoneygate 123 Ltd. was to be held for investment purposes. There was no evidence to suggest this was the case. It is a separate point that it was capable of being held as such but that is not a realistic appraisal of the facts. Notes of meetings Mr Ferro took part in prior to implementation of the scheme (25 September 2003) reveal him wanting to extract bonus so he could reinvest. Advice in relation to the scheme show us what its objects were. The note of 4 March 2004 makes reference to "invest the money". Mr Ferro's adviser was keen to follow up on getting the money.

205. It was clear at the outset of the scheme when £300,000 was transferred by the appellant to SG123 Ltd. that the scheme was not going to end with Mr Ferro holding on to shares in SG123 Ltd.

206. We also find it implausible that anyone else would enter into this kind of arrangement to hold investments through such a company. In *NMB Holdings* it was possible for the directors to hold onto platinum sponge but ultimately it was not realistic to find they would do so. Similarly it was possible Mr Ferro would hold onto the shares but it was not realistic.

207. The facts of this transaction, which disclose series of meetings, resolutions, agreements and transfers, whereby Mr Ferro dutifully followed detailed instructions given to him, and signed what he was asked to sign, all performed with the ultimate objective of avoiding tax, can without any hesitation be described as components in a contrived and artificial scheme to avoid tax.

208. It is accepted by the Respondents that a motive to avoid tax, which there clearly was here, is not fatal to a scheme being held to be effective but as pointed out by the UT in *UBS* at [162] quoted above at [152] "it may of course throw light on matters such as the commerciality of the arrangements made, or the likelihood of pre-planned events occurring".

209. In our view, the light the tax avoidance motive casts on any suggestion that there was a commercial reason for holding onto the shares is an unfavourable one. It also makes any suggestion that there was not an expectation that the steps that were to be taken to turn the shares to money were not pre-planned less tenable. The lack of explicit machinery to turn the shares to money as compared with the platinum sponge in *NMB* is not surprising given the different subject matter involved.

210. We have considered whether, as in *UBS*, the shares, were of a character such that the step of awarding them could not be ignored. We have found the shares and the circumstances of their award are materially different and conclude the shares in SG123 can be regarded as a vehicle for payment of cash.

211. SG123 Ltd. and SG108 had no role other than to play their part in the scheme to avoid tax. The steps which followed the appellant's decision that it would pay Mr Ferro a £300,000 bonus, such as the award of shares in a special purpose vehicle, the transfer of shares, the giving of the guarantee disclose no commercial purpose.

212. We should also mention we have not overlooked the appellant's argument to the effect that HMRC want to "have their cake and eat it" by saying something is earnings if they cannot get a charge to stick under Part 7 ITEPA. What would happen, they say, if it turned out the shares continued to be held?

213. We are not persuaded this argument gets the appellant anywhere. As at the time of the award of shares our finding is that realistically what Mr Ferro was getting was money. On that basis Part 7 is not accessed. The effectiveness or otherwise of the scheme negotiating its way through Part 7 without a tax charge is not relevant.

214. Our conclusion is the transactions which took place when realistically appraised amount to an artificial contrived scheme, whose essence was to pay money. The transaction when viewed realistically is one which it was the intention of Parliament to exclude from the regime in Part 7 by operation of the "money" exception.

The amount going into the scheme and coming out of it

215. In *UBS* the Upper Tribunal commented at [165] that HMRC's Regulation 80 determination notice was determined in the sum of the gross amount paid by UBS into the ESIP. They state:

> " …in our view there is no intellectually coherent way, in this case, of equating the payment in by the employer with the ultimate payment out received by the employee and the facts are resistant to any form of high-level *Ramsay* analysis or reconstruction."

216. For the reasons discussed above at [189] to [195] as to the distinctions between the "real and enduring nature" of the ESIP shares in contrast to the shares in SG123 Ltd. we do not think the same difficulty arises in this case. As stated in reasoning of the Secretary of State in *NMB Holdings* at [6(22)] which was endorsed by Langley J in his consideration of the application of *Ramsay* it is the series of transactions which has to be pre-ordained rather than the amount of cash.

217. The fact that what was received was different from what was extracted from the company does not therefore mean it is not possible to take an approach whereby a series of steps which amount to a composite transaction are found to fall within a statutory provision which applies to such transactions.

Conclusion on determinations

218. The scheme amounts to a bonus of money rather than shares. Under Rule 3(c) in s18 ITEPA the timing of the payment was when the amount was determined. In accordance with our finding this was 30 April 2004 which was the date when the appellant awarded Mr Ferro shares and in doing so committed to operating the share scheme in favour of Mr Ferro. The Regulation 80 determinations under appeal are upheld.

National Insurance Contributions position

219. Both parties were in agreement that the analysis for National Insurance Contributions would follow the income tax analysis.

220. We agree. On the basis that Part 7 ITEPA was irrelevant for income tax then Regulation 25 and paragraph 1 Part IX of Schedule 3 to the Social Security (Contributions) Regulations 2001 ("the NICs Regulations") which provide for an earnings disregard for payments by way of "securities" and "restricted securities" is irrelevant too. The "money" exception in s420 ITEPA was equally relevant to NICs in that the definitions of "securities" and "restricted securities" in Regulation 1(2) of the NICs Regulations reflected the corresponding definitions of those terms in ITEPA 2003. There was a bonus of money rather than securities. The money counted as earnings for NIC purposes. The Respondents relied on *HM Revenue and Customs v Forde and McHugh* [2012] EWCA Civ 692 for the proposition that the money was paid to or for the benefit of the employee on the date on which it was paid into the scheme even if there was an obstacle bar to immediate enjoyment. The appellant did not make any argument against this.

221. The s8 decisions under appeal are confirmed.

Conclusion

222. The scheme amounted to a bonus in money rather than shares. The Regulation 80 determinations and the s8 decisions under appeal are upheld. The appellant's appeal is dismissed.

223. 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.

SWAMI RAGHAVAN
TRIBUNAL JUDGE

RELEASE DATE: 29 August 2013