[2014] UKFTT 1023 (TC)

TC04119

Appeal number: TC/2012/11057

INCOME TAX – taxation of overseas dividends received by resident beneficiary of non-resident trust - distributions from non-UK resident companies - interpretation of legislation rewritten as part of the Tax Law Rewrite Project – s399 Income Tax (Trading and Other Income) Act 2005 – appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

PHILIP SHIRLEY **Appellant**

- and -

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

TRIBUNAL: JUDGE NICHOLAS ALEKSANDER
MR MICHAEL SHARP FCA

Sitting in public at 45 Bedford Square, London WC1 on 1 and 2 May 2014

Michael Firth, counsel, for the Appellant

David Yates, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. This is an appeal against closure notices issued by HMRC. The amount of tax at stake is £413.23, however the issues to be determined by the Tribunal could affect a number of other taxpayers who are in a similar position to the appellant, Mr Shirley.

2. The following appeals are before the Tribunal:

(1) 2005/06 – closure notice dated 23 November 2012 under paragraph 7, Schedule 1A, Taxes Management Act 1970 ("TMA") in respect of a claim by Mr Shirley for tax credit of £106

(2) 2007/08 – closure notice dated 23 November 2012 under section 28A TMA in respect of a claim in Mr Shirley's self-assessment tax return for tax credit of £209; and

(3) 2008/09 – closure notice dated 23 November 2012 under section 28A TMA in respect of a claim in Mr Shirley's self-assessment tax return for tax credit of £1.80.

3. Income for the year 2006/7 is not before this Tribunal, as HMRC were out of time to open an enquiry.

4. We had before us a witness statement from Mr Shirley, but Mr Shirley did not give oral evidence. We also had a bundle of documents, including a statement of agreed facts. Mr Firth represented Mr Shirley and Mr Yates represented HMRC.

5. At the conclusion of the hearing we gave directions for further written submissions to be made by the parties.

6. References in this decision to section numbers are to sections of the Income Tax (Trading and Other Income) Act 2005 ("ITTOIA"), unless otherwise specified.

The facts

7. The facts are not in dispute and we find them to be as follows:

8. Mr Shirley was at all material times tax resident in the UK.

9. Mr Shirley is the life tenant and interest in possession beneficiary of two settlements ("the Trusts"). The Philip Shirley Trust was established by Mr Shirley's father in the early 1960s at a time when Mr Shirley's father was resident in the Republic of Ireland. The Philip Shirley Trust is governed by Irish law. The PES Manx Trust was established by an unrelated party with a nominal sum, but was later funded by an appointment from a settlement set up by Mr Shirley's mother in the early 1960s, at a time

when she was resident in Ireland. The PES Manx Trust is governed by Manx law. The trustees of the Trusts were resident and the settlements were managed in Ireland, until Mr Shirley's parents moved to the Isle of Man in 1977. At all times the trustees of the Trusts have been resident outside the UK, and the Trusts have been managed outside the UK.

10. Mr Shirley is the life tenant of the Trusts, and the dividends and other income of the Trusts have always been paid to him as life tenant.

11. The appeal is in respect of dividends arising on shares owned by the Trusts in companies resident in the following countries:

(a) Bermuda

(b) Canada

(c) France

(d) Germany

(e) Hong Kong

(f) Ireland

(g) Switzerland; and

(h) the USA

12. Historically, the shares were registered in the name of a nominee company in the Isle of Man and the dividends were not remitted to the UK. However, this was cumbersome and expensive, and the trustees decided to transfer the shares to a nominee company in the UK during the course of 2005/06. 2005/06 was a transitional year, and not all of the shares were transferred from the Manx nominee to the UK nominee in this year.

13. The dividend income that is the subject of this appeal has been distributed by the Trusts to Mr Shirley as the life tenant of the Trusts.

14. As a UK resident, Mr Shirley is chargeable to income tax on the dividends to the extent the dividends are remitted to the UK.

15. The issue before the Tribunal is whether Mr Shirley is to be treated as if he had paid tax on the distributions pursuant to s399.

16. This question arises in respect of the years

(a) 2005/6

(b) 2007/8; and

(c) 2008/9

The legislation

17. For the tax years 2005/6 and 2007/8 the relevant legislation read as follows:

Chapter 3

Dividends Etc. From UK Resident Companies Etc.

Introduction

382 **Contents of Chapter**

(1) This Chapter—

(a) imposes a charge to income tax on dividends and other distributions of UK resident companies (see section 383),

(b) treats dividends as paid in some circumstances (see sections 386 to 391), and

(c) makes special provision where the charge is in respect of shares awarded under an approved share incentive plan (see sections 392 to 396).

(2) This Chapter also makes provision about tax credits, tax being treated as paid and reliefs available in respect of certain distributions which applies whether or not the distributions are otherwise dealt with under this Chapter (see sections 397 to 401).

(3) For exemptions from the charge under this Chapter, see in particular—

Chapter 3 of Part 6 (income from individual investment plans),

Chapter 5 of that Part (venture capital trust dividends),

section 770 (amounts applied by SIP trustees acquiring dividend shares or retained for reinvestment), and

section 498 of ITEPA 2003 (no charge on shares ceasing to be subject to SIP in certain circumstances).

(4) In this Chapter "dividends" does not include income treated as arising under section 410 (stock dividends).

[…]

Tax credits and payment and deduction of tax

397 **Tax credits for qualifying distributions: UK residents and eligible non-UK residents**

(1) A UK resident or eligible non-UK resident receiving a qualifying distribution made by a UK resident company is entitled to a tax credit equal to one-ninth of the amount or value of the distribution (but see subsections (3) and (6)).

(2) Such a person may claim to deduct the tax credit from—

(a) the income tax charged on the person's total income for the tax year in which the distribution is made, or

(b) the income tax charged on the person's income under section 3 of ICTA (certain income charged at basic rate) for that year.

(3) Subsection (1) only applies so far as the distribution is brought into charge to tax, and accordingly if the person's total income is reduced by any deductions which fall to be made from the distribution, the tax credit for the distribution is reduced in the same proportion as the distribution.

(4) For the purposes of this section “eligible non-UK resident”, in relation to a qualifying distribution, means an individual who at any time in the tax year in which it is received is a non-UK resident within section 278(2) of ICTA (Commonwealth citizens, EEA nationals etc.).

(5) If a distribution is, or is treated under any provision of the Tax Acts as, the income of a person (“P”) other than the recipient (“R”), P (not R) is treated as receiving it for the purposes of this section (and so P (not R) is entitled to a tax credit if P falls within subsection (1)).

(6) This section is subject to the following provisions—

section 231AA of ICTA (no tax credit for borrower under stock lending arrangement or interim holder under repurchase agreement),

section 231AB of ICTA (no tax credit for original owner under repurchase agreement in respect of certain manufactured dividends),

section 469(2A) of ICTA (no tax credit for trustees of a unit trust scheme that is neither an authorised unit trust nor an umbrella scheme), and

section 171(2B) of FA 1993 (no tax credit for distributions in respect of assets in Lloyd's member's premium trust fund).

398 **Increase in amount or value of dividends where tax credit available**

(1) If a person is entitled to a tax credit in respect of a dividend or other distribution, the amount or value of the dividend or other distribution is treated as increased by the amount of the tax credit for all income tax purposes (except section 397(1)).

(2) Subsection (1) does not apply if the distribution is dealt with under Chapter 2 of Part 2 unless the trade consists of the underwriting business of a member of Lloyd's.

399 **Qualifying distributions received by persons not entitled to tax credits**

(1) This section applies if a person is not entitled to a tax credit for a qualifying distribution included in the person's income for a tax year.

(2) The person is treated as having paid income tax at the dividend ordinary rate on the amount or value of the distribution (but see subsection (7)).

(3) For the purposes of subsection (2), if the person is non-UK resident the amount or value of the distribution is treated as the grossed up amount, unless the person is a company which is beneficially entitled to the income.

(4) If the person is non-UK resident and the distribution is income to which section 686 of ICTA applies (accumulation and discretionary trusts: special rates of tax), for the purposes of that section the amount or value of the distribution is treated as the grossed up amount.

(5) In this section “the grossed up amount” means the actual amount or value of the distribution, grossed up by reference to the dividend ordinary rate for the tax year.

(6) The income tax treated as paid under subsection (2) is not repayable.

(7) Subsection (2) is subject to the following provisions—

section 231AA(1A) of ICTA (which disapplies subsection (2) for borrower under stock lending arrangement or interim holder under repurchase agreement),

section 231AB(1A) of ICTA (which disapplies subsection (2) for original owner under a repurchase agreement in respect of certain manufactured dividends), and

section 469(2B) of ICTA (which disapplies subsection (2) for trustees of a unit trust scheme that is neither an authorised unit trust nor an umbrella scheme).

400 **Non-qualifying distributions**

(1) This section applies if a person's income in a tax year includes a non-qualifying distribution.

(2) The person is treated as having paid income tax at the dividend ordinary rate on the amount or value of the distribution.

(3) The income tax treated as paid under subsection (2) is not repayable.

(4) If the distribution is income to which section 686 of ICTA applies (accumulation and discretionary trusts: special rates of tax), the trustees' liability for income tax at the dividend trust rate on the amount or value of the whole or any part of the distribution is reduced.

(5) The amount of the reduction is equal to income tax at the dividend ordinary rate on so much of the distribution as is assessed at the dividend trust rate.

(6) In this section and section 401 "non-qualifying distribution" means a distribution which is not a qualifying distribution.

401 **Relief: qualifying distribution after linked non-qualifying distribution**

(1) Where a person pays an amount in respect of extra liability for a non-qualifying distribution, the person's extra liability for a subsequent qualifying distribution is reduced by that amount if conditions A and B are met.

(2) Condition A is that the non-qualifying distribution consists of the issue of share capital or security.

(3) Condition B is that the qualifying distribution consists of a repayment of the share capital or the principal of the security.

(4) A person's extra liability for a distribution charged to tax for the tax year 1999– 2000 or a later tax year is the amount by which the person's liability to income tax on the distribution exceeds the amount it would be if it were charged only at the dividend ordinary rate.

(5) A person's extra liability for a distribution charged to tax for a tax year after the tax year 1992–93 and before the tax year 1999–2000 is the amount by which the person's liability to income tax on the distribution exceeds the amount it would be if it were charged only at the lower rate.

(6) A person's extra liability for a distribution charged to tax for a tax year before the tax year 1993–94 is the amount by which the person's liability to income tax on the distribution exceeds the amount it would be if it were charged only at the basic rate.

(7) In this section "security" has the meaning given in section 254(1) of ICTA.

18. But sections 397 to 401 were amended by the Income Tax Act 2007 and the Finance Act 2008, so that for the tax year 2008/9 they read as follows:

397 **Tax credits for qualifying distributions of UK resident companies: UK residents and eligible non-UK residents**

(1) A UK resident or eligible non-UK resident receiving a qualifying distribution made by a UK resident company is entitled to a tax credit equal to one-ninth of the amount or value of the distribution (but see subsections (3) and (6)).

(2) Such a person may claim to deduct the tax credit from—

(a) the income tax charged on the person's total income for the tax year in which the distribution is made,

(3) Subsection (1) only applies so far as the distribution is brought into charge to tax, and accordingly if the person's total income is reduced by any deductions which fall to be made from the distribution, the tax credit for the distribution is reduced in the same proportion as the distribution.

(4) For the purposes of this section “eligible non-UK resident”, in relation to a qualifying distribution, means an individual who at any time in the tax year in which it is received is a non-UK resident within section 278(2) of ICTA or section 56(3) of ITA 2007(Commonwealth citizens, EEA nationals etc.).

(5) If a distribution is, or is treated under any provision of the Tax Acts as, the income of a person (“P”) other than the recipient (“R”), P (not R) is treated as receiving it for the purposes of this section (and so P (not R) is entitled to a tax credit if P falls within subsection (1)).

(6) This section is subject to the following provisions—

section 504(4) of ITA 2007 (disapplication of certain provisions for income of unauthorised unit trusts),

section 592 of ITA 2007 (no tax credits for borrower under stock lending arrangement),

section 593 of ITA 2007 (no tax credits for interim holder under repo),

section 594 of ITA 2007 (no tax credits for original owner under repo), and

section 171(2B) of FA 1993 (no tax credit for distributions in respect of assets in Lloyd's member's premium trust fund).

397A **Tax credits for distributions of non-UK resident companies: UK residents and eligible non-UK residents**

(1) This section applies where a UK resident or eligible non-UK resident receives a relevant distribution made by a non-UK resident company, provided that—

(a) the company is not an offshore fund (within the meaning of section 756A of ICTA), and

(b) the person is a minority shareholder in the company at the time the distribution is received.

(2) The person is entitled to a tax credit equal to one-ninth of the amount or value of the grossed up distribution (but see subsections (3) and (6)).

(3) Subsection (2) only applies so far as the distribution is brought into charge to tax, and accordingly if the person's total income is reduced by

any deductions which fall to be made from the distribution, the tax credit for the distribution is reduced in the same proportion as the distribution.

(4) The person may claim to deduct the tax credit from the income tax charged on the person's total income for the tax year in which the distribution (or the part of the distribution to which the tax credit relates) is brought into charge to tax.

(5) If a distribution is, or is treated under any provision of the Tax Acts as, the income of a person ("P") other than the recipient ("R"), P (not R) is treated as receiving it for the purposes of this section (and so P (not R) is entitled to a tax credit if P falls within subsection (1)).

(6) This section is subject to the following provisions—

section 171(2B) of FA 1993 (no tax credit for distributions in respect of assets in Lloyd's member's premium trust fund),

section 504(4) of ITA 2007 (disapplication of certain provisions for income of unauthorised unit trusts),

section 592 of ITA 2007 (no tax credits for borrower under stock lending arrangement),

section 593 of ITA 2007 (no tax credits for interim holder under repo), and

section 594 of ITA 2007 (no tax credits for original owner under repo).

(7) In this section—

"eligible non-UK resident", in relation to a distribution, means an individual who, at any time in the tax year in which the distribution (or the part of the distribution to which the tax credit relates) is brought into charge to tax, is a non-UK resident who meets the condition in section 56(3) of ITA 2007 (residence etc of claimants),

"grossed up distribution" means the distribution increased by the amount of any tax chargeable in respect of the distribution directly or by deduction under the laws of the territory in which the company is resident, including special withholding tax,

"minority shareholder", in relation to a company, has the meaning given in section 397C,

"relevant distribution", in relation to a person, means—

(a) a qualifying distribution arising in a relevant tax year,

(b) a cash dividend paid over to the person under paragraph 68(4) of Schedule 2 of ITEPA 2003 (cash dividend paid over if not reinvested etc) in a relevant tax year, and

(c) a dividend treated under section 407 as paid to the person in a relevant tax year, “relevant tax year” means the tax year 2008–09 or a subsequent tax year, and

“special withholding tax” has the meaning given in section 107(3) of FA 2004.

(8) Section 397B makes provision about the application of this section in the case of overseas dividends arising from manufactured overseas dividends (within the meaning of Chapter 2 of Part 11 of ITA 2007).

397B **Tax credits under section 397A: manufactured overseas dividends**

(1) This section applies where, under section 581 of ITA 2007, a person is treated as receiving an overseas dividend by virtue of having received a manufactured overseas dividend which is representative of an overseas dividend.

(2) For the purposes of section 397A, the person is treated as receiving a relevant distribution made by a non-UK resident company that is not an offshore fund if, and only if, the manufactured overseas dividend is representative of such a distribution.

(3) References in section 397A to the grossed up distribution have effect as if they were references to the gross amount of the overseas dividend of which the manufactured overseas dividend is representative, disregarding the amount of any overseas tax credit.

(4) In this section—

“gross amount”, in relation to a manufactured overseas dividend, has the same meaning as in Chapter 2 of Part 11 of ITA 2007 (manufactured payments) (see section 589 of that Act),

“manufactured overseas dividend” and “overseas tax credit” have the same meaning as in Chapter 2 of that Part (see sections 581 and 591 of that Act), and

“overseas dividend” has the same meaning as in that Part (see section 567 of that Act).

397C **Meaning of “minority shareholder”**

(1) In section 397A “minority shareholder”, in relation to a non-UK resident company, means a person whose shareholding in the company is less than 10% of the company's issued share capital.

(2) Subsections (3) to (6) make provision about the circumstances in which shares form part of a person's shareholding in a company for the purposes of this section.

(3) Shares form part of a person's shareholding in a company to the extent that the person is beneficially entitled to the shares or to a distribution arising in respect of the shares (or both).

(4) Shares form part of a person's shareholding in the company where—

(a) a person is a settlor in relation to a settlement, and

(b) income arising from shares comprised in the settlement is treated for income tax purposes as the income of that person and of that person alone.

(5) Shares form part of the shareholding in a company of a person ("P") if—

(a) they form part of the shareholding in the company of a person connected with P,

(b) P transferred the shares to the connected person or arranged for the connected person to acquire the shares, and

(c) the purpose of the transfer or arrangement was wholly or mainly to enable P to avoid tax.

(6) Shares form part of a person's shareholding in a company if that person has transferred the shares to another person under a repo or stock lending arrangement.

(7) In this section—

"repo" has the same meaning as in Part 11 of ITA 2007 (see section 569 of that Act),

"settlement" and "settlor" have the same meaning as in Chapter 5 of Part 5 of this Act, and

"stock lending arrangement" has the same meaning as in Part 11 of ITA 2007 (see section 568 of that Act).

398 **Increase in amount or value of dividends where tax credit available**

(1) If a person is entitled to a tax credit under section 397 or 397A in respect of a dividend or other distribution, the amount or value of the dividend or other distribution is treated as increased by the amount of the tax credit for all income tax purposes (except sections 397(1) and 397A(2)).

(2) Subsection (1) does not apply if the distribution is dealt with under Chapter 2 of Part 2 unless the trade consists of the underwriting business of a member of Lloyd's.

399 **Qualifying distributions received by persons not entitled to tax credits**

(1) This section applies if a person is not entitled to a tax credit under section 397 or 397A for a qualifying distribution included in the person's income for a tax year.

(2) The person is treated as having paid income tax at the dividend ordinary rate on the amount or value of the distribution (but see subsection (7)).

(3) For the purposes of subsection (2), if the person is non-UK resident the amount or value of the distribution is treated as the grossed up amount, unless the person is a company which is beneficially entitled to the income.

(4) If the person is non-UK resident, the amount or value of the distribution is treated for the purposes of Chapters 3, 4 and 6 of Part 9 of ITA 2007 (special rates for trustees' income) as the grossed up amount.

(5) In this section "the grossed up amount" means the actual amount or value of the distribution, grossed up by reference to the dividend ordinary rate for the tax year.

(6) The income tax treated as paid under subsection (2) is not repayable.

(7) Subsection (2) is subject to the following provisions—

section 504(4) of ITA 2007 (disapplication of certain provisions for income of unauthorised unit trusts),

section 592 of ITA 2007 (no tax credits for borrower under stock lending arrangement),

section 593 of ITA 2007 (no tax credits for interim holder under repo), and

section 594 of ITA 2007 (no tax credits for original owner under repo).

400 **Non-qualifying distributions**

(1) This section applies if a person's income in a tax year includes a non-qualifying distribution.

(2) The person is treated as having paid income tax at the dividend ordinary rate on the amount or value of the distribution.

(3) The income tax treated as paid under subsection (2) is not repayable.

(4) If the distribution is assessed (in whole or in part) at the dividend trust rate by virtue of Chapter 3 of Part 9 of ITA 2007 (trustees' accumulated or discretionary income to be charged at special rates), the trustees' liability for income tax at that rate is reduced.

(5) The amount of the reduction is equal to income tax at the dividend ordinary rate on so much of the distribution as is assessed at the dividend trust rate.

(6) In this section and section 401 “non-qualifying distribution” means a distribution which is not a qualifying distribution.

(7) Subsection (2) is subject to section 504(4) of ITA 2007 (disapplication of certain provisions for income of unauthorised unit trusts).

401 **Relief: qualifying distribution after linked non-qualifying distribution**

(1) Where a person pays an amount in respect of extra liability for a non-qualifying distribution, the person's extra liability for a subsequent qualifying distribution is reduced by that amount if conditions A and B are met.

(2) Condition A is that the non-qualifying distribution consists of the issue of share capital or security.

(3) Condition B is that the qualifying distribution consists of a repayment of the share capital or the principal of the security.

(4) A person's extra liability for a distribution charged to tax for the tax year 1999– 2000 or a later tax year is the amount by which the person's liability to income tax on the distribution exceeds the amount it would be if it were charged only at the dividend ordinary rate.

(5) A person's extra liability for a distribution charged to tax for a tax year after the tax year 1992–93 and before the tax year 1999–2000 is the amount by which the person's liability to income tax on the distribution exceeds the amount it would be if it were charged only at the lower rate.

(6) A person's extra liability for a distribution charged to tax for a tax year before the tax year 1993–94 is the amount by which the person's liability to income tax on the distribution exceeds the amount it would be if it were charged only at the basic rate.

(6A) The reduction under this section is given effect at Step 6 of the calculation in section 23 of ITA 2007.

(7) In this section “security” has the meaning given in section 254(1) of ICTA.

19. The effect of s397 is to provide for a tax credit for qualifying distributions from UK resident companies. Under s397(1), a non-refundable tax credit is provided equivalent to 1/9th of the value of the distribution. s398(1) provides that the value of the distribution is grossed-up so as to include the tax credit (that is to say by 100/90) and it is this grossed-up amount which is treated as the taxpayer’s taxable income.

20. For example, if a taxpayer receives a dividend from a UK resident company of £90, the tax credit is £10 (£90 x 1/9). The dividend is grossed-up to £100 under s398. The taxpayer is treated as having taxable income of £100, but treated as if he had paid £10 tax on that income.

21. Section 399 operates differently. Rather than providing for a tax credit, s399(2) treats the taxpayer as having paid income tax at the dividend ordinary rate. In the event that the taxpayer's liability to income tax is less than the amount of tax deemed paid, the tax deemed paid is not repayable.

22. Assuming that s399 can apply to a UK resident taxpayer (an issue in dispute), if a taxpayer received a dividend of £90, he would be treated as having paid income tax on that dividend at the dividend ordinary rate (at all relevant times 10%), that is to say £9. However the taxpayer only has to bring into account for tax purposes £90 of taxable income. A UK resident taxpayer would not be treated as having received the grossed-up amount, as the grossing-up provisions in s399(3) are expressed only to apply to non-UK residents. The taxpayer is treated as having taxable income of £90, and treated as if he had paid £9 tax on that income.

23. To basic rate taxpayers, there is no difference between s397 and s399 in the amount of tax which they will have to pay. However, for a higher rate taxpayers, under s397 they would have to account for £100 of income (with a £10 credit), whereas under s399 they would have to account for £90 of income (with a £9 credit). The net effect is that under s399, a higher rate taxpayer enjoys a lower effective rate of tax (22.5% in the periods under appeal), compared with s397 (25%).

Tax Law Rewrite Project

24. The long title of ITTOIA is

> An Act to restate, with minor changes, certain enactments relating to income tax on trading income, property income, savings and investment income, and certain other income; and for connected purposes.

25. ITTOIA was enacted as part of the Tax Law Rewrite Project. The origins of the Project can be found in s160, Finance Act 1995 which provided for the (then) Inland Revenue to prepare a report on tax simplification. Explanatory notes are prepared in respect of Bills before Parliament for the benefit of its members. The explanatory notes to (the Bill that became) ITTOIA record what then happened:

> 8. In December 1995 the Inland Revenue presented a report to Parliament on the scope for simplifying the United Kingdom tax system (*The Path to Tax Simplification*). The main recommendation was that United Kingdom direct tax legislation should be rewritten in clearer, simpler language.

> 9. This recommendation was welcomed, both in Parliament and in the tax community. In his November 1996 Budget Statement, the then Chancellor of the Exchequer (the Rt Hon Kenneth Clarke MP QC) announced that the Inland Revenue would propose detailed arrangements for a major project to rewrite direct tax legislation in plainer language.
>
> 10. The project team was given the task of rewriting the United Kingdom's existing primary direct tax legislation. The aim is that the rewritten legislation should use simpler language and structure than previous tax legislation. The members of the project are from different backgrounds, including Inland Revenue employees, private sector tax professionals and parliamentary counsel, including (as head of the drafting team) a senior member of the Parliamentary Counsel Office.

26. ITTOIA is one of a series of statutes enacted by Parliament which rewrote the UK's primary direct tax legislation.

27. The provisions relevant to this appeal that were rewritten by ITTOIA were s231 and s233 Income and Corporation Taxes Act 1988 ("ICTA"). Section 231 ICTA was rewritten as s397, and s233 ICTA was rewritten as s399.

28. At this point we should note that a change in the law is mentioned in Annex 1 to the explanatory notes in relation to ss397, 399 and 400 – but this has nothing to do with the issues before the Tribunal, rather the amendments relate to the position of companies acting in a fiduciary or representative capacity. There is no reference in the explanatory notes to any amendments made by ITTOIA in relation to the issues we have to consider.

29. Under the regime as originally enacted in ICTA, distributions from UK resident companies were taxed in the hands of individual shareholders under Schedule F, and distributions from non-UK resident companies were taxed under Case V of Schedule D.

30. Section 231 ICTA originally provided for a tax credit equal to the rate of advance corporation tax ("ACT") on distributions made by UK companies. With the abolition of ACT from 6 April 1999, a credit of 1/9th of the amount of the dividend was introduced, together with a new regime for Schedule F. New s1A(1A) and s1B ICTA provided for a Schedule F ordinary rate of 10% and an upper rate of 32.5%. This new rate applied not only to Schedule F income, but also to distributions from non-UK companies taxable under Case V of Schedule D.

31. Section 233 ICTA (like s399) did not provide for a tax credit, but instead treated the taxpayer as having paid income tax at the Schedule F ordinary rate.

32. Both s231 and s233 were included within Part VI, ICTA. Section 20(3) ICTA makes express reference to Part VI in relation to the charge under Schedule F. There is no provision which applies Part VI (or which refers to Part VI) in relation to income falling within Case V of Schedule D.

Issues before the Tribunal

33. HMRC's position is that s399 does not apply to UK resident individuals who receive distributions from non-UK resident companies.

34. Mr Shirley's position is that the wording of the legislation is clear and that s399 applies to dividends received by UK resident individuals from non-UK resident companies. He submits that the legislation is not reasonably capable of having any other meaning, and that the context and other factors support his interpretation. He also submits that due to principles of EU law, the Tribunal is not entitled to adopt the interpretation for which HMRC contend.

35. HMRC's interpretation is based upon the following:

(1) The overall purpose and rationale of Chapter 3 and Part 4 of ITTOIA

(2) The content and wording of the surrounding sections of ITTOIA and

(3) The fact that ITTOIA is a tax law rewrite statute and there was no intention to change the law.

36. Section 399, on its face, is not expressly limited to qualifying distributions from UK companies, or (latterly) non-UK companies within s397A.

37. ITTOIA was enacted as part of the Tax Law Rewrite Project, and s399 is rewritten legislation. HMRC's argument is, at least in part, that it was not the intention of the rewrite (at least as regards s399) to change the law, and that it is permissible (at least in the circumstances of this appeal) to consider the previous law when interpreting a rewrite statute.

Interpretation of Tax Law Rewrite Statutes

38. The approach to be taken in construing a tax law rewrite statute was set out in the decision of Sales J in *Eclipse Film Partners (No 35) LLP v HMRC* [2013] UKUT 639 (TC) at paragraph 97:

> The law regarding the approach to construction of a consolidating statute was explained by the House of Lords in *Farrell v Alexander* [1977] AC 59 and is well settled. When construing a consolidating statute, which is intended to operate as a coherent code or scheme governing some subject matter, the principal inference as to the intention of Parliament is that it should be construed as a single integrated body of law, without any need for reference back to the same provisions as they appeared in earlier legislative versions: see *Farrell v Alexander* [1977] AC 59, 73B-C (Lord Wilberforce), 82B-D and 83D-H (Lord Simon of Glaisdale) and 97B-E (Lord Edmund-Davies). An important part of the objective of a consolidating statute or a project like the Tax Law Rewrite Project is to gather disparate provisions into a single, easily accessible code. That

> objective would be undermined if, in order to interpret the consolidating legislation, there was a constant need to refer back to the previous disparate provisions and construe them. Therefore the court's main task in this case must be to construe the ITTOIA without reference back to section 18 ICTA and Schedule D. However, where, after undertaking such an exercise, a provision which falls to be applied is found to be ambiguous, a subordinate presumption comes into play, namely that it is presumed that there was no intention to change the meaning of the provision which has been repeated in the same language in the consolidated code. In such circumstances, it may be relevant to try to determine the meaning of the relevant provision by looking to see what it meant when it was previously enacted: see [1977] AC 59 at 73B (Lord Wilberforce), 84D-H (Lord Simon of Glaisdale) and 97B (Lord Edmund-Davies).

39. In other words, in interpreting a tax law rewrite statute reference to the prior legislation is not permitted, unless the rewrite statute is itself ambiguous.

40. Authority for this approach can be found in the decisions of the House of Lords in *IRC v Joiner* [1975] 1 WLR 1701 and *Farrell v Alexander* [1977] AC 59.

41. In *IRC v Joiner*, two of the members of the Appellate Committee refer in their speeches to the approach to be taken to the interpretation of consolidation statutes. Viscount Dilhorn (at page 1709A) says:

> The practice of consolidation would lose much of its point if, whenever a question as to construction arose, reference had to be made to the individual Acts consolidated. Only when the consolidation Act itself gives no guidance as to its proper interpretation should it be permissible in my opinion to refer to the earlier Acts.

42. Lord Diplock (with whom Lord Edmund-Davies agreed) says (at page 1710H):

> The modern practice of parliamentary draftsmen in preparing for adoption by Parliament legislation to effect a change in the existing law, particularly when the subject-matter of the law is one, such as taxation, in which legislative changes are frequent, is to express the changes to be effected in the form of amendments to the language of particular provisions in earlier statutes dealing with the same subject-matter. This method of drafting becomes progressively more cryptic as amendments to previous amendments follow one another in successive statutes. The need to refer to and fro and back and forth between ever-increasing numbers of different statutes in order to discover what a particular provision of any of those statutes means reaches a point at which the difficulty of finding out what the law is may have the practical consequence of depriving the citizen of his right to know, in advance of a decision of your Lordships' House which must needs be *ex post facto*, what the legal consequences will be of a course of conduct which he contemplates adopting. The purpose of a consolidation Act is to remove this difficulty by bringing together in a

> single statute all the existing statute law dealing with the same subject-matter which forms the general context in which the particular provisions of the Act fall to be construed, so that it will be no longer necessary to seek that context in a whole series of amended and re-amended provisions appearing piecemeal in earlier statutes. This is the only purpose of a consolidation Act; this is the only "mischief" it is designed to cure. It is true that a consolidation Act is not intended to alter the law as it existed immediately before the Act was passed, but to treat this absence of intention as justifying recourse to the previous legislation repealed by the consolidation Act in order to ascribe to any of the provisions of that Act a meaning different from that which it would naturally bear when read only in the context of the other provisions of the consolidation Act itself, would be to defeat the whole purpose of this type of legislation-to allow the absence of a tail to wag the dog.
>
> So the primary rule of construction of a consolidation Act is to examine the actual language used in the Act itself without reference to any of the statutes which it has repealed. If this examination leads to the conclusion that, when read in the context of the other provisions of the Act, the language in which a general description of some factual situation is expressed is more apt to include than to exclude the particular factual situation found to exist in the case for decision or *vice versa*, the duty of the court is to ascribe to that language the more apt meaning and to give effect to it accordingly. It is only where such an examination of the actual language of the general description has led to the conclusion that it is no more apt to include than to exclude the particular factual situation, that it is permissible for a court of construction to have recourse to the repealed legislation in order to see if its meaning was clearer, and, if it was, to ascribe to the corresponding provision of the consolidation Act a meaning which would not involve an alteration in the previous law.

43. Sales J in *Eclipse Film Partners* refers to the decision of the House of Lords in *Farrell v Alexander*. This was a case which turned on the interpretation of the Rent Act 1968, which was a consolidating statute. The House of Lords reached their decision by a majority (Lord Russell dissenting). Each of members of the Appellate Committee delivered a separate speech, and none of the speeches expressed agreement with any of the other speeches. Only three of the speeches consider in any detail the approach to be taken when interpreting a consolidation statute.

44. Lord Wilberforce (at page 72G) said:

> I would agree and endorse the principle that it is quite wrong that, in every case where a consolidation Act is under consideration, one should automatically look back through the history of its various provisions, and the cases decided upon them, and minutely trace the language from Act to Act—a process, which, incidentally, has led to an argument of four days' length in this House. In recent times, because modern statutes have become so complicated, the courts myself included (cf. *IRC. v. Joiner*

[1975] 3 All ER. 1050) rather too easily accept this process, whether under persuasion of counsel or from their own scholarly inclinations. But, unless the process of consolidation, which involves much labour and careful work, is to become nothing but a work of mechanical convenience, I think that this tendency should be firmly resisted ; that self-contained statutes, whether consolidating previous law, or so doing with amendments, should be interpreted, if reasonably possible, without recourse to antecedents, and that the recourse should only be had when there is a real and substantial difficulty or ambiguity which classical methods of construction cannot resolve.

45. Lord Edmund-Davies (at page 94B) said:

Although it effected amendments to sections 32 and 34 of the Rent Act 1965, the 1968 Act was, and was described as, a consolidating enactment. As such, there is a presumption that it was not intended to alter the law and accordingly, if the need arises, regard may be had to decisions on the construction of the earlier enactments which are consolidated, even if the words used are not identical, though this presumption must yield to plain words to the contrary; see *Halsbury's Laws of England*, 3rd ed. Vol. 36, p. 406 and the cases there cited. But where earlier legislation has been substantially altered by amending legislation before consolidation, decisions on the earlier provision cannot affect the construction of the later; ibid, p. 407. It is legitimate to refer to an earlier statute in *pari materia*, even if it has expired or has been repealed, but "only where there is an ambiguity" (per Lord Russell of Killowen, C.J., *Reg. v. Titterton* {1895] 2 QB 61, at 66). As my noble and learned friend, Lord Simon of Glaisdale, said in *Maunsell v. Olins* [1974] 3 WLR. 835, at 847D)—

"It has been generally accepted in the past that there is a presumption that Parliament does not intend by a consolidation Act to alter the pre-existing law: see *Maxwell* pp. 20-25 and *Beswick v. Beswick* [1968] AC 58, 73 ... But . . . such a presumption has no scope for operation where the actual words of the consolidation Act are not, as a matter of legal language, capable of bearing more than one meaning. The docked tail must not be allowed to wag the dog ".

46. In his speech, Lord Simon first describes three kinds of consolidating acts (at page 82B):

There are three sorts of consolidation Act: (1) "pure" consolidation (i.e., re-enactment); (2) consolidation under the Consolidation of Enactments (Procedure) Act 1949, which allows consolidation with "corrections and "minor improvements" (for their definition see Lawton L.J. in the instant case [1976] Q.B. at page 366D); (3) consolidation "with Law Commission "amendments" under a procedure adopted by parliament in 1965. What all three types of consolidation have in common is that there is a short circuiting of the normal parliamentary procedures. This can be seen by comparison with the nearest parliamentary analog—an Act "to consolidate

> and amend" the previous law. This was formerly a very common legislative exercise, and very advantageous to all except government business managers. Its objection for the latter is that all stages of the bill leading to the Act are subject to normal and full parliamentary control; so that amendments may be made, not only to the amending provisions of the bill, but also to those provisions which merely re-enact the pre-existing statute law. Such measures therefore make the full normal demand on the parliamentary timetable. By contrast, the detailed scrutiny of every type of consolidation bill is referred to a joint select committee of both Houses of Parliament; and, in reliance on the report of this committee, the Houses forego discussion (and, other than exceptionally, amendment) of the consolidation bill in so far as it merely re-enacts pre-existing statute law (including re-enactment with " corrections and minor improvements " in the case of 1949-Act-procedure bills). The long title of the statute shows whether it is a consolidation Act: if it is merely "to consolidate . . .", it is a "pure" consolidation Act; while if it is under the 1949 or 1965 procedures this will be specifically indicated in the long title (see, e.g., Juries Act 1974; Friendly Societies Act 1974). Special parliamentary practice governs consolidation under the 1949 and 1965 procedures respectively; and, should a consolidation Act passed under either of these procedures fall for interpretation, I would hope that the court of construction would not make heavy weather of discovering how much of the Act in question represents amendment and would in interpretation discriminate between 1949-and 1965-type amendments. But no such questions arise on the instant appeal; the Rent Act 1968 is "pure" consolidation.

47. To pause for a moment, Mr Yates, for HMRC, submits that ITTOIA is analogous to a consolidation act falling into the second of Lord Simon's three categories – namely a re-enactment of the prior law with corrections and minor improvements.

48. Lord Simon then went on to consider the circumstances in which it was permissible to consider the previous law when interpreting a consolidation statute (at page 84C):

> It might be objected that the statutory objective of a consolidation Act is merely to consolidate the previous law; so that it is necessary to look back to the superseded legislation to ascertain its various statutory objectives. But in vindicating the paramount objective of consolidating the preceding statute law the consolidation Act is also furthering the statutory objectives of the legislation which is consolidated. […] [T]he various statutory objectives will be apparent from a scrutiny of the provisions of the consolidation Act itself (possibly aided by judicial notice and perusal of official reports). The primary approaches to statutory interpretation (which I have tried to summarize earlier) are therefore as appropriate for construction of a consolidation Act as for any other type of statute. It is only on failure of the primary aids to construction that the fact that the statute to be construed is a consolidation Act permits any special approach: what it does then is to provide an additional secondary canon of construction which will sometimes be of service—namely, a presumption

> that a consolidation Act (in so far as it merely re-enacts) does not change the law.
>
> If a court of construction places itself in the position of the draftsman, acquires his knowledge, recognizes his statutory objectives, tunes in to his linguistic register, and then ascertains the primary and natural meaning in their context of the words he has used, that will generally be an end of the task of construction. But occasionally something will go wrong. It may become apparent that the primary and natural meaning cannot be what Parliament intended: it produces injustice, absurdity, anomaly or contradiction, or it stultifies or runs counter to the statutory objective. Or sometimes the words have no primary meaning in their context; they are fairly capable in all the circumstances of being taken in two senses: there is, in other words, an ambiguity. There are a number of secondary canons of construction avail- able to resolve ambiguity: which of them is most helpful will vary from case to case. But in nothing of the foregoing does the construction of a consolidation Act differ from that of any other statute. Its only peculiarity is that if the primary approach to construction discloses an ambiguity in a consolidation Act, that may sometimes (though rarely) be resolved by examination of the superseded legislation.

49. Mr Yates submits that reference can be made to prior legislation not only when the legislation is ambiguous, but also where a literal interpretation results in "injustice, absurdity, anomaly or contradiction, or it stultifies or runs counter to the statutory objective". In support of this submission, he refers to the speech of Lord Simon quoted above, but also to the decision of the Court of Appeal in *O'Rourke v Binks* [1992] STC 703, which concerned the taxation of "small" capital distributions. Section 72(2) Capital Gains Tax Act 1979 ("CGTA") allowed a capital distribution to be ignored as a capital disposal where an Inspector of Taxes was satisfied that it was "small", in such cases the amount of the capital distribution was instead deducted from the expenditure attributable to the shares. (in other words the base cost). Section 72(4)(a) disapplied section 72(2) where the amount of the capital distribution exceeded the base cost, and section 74(4)(b) provided for an election that any amount distributed would be reduced by the amount of allowable expenditure.

50. The taxpayer argued that section 72(4)(b) permitted an election to be made regardless of whether the capital distribution fell within section 72(2) in the first place (namely that the distribution was "small"). In his judgment Scott LJ (with whom Stuart-Smith LJ agreed) says (at page 707h):

> It is, however, pointed out that sub-s (4) contains no express limitation of the scope of the subsection. It is said that, read literally, and there being no express limitation, the subsection applies to all capital distribution cases, whether or not small. I agree that, read literally, that is so. Mr Bretten QC, counsel for the taxpayer, contended that on a literal reading of sub-s (4) the meaning was clear, there was no ambiguity, and a court of construction

> had no alternative but to give effect to the express statutory language contained in the subsection.
>
> I am unable to accept that this strict approach is the right one. An ambiguity in a statutory provision may arise in more than one way. In the present case, s 72(4) read in the context of the 1979 Act as a whole and, in particular, in the context of s 72 as a whole, leads the reader to conclude that the statutory intention was to limit the subsection to small distributions. That was how the judge read it. That was how I read it. The natural construction of sub-s (4) in its context is, in my opinion, that it is limited in its scope. But the absence of any express limitation makes it possible that no limitation was intended. The contrast between the limitation that would be inferred from a reading of the subsection in its statutory context on the one hand, and the absence of any express limitation on the other hand, produces, in my judgment, an ambiguity.
>
> Accordingly, in my opinion, it is permissible as an aid to construction, as an aid to identifying the legislative intention behind s 72(4), to take into account the anomalies that the absence of any limitation to the scope of the subsection will produce. It is permissible to take account of the antecedent legislation. The 1979 Act is a consolidating Act and it is to be presumed that there was no intention to change the previous law. It is permissible to take account of the manner in which, in the 1979 Act, other types of small distributions are dealt with.

51. It is worth noting that Lloyd LJ in his concurring judgment is able to reach the same conclusion as to the interpretation of the provisions, but without finding that there was an ambiguity and without the need to refer to the antecedent legislation.

52. We were also referred to various other decisions which deal generally with the approach to be taken in interpreting a statute.

53. In his decision in *Chevron UK v IRC* [1995] STC 712, Vinelot J says (at page 721):

> The fundamental principle was stated by Lord Wilberforce in a well known passage in *W T Ramsay Ltd v IRC* [1981] STC 174 at 179, [1982] AC 300 at 323:
>
> "A subject is only to be taxed on clear words, not on "intendment" or on the "equity" of an Act. Any taxing Act of Parliament is to be construed in accordance with this principle. What are "clear words" is to be ascertained upon normal principles; these do not confine the courts to literal interpretation. There may, indeed should, be considered the context and scheme of the relevant Act as a whole, and its purpose may, indeed should, be regarded ..."
>
> It can never be right to look at a specific provision in a taxing Act, any more than in other legislation, in isolation and to resort to the context and scheme of the Act as a whole, only if that provision taken in isolation gives rise to an apparent equivocation or ambiguity. The question whether a

> literal construction gives rise to an absurd, unjust or capricious result can be answered only if the particular provision under consideration is placed in its setting as part of the legislative scheme. The question must always be whether it can be read in a way which, taken as part of the Act as a whole, produces a coherent and reasonable result. There may be cases where 'to achieve the obvious intention and produce a reasonable result [the court] must do some violence to the words' (see *Luke v IRC* [1963] AC 557 at 577, 40 TC 630 at 646 per Lord Reid); or, without doing violence to the words used, the court may be able to avoid an unreasonable result by the importation of an implied restriction covering the scope of a particular provision (as in *O'Rourke (Inspector of Taxes) v Binks* [1992] STC 703). There is nothing new or revolutionary in this approach to construction, although in recent years no doubt greater emphasis has been placed upon the need to discern the legislative purpose and to fit the particular provision under consideration into a reasonable and coherent scheme and less upon semantic delicacy. It would be a very rare case when the court would feel compelled to conclude that although the legislative purpose was clear the legislation had "missed fire".

54. In *Pepper v Hart* [1992] STC 898 Lord Browne-Wilkinson says at page 919 (cited with approval by Lord Neuberger MR in *Chilcott v HMRC* [2011] STC 456 at page 830):

> The court cannot attach a meaning to words which they cannot bear, but if the words are capable of more than one meaning why should not Parliament's true intention be enforced rather than thwarted.

55. We were also referred to a number of older cases (which are listed at the end of the decision) but we did not find that these added materially to the description of the law as given in the decisions from which we have quoted.

56. We draw from these decisions the following as the approach to be taken to the construction of a Tax Law Rewrite Statute:

(1) We first examine the actual language used in the Act itself without reference to any of the statutes which it has replaced.

(2) In interpreting the language of the Act, we adopt the usual canons of statutory interpretation – giving consideration to the "clear words" of the legislation. What are "clear words" is to be ascertained upon normal principles; these do not confine us to literal interpretation. We must consider the context and scheme of the relevant Act as a whole, and its purpose.

(3) In undertaking this exercise, we are only permitted to adopt an interpretation that the statutory language is reasonably capable of bearing.

(4) Only when there is a real and substantial difficulty in interpreting the provisions, or there is an ambiguity which classical methods of construction cannot resolve, can the recourse be had to the antecedent legislation.

57. We disagree with HMRC's submission that recourse can be had to antecedent legislation where the interpretation would otherwise result in "injustice, absurdity, anomaly or contradiction, or it stultifies or runs counter to the statutory objective". This was a phrase used by Lord Simon in his speech in *Farrell v Alexander*. However none of the other members of the Appellate Committee in that case agreed with this formulation, and we therefore do not consider that it is binding upon us. However we note that an interpretation that leads to injustice etc. may not accord with the clear words of the legislation, and that a literal interpretation of the legislation may be inappropriate – even without having regard to antecedent provisions.

58. We note that in *O'Rourke* Scott LJ considered that he was able to refer to antecedent legislation, not because the provisions before him were anomalous, but because the anomaly led to the conclusion that the legislation was ambiguous in the particular context. We also note that Lloyd LJ was able to adopt a non-literal approach to the interpretation of s72 CGTA without recourse to the antecedent legislation.

Contentions of Mr Shirley

59. The primary contention of Mr Firth on behalf of Mr Shirley is that the clear and ordinary meaning of the words in s 399 apply to dividends from non-UK resident companies.

60. The relevant words are:

> This section applies if a person is not entitled to a tax credit for a qualifying distribution included in the person's income for a tax year. (s399(1) for 2005/6 and 2007/8)
>
> This section applies if a person is not entitled to a tax credit under section 397 or 397A for a qualifying distribution included in the person's income for a tax year (s399(1) for 2008/9)

61. "Qualifying distribution" is a defined term. Schedule 4 ITTOIA refers to s832(1) ICTA (for 2005/6) or s989 Income Tax Act 2007 (for 2007/8 and 2008/9). These provisions refer in turn to s14(2) ICTA:

> (2) In this Act "qualifying distribution" means any distribution other than—
>
> (a) a distribution which, in relation to the company making it, is a distribution by virtue only of section 209(2)(c); or
>
> (b) a distribution consisting of any share capital or security which the company making the distribution has directly or indirectly received from the company by which the share capital or security was issued and which, in relation to the latter company, is a distribution by virtue only of section 209(2)(c).

62. Mr Firth submits that the definition of "qualifying distributions" is not restricted to distributions from UK companies as the definition refers to "any" distribution. Neither of the qualifications in paragraphs (a) and (b) are relevant to the present case.

63. As the language of the statute is clear and unambiguous, Mr Firth submits that the Tribunal is not permitted to consider the prior law. Even if the effect of ITTOIA was to make "accidental" changes to the meaning of the legislation as a result of the rewrite, Parliament accepted those changes as the price of tax simplification. This is illustrated by Judge Bishopp's decision in *Barnetts (a firm) v HMRC* [2010] UKFTT 286 (TC) at paragraph 11:

> The difficulty with that argument, in my judgment, is that while it may be that the Rewrite Project did not intend to make material changes, s366(1) [ITTOIA] is in unambiguous terms which may be overridden, by virtue of 2(3) only by another rule of law […] The change, if change it is, may have been unintended but in my view the statutory rules are clear.

64. But even if the Tribunal were to refer to the antecedent law, Mr Firth submits that it would not help HMRC's arguments. The prior law was contained in s233 ICTA, and as s233 ICTA contained no restriction limiting its provisions to distributions from UK resident companies, a distribution from a non-UK resident company would fall within the provision if the recipient of the distribution was not entitled to a tax credit. Whilst s233 ICTA deems tax to have been paid at the Schedule F Ordinary Rate, that, submits Mr Firth, is merely a reference point for the amount of tax deemed to have been paid – it does not matter under which Schedule the distribution is taxed.

65. Further, Mr Firth submits that s397 ITTOIA makes it clear that qualifying distributions must include distributions by non-UK companies. Section 397 refers to "a qualifying distribution made by a UK resident company". The limitation to UK resident companies would not be necessary if "qualifying distributions" related only to UK companies. Finally, when s14(1) ICTA was in force, it charged advance corporation tax "where a company resident in the United Kingdom makes a qualifying distribution". Again, if, it were the case that "qualifying distribution" was limited to distributions made by UK companies, the limitation in s14(1) would not be necessary.

66. Mr Firth submits that when enacting ITTOIA, Parliament must have contemplated that s399 applied to qualifying dividends from non-UK resident companies. This is because s399(3) includes the phrase "if the person is non-UK resident". Because s399(3) explicitly singles out "non-UK residents", the implication must be that s399 can potentially apply both to UK and non-UK residents. As it is accepted that UK residents receiving qualifying distributions from UK resident companies would receive a tax credit (and so must fall outside s399), Parliament must have contemplated that s399 applies to qualifying distributions from non-UK resident companies, as that is the only way in which it could possibly apply to a UK resident.

67. As originally drafted, Chapters 3 and 4 of Part 4 of ITTOIA were entitled "Dividends etc. from UK resident companies etc." and "Dividends from non-UK resident companies".

68. Mr Firth explains the first "etc" in the title to Chapter 3 by reference to the fact that the charge in Chapter 3 encompasses not only dividends, but distributions generally. He explains the second "etc" because the Chapter also includes provisions dealing with distributions otherwise than from UK resident companies. He submits that these include distributions from non-UK resident companies. The fact that the title to Chapter 3 was later amended to include an express reference to distributions from non-UK resident companies does not undermine the fact (according to Mr Firth) that the Chapter previously so applied, as recognized by the second "etc".

69. Mr Firth referred us to s382, which introduces Chapter 3. He noted that sub-section (1)(a) specifies that the Chapter applies to distributions from UK resident companies, whereas subsection (2) refers to "certain distributions" (without any express "UK" qualification). From this Mr Firth reaches the conclusion that Parliament makes express reference to distributions from UK companies when that is what it means, and so the reference in sub-section (2) to "certain distributions" must mean that Parliament intended that s399 applies to distributions from non-UK companies.

70. Sub-section (2) also specifies that Chapter 3 applies to distributions, even if they are not otherwise dealt with under Chapter 3. Mr Firth submits that this must mean that there is no link between the charging provisions in Chapter 3 and the relieving provisions. HMRC gave one example in their Statement of Case where a dividend might not be taxed under Chapter 3, namely when the dividend is trading income – but, submits Mr Firth, that does not rule out other reasons.

71. Mr Firth noted that even after s397A was inserted into ITTOIA by Finance Act 2008, s383(2) continued to refer to "certain distributions" and applied "whether or not the distributions are otherwise dealt with under this Chapter". Further, the title of the Chapter was amended to "Dividends etc. from UK resident companies and tax credits etc. in respect of certain distributions". It must therefore follow, submits Mr Firth, that "certain distributions" can include distributions by non-UK resident companies and that the drafting of s383(2) is apt to include such distributions.

72. Mr Firth noted that following the amendments made by the Finance Act 2008, s399(1) was amended to read:

> (1) This section applies if a person is not entitled to a tax credit under section 397 or 397A for a qualifying distribution included in the person's income for a tax year.

73. Mr Firth noted that s397A applies only to distributions made by non-UK resident companies; the fact that s397A was specifically carved out from the scope of s399

demonstrates that s399 would otherwise have applied to distributions from non-UK resident companies (at least in respect of the tax year 2008/09 – from when the amendments made by the Finance Act 2008 took effect).

74. Mr Firth also noted that although tax credits for non-UK distributions were introduced into Chapter 3 by s397A, the charging provision for non-UK distributions are not in that chapter – the charging provisions for non-UK dividends are in Chapter 4. Mr Firth submits that this demonstrates that there is no link between whether a distribution is chargeable under Chapter 3, and whether it falls within the scope of the tax credit/deemed payment of tax provisions.

75. Finally, Mr Firth referred us to points of EU law. Mr Firth submits that if s399 is construed as HMRC suggest, this would result in a breach of the EU principle of free movement of capital. Mr Shirley's position is that it is unnecessary for him to rely on principles of EU law for his appeal to succeed – but makes the submission nonetheless that as a matter of EU law, the Tribunal is not entitled to interpret the legislation in dispute in the manner for which HMRC contend. Mr Firth's submission is that the Tribunal should not give s399 a construction which is incompatible with the UK's obligations as a matter of EU law. This is because, first, the Tribunal should presume that Parliament intends that its legislation is compatible with EU law, and secondly because (irrespective of Parliamentary intention) the Tribunal must give effect to EU law.

Contentions of HMRC

76. Mr Yates on behalf of HMRC contends that it is apparent that Parliament intended in s397 to limit tax credits to qualifying distributions from UK companies.

77. The tax credit was an element of the partial imputation system of corporation tax introduced in the early 1970s, and gave individual shareholders some credit for the tax paid by the company on the income from which the distribution was paid. The effect was to mitigate (but not entirely eliminate) the economic double taxation that otherwise arises in a classical system of corporate taxation.

78. In contrast (putting aside EU considerations), Mr Yates submits that there was no need to provide for any credit in respect of distributions made by non-UK companies, as there was no UK economic double taxation, as the foreign company had not suffered any UK tax. Tax credits were extended to relevant distributions from non-UK resident companies with the introduction of s397A from 2008/9, but this serves to highlight the fact that previously tax credits were only available for distributions from UK resident companies.

79. Mr Yates contends that s399 has a limited role – to provide a tax credit where the requirements of s397 (and latterly s397A) are satisfied in respect of the distribution, but not in respect of the individual. In most cases the individual will not be eligible because he is not UK resident. However there are circumstances where s397 does not apply in the

case of a qualifying distribution received from a UK resident company. HMRC acknowledge that if s399 were intended only to apply to non-UK residents in respect of distributions from UK resident companies, then the wording of s399(3) and s399(4) are in tension with this. However Mr Yates submits that Parliament did not want to rule out "niche" situations which might have previously been permissible under s233 ICTA (which, like s399, is not expressly limited to non-UK residents). Mr Yates says that in leaving open the possibility for certain UK residents to be able to make claims under s399, Parliament intended to retain the *status quo ante*, rather than intending to allow s399 to be claimed by everyone, regardless of whether the distribution was made by a UK or a non-UK resident company.

80. Mr Yates further submits that if it really was the case that s399 meant that individuals such as Mr Shirley could claim a deemed payment of income tax in respect of foreign dividends, there would be no rationale in setting up detailed restrictions for tax credits under s397 and s397A, given that a more generous treatment was available under s399.

81. Mr Yates also submits that the context and wording of the surrounding provisions also support (or at least are consistent with) HMRC's interpretation.

82. As regards the title to Chapter 3, Mr Yates says agrees with Mr Firth that the first "etc" refers to distributions which are not dividends. He also agrees with Mr Firth that the second "etc" refers to distributions otherwise that from UK companies. However, in contrast to Mr Firth he considers that this is a reference to distributions made by UK entities other than companies (such as OIECs and Authorized Unit Trusts) which are also taxed under s382.

83. With the insertion of s397A by the Finance Act 2008, a number of other amendments were made to the legislation:

(a) The title of Chapter 3 was changed to "Dividends etc. from UK resident companies and tax credits etc. in respect of distributions"

(b) Sections 397A to 397C were inserted

(c) Section 399 was amended to include a reference to s397A.

84. Mr Yates submit that the fact that these amendments were all made to Chapter 3, and not Chapter 4 does not detract from the arguments relating to the operation of Chapter 3 prior to the amendments.

85. Mr Yates acknowledges that the references to s397A have the effect of expanding the scope of s399 to include dividends and other distributions that would otherwise fall within s397A. However he submits that the points raised in relation to the interaction between s 397 and s399 which are discussed above carry across to the interaction between s 397A and s399. He also notes that in ss397A to 397C, Parliament enacted a

detailed code setting out the circumstances in which a tax credit can be claimed in respect of a dividend from a non-UK resident company. If the interpretation for which Mr Shirley contends is correct, this would be entirely unnecessary, as a more generous relief would be available under s399.

86. It was submitted on behalf of Mr Shirley by Mr Firth that s397A was a “carve out” from s399, rather than an extension to s397. Mr Yates submitted that this was a strained use of language, particularly given the use of the tax credit mechanism. Mr Yates submitted that Parliament enacted the provisions on the basis that no relief was afforded in respect of foreign dividends prior to the amendments made by the Finance Act 2008, either by s397 or by s399, and it was unreal to suggest that Parliament was consciously providing a tax credit in circumstances where it understood that s399 already provided for a deemed payment of tax.

87. We were referred by Mr Yates to the explanatory notes to the relevant clauses of the Finance Bill 2008:

> When dividends from UK resident companies are charged to tax, shareholders are entitled to a non-payable tax credit of one-ninth of the distribution under the provisions of s397(1) of the Income Tax (Trading and Other Income) Act 2005. Because tax is charged on the gross dividend received, including the tax credit, this lowers the effective rate of tax on these dividends at the personal level to 0 per cent and 25 per cent. By contrast, until now, there has been no tax credit available to shareholders in non-UK resident companies.

88. Mr Yates acknowledged the principle established in *John Hudson & Co v Kirkness* [1955] AC 696 that the Tribunal cannot use subsequent legislation as an aid to the interpretation of prior legislation. But Mr Yates submits that the principle in *Hudson* does not apply (a) when interpreting the legislation as it stood in 2008/09, only to earlier years, and (b) when the prior legislation is itself ambiguous, as was (he submitted) the case here. Mr Yates submitted that the phrase in s399 “if a person is not entitled to a tax credit under section 397 for a qualifying distribution” is inherently ambiguous because it could mean a person not entitled by virtue of their residence or a person not entitled by virtue of the residence of the distributing company.

89. But in any event, as regards all of the periods under appeal, Mr Yates submits (a) because the drafting of s399 is itself ambiguous, and (b) that the illogicality of a literal reading of the provisions is an indication that they are ambiguous (per *O’Rourke*). For these reasons this Tribunal can (and should) have regard to what Parliament understood the law to be when enacting the Finance Act 2008, not least that s233 ICTA did not apply to distributions from non-UK resident companies, and Parliament did not intend to change the law when enacting ITTOIA..

90. Mr Yates drew our attention to an article by Mr Shirley in the 2 February 2011 edition of *Taxation*, in which Mr Shirley described the taxation treatment of foreign

dividends as having changed under ITTOIA, whereas, the submissions made by Mr Firth were that the treatment had not changed (see paragraph 64 above). If the Tribunal was to agree with HMRC's position (and Mr Shirley's original position as stated in his article), then Mr Yates submits that this should be taken into account in considering whether (per *O'Rourke*) Mr Shirley's arguments result in an anomalous or absurd result, such that there is an ambiguity, allowing us to take account of the intention of Parliament not to change the law (at least in this respect).

91. As regards the EU law points, Mr Yates submitted that the interpretation favoured by HMRC did not infringe the requirement of EU law – save (since 2009/10) possibly in respect of dividends from Finland and Greece (and certain Irish dividends), in consequence of those countries imposing no (or little) withholding taxes. This is because even if the UK system of tax credits had a discriminatory effect, there would be no breach of EU law to the extent that any double tax relief in respect of dividend withholding taxes exceeds the credit that would have been available is 397 applied to dividends from non-UK resident companies (see the limited discussion of this point by Henderson J in *Prudential Assurance Co Ltd v HMRC* [2013] EWHC 3249 at [95] to [96]).

92. Because we were (as will become apparent) able to reach a decision without needing to consider the compatibility of these provisions with EU law, we do not deal with these issues further in this decision..

Discussion

93. First, we disagree with Mr Yate's submission that s399 is itself ambiguous. We find that the phrase "if a person is not entitled to a tax credit under section 397 for a qualifying distribution" must refer to both circumstances – namely the residence of the person receiving the dividend and the company paying the dividend. This is because a person not entitled to a tax credit by virtue of the distributing company's residence is "a person [who is] not entitled to a tax credit under section 397".

94. We therefore find that the literal reading of the legislation is unambiguous and supports the interpretation for which Mr Shirley contends. For HMRC to succeed, they need to persuade us that such a literal interpretation is not appropriate.

95. At its root, the question we need to determine is whether the terms of the legislation are such that we can adopt HMRC's interpretation either (a) by using the normal canons of statutory interpretation, or (b) by recourse to antecedent legislation, on the basis that there is an ambiguity (or other real and substantial difficulty) which classical methods of construction cannot resolve.

96. The literal language of the legislation is clear and unambiguous on its face. We consider that the title to the Chapter can be read consistently with the interpretations of both parties, as the second "etc" could refer both to foreign dividends and to dividends

from non-corporates. Nor do we consider that the allocation of the provisions of the legislation between Chapter 3 and Chapter 4 give rise to grounds for finding any ambiguity.

97. Nor do we consider that the amendments made by Finance Act 2008 can be used as an aid to the interpretation of ITTOIA as originally enacted. Both parties acknowledge that we are permitted only to refer to the provisions of subsequent legislation in limited circumstances.

98. In his speech in *John Hudson v. Kirkness* 36 TC 28, Viscount Simonds said (at p63):

> When an Act of Parliament becomes law and its meaning is plain and unambiguous a citizen is entitled to order his affairs accordingly and to act upon the footing that the law is what it unambiguously is. He must be assumed to know that the law may be altered but, if so, he may be assumed to know also that it is contrary to the general principles of legislation in this country to alter the law retrospectively. He should know, too, that, if Parliament alters the existing law retrospectively, it does so by an amendment which is an express enactment and above all he is surely entitled to be confident that it will not do so by force merely of an assumption or an allusion in a later Act. When the *Ormond* case was heard at first instance by Rowlatt, J. he described an argument to the contrary as "a sinister and menacing proposition." So it is, and I hope that your Lordships will have none of it.
>
> My Lords, it follows from what I have said that, even where two Acts are to be read together, it is not permissible to make what is clear in the earlier Act obscure and ambiguous by reference to something in the later Act.

99. Lord Reid (with whom Lord Somervell agreed) said in his speech (at p79 –80):

> So the question is whether Section 17(1)(a) of the Act of 1945 taken in its context in that Act is, as Lord Buckmaster put it, so ambiguous that it is open to two perfectly clear and plain constructions, or whether, as Lord Sumner put it, there is no reason on the face of the Act why one construction should be more right than the other, or whether, as Lord Atkinson put it, the 1945 Act is readily capable of more than one interpretation. A provision is not ambiguous merely because it contains a word which in different contexts is capable of different meanings. It would be hard to find anywhere a sentence of any length which does not contain such a word. A provision is, in my judgment, ambiguous only if it contains a word or phrase which in that particular context is capable of having more than one meaning…
>
> Moreover, I think that, taking the whole trend of the speeches in that case. Lord Sumner must be right in his view that the later Act cannot be used to impose a non-natural construction on the words of the earlier Act, and to hold that sale includes compulsory acquisition would, in my view, be to

> impose on that word a non-natural though in some contexts an appropriate construction.

100. The test laid down in *Kirkness* is whether the legislation is "open to two perfectly clear and plain constructions" (Viscount Simonds elsewhere in his speech referred to the legislation being "fairly and equally open to diverse meanings"). We consider that s399 is, for the reasons given earlier, unambiguous in its terms, and we therefore cannot consider the amendments made by the Finance Act 2008 as an aid to the interpretation of ITTOIA as originally drafted.

101. Nor do we consider that we can refer to the explanatory notes to Finance Act 2008 in aid of the interpretation of ITTOIA as originally enacted. Mr Firth submitted that *Kirkness* was authority only for looking at provisions of subsequently enacted statutes. In relation to other material, such as explanatory notes, the applicable law was to be found in *Inland Revenue Commissioners v Dowdall, O'Mahoney & Co Ltd* [1952] AC 401, which, he submitted, does not permit reliance in any circumstances (even where there is clear ambiguity). The *Dowdall* case related to amendments made by Parliament to the law concerning excess profits tax. The amendments were clearly drafted on the assumption that the prior law allowed equivalent foreign taxes to be taken as a deduction, whereas the case law authorities were clear that no such deduction was allowed – and thus Parliament's assumption was wrong. The House of Lords held that the amendments could not be taken to imply that a right of deduction had previously existed. Mr Yates submitted that this appeal was very different from *Dowdall*, as it was not at all clear that s399 and its predecessors provide for a deemed payment of income tax in relation to a UK resident individual in respect of a foreign dividend, and therefore that Parliament had clearly made a mistake. Mr Yates submits that this not a case where the Tribunal is being asked to consider whether a later Act has changed the law by implication; rather due to the ambiguity of the earlier legislation, a later Act is of some persuasive relevance in construing the earlier legislation. Mr Yates cited the speech of Lord Reed in *Kirkness* itself where at 736 he commented on Dowdall:

> The other case, *Inland Revenue Commissioners v. Dowdall, O'Mahoney & Co. Ld.*, was dealing with rather a different question. There, the earlier statutory provisions could not be said to be ambiguous because their meaning had formed the subject of decisions in this House, and so the later Act could only have effect if it could be held to enact an amendment. But it was held that it could not be so interpreted.

102. At best, according to Mr Yates, the legislation is ambiguous and, this being so, it is permissible to refer to a later enactment.

103. We have reached the conclusion that the explanatory notes to the Finance Act 2008 are not admissible as an aid to the interpretation of the prior legislation. First, contrary to Mr Yates submission, we find the drafting of the legislation to be clear, and that there is no ambiguity. So, the principles in *Kirkness*, (even if they extended to non-statutory materials) would not allow us to admit these items.

104. In addition, in *R (oao H) v IRC* [2002] EWHC 2164 (Admin), Burnton J said (at [27]):

> The 2001 Act is not yet in force. While the Home Secretary's statements to the House of Commons in the debates on the Criminal Justice and Police Bill may, in due course, be admissible under the principle of *Pepper v Hart* [1993] AC 593 to resolve an ambiguity in the Criminal Justice and Police Act 2001, they cannot be relevant or admissible for the purpose of interpreting previous legislation. The beliefs or assumptions of Parliament are not an admissible aid to the interpretation of previous legislation. As Lord Radcliffe said in *Inland Revenue Commissioners v Dowdall, O'Mahoney & Co Ltd* [1952] AC 401 at 426:
>
> "The beliefs or assumptions of those who frame Acts of Parliament cannot make the law."

105. *R (oao) H v IRC* is a decision of the High Court and is binding upon us.

106. For these reasons we find that the explanatory notes to the Finance Act 2008 cannot therefore be used as an aid to the interpretation of ITTOIA as originally enacted.

107. Accordingly, the only basis on which we can consider antecedent legislation is if a literal interpretation would lead to anomalies or absurdities, such that the legislation must be considered to be ambiguous.

108. The difficulty that Mr Yates and HMRC face is that it is not possible to ascertain a consistent and logical basis in the legislation for the taxation of dividends. Whilst there might have been some sort of logical underpinning to the basis of taxation of dividends in the early 1970's, when the partial imputation system was introduced (with ACT and tax credits) – any such logic had long disappeared as a result of the many amendments to dividend taxation in the period leading to the enactment of ITTOIA. Parliament has chosen to legislate for a system of great complexity, involving different tax rates, tax credits, deemed payments of tax, grossing up and various other matters. There are no logically consistent principles (as it were) underpinning the taxation of dividends, against which the result of a literal interpretation can be compared - in order to reach a judgment that a literal interpretation results in an anomaly or absurdity.

109. Mr Yates submits that (on Mr Shirley's interpretation) it is absurd that UK residents eligible under s399 should enjoy a lower effective tax rate than those entitled to a credit under s397 (as grossing-up under s399 applies only to non-residents). Mr Firth notes that HMRC's contention is not that UK and overseas dividends should be taxed equally, but rather that overseas dividends should be taxed at a much higher rate. Mr Firth submits that we have no basis for determining that one result is absurd and the other is not. Indeed, Mr Firth went on to say that the difference in the tax treatment of overseas and UK dividends arises from the fact that s399(3) only applies grossing-up to non-UK resident recipients, and that this is the a point in the legislation about which there can be no doubt of Parliament's intention.

110. In one sense, the interpretation sought by Mr Shirley is no more anomalous or absurd than any other interpretation – not least that sought by HMRC.

111. However, in our view, the interpretation sought by Mr Shirley is neither anomalous nor absurd. Given the complexity of the legislation and the absence of any logical underpinning, the only basis on which it can be applied is to take a literal approach to its interpretation.

112. As there is no real or substantial difficulty in interpreting the literal words of the statute, and as there is no ambiguity (even taking account of *O'Rourke*), we find that cannot consider antecedent legislation. For these reasons, we cannot give any weight to Mr Yate's submissions about the history of the provisions.

113. It may be that Parliament did not expressly and consciously intend to amend the law (and according to Mr Firth, Parliament, in any event did not amend the law), but we find that s399 is drafted in clear and unambiguous terms, and must be applied in accordance with those clear and unambiguous terms.

114. As the literal interpretation of s399 is consistent with the principles of EU law on freedom of movement of capital, we have not needed to consider the arguments of the parties on these issues.

115. Finally we note the 2 February 2011 article by Mr Shirley, and note that it is open to Mr Shirley to change his mind.

Determination

116. We allow the appeal.

117. 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.

NICHOLAS ALEKSANDER
TRIBUNAL JUDGE

RELEASE DATE: 11 November 2014

Amended pursuant to rule 37 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 on 21 November 2014

Cases referred to in the course of arguments:

Bank of England v Vigliano Bros [1891] AC 107
Shannon Realites v Ville de St Michael [1924] AC 185
IRC v Trustees of Joseph Reid (1949) 30 TC 431
IRC v Dowdall, O'Mahoney & Co Ltd [1952] AC 401
John Hudson and Co Ltd v Kirkness (1955) 36 TC 28
Kirkness (Inspector of Taxes) v John Hudson and Co Ltd [1855] AC 696
Jones v DPP [1962] AC 635
IRC v Luke (1963) 40 TC 630
Luke v IRC [1963] AC 557
Rae v Lazard Investment Co Ltd [1963] WLR 555
IRC v Joiner [1975] 1 WLR 1701
Farrell and anr v Alexander [1977] AC 59
Frankland v IRC [1997]STC 1450
Duport Steels Ltd and ors v Sirs and ors [1980] 1 All ER 529
WT Ramsey v IRC [1981] STC 174
Williams and Glyn's Bank Ltd v Boland [1981] AC 487
Garland v British Rail Engineering Ltd [1983] 2 AC 751
O'Rourke v Binks [1992] STC 703
Pepper (Inspector of Taxes) v Hart [1992] STC 898
Chevron UK Ltd v IRC [1995] STC 712
Peterbroeck Van Campenhout & Cie SCS v Belgium [1996] 1 CMLR 793
Inco Europe Ltd and ors v First Choice Distribution (a firm) and ors [2000] 1 WLR 586
Staarssecretaris Van Financien v Verkooijen C35-98 [2002] STC 654
Lenz v Finanzlandesdireektion fur Tirol C-315/02 [2004] ECR I-7063
Proceedings brought by Manninen C319-02 [2004] STC 1444
A and ors v Secretary of State for the Home Department (no 2) [2005] UKHL 71
Meilicke v Finanzant Bonn-Innenstadt C292-04 [2008] STC 2267
Damseaux v Belgium [2009] STC 2689
John Williams (Motor Engineers) Ltd v HMRC [2009] STC 2485
Barnetts (a firm) v HMRC [2010] UKFTT 286 (TC)
Chilcott and ors v HMRC [2011] STC 456
Haribo Lakritzen Hans Riegel BetriebsgmbH and anr v Finanzamt Linz [2011]STC 917
Meilicke v Finanzant Bonn-Innenstadt C262-09 [2013] STC 1494
Trustees of the BT Pension Scheme v HMRC [2013] STC 1781
Prudential Assurance Co Ltd v HMRC [2013] EWHC 3249 (Ch)
Eclipse Film Partners (No 35) LLP v HMRC [2013] UKUT 0639 (TCC)
Trustees of the BT Pension Scheme v HMRC [2014] EWCA Civ 23
Bristol and West plc v HMRC [2014] UKUT 0073 (TCC)