[2016] UKFTT 0145 (TC)

TC04930

Appeal number: TC/2015/02703

Entrepreneurs Relief – meaning of 'ordinary shares' – principles of statutory construction – TCGA 1992 s169S – ITA 2007 s989 – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

ALAN CASTLEDINE **Appellant**

- and -

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

TRIBUNAL: Judge Malachy Cornwell-Kelly
Mr Ian Menzies-Conacher FCA

Sitting in public at Fox Court, Brooke Street, London EC1 on 20 January 2016

Mr Jeremy Woolf instructed by Clarke Willmott LLP for the taxpayer

Mr Alan Hall of HM Revenue and Customs for the Crown

DECISION

1 This appeal concerns claims by Mr Alan Castledine for Entrepreneurs' Relief for the years 2011/12 and 2012/13 in respect of the disposal of loan notes in Dome Holdings Limited (DHL). The only issue is whether the test for eligibility for the relief stated in section 169S(3) of the Taxation of Chargeable Gains Act 1992 is met.

2 In addition to the usual documentary evidence, we received the sworn evidence of Mr Castledine. We find the following facts proved at least on the balance of probabilities.

Facts

3 The question to be resolved concerns the classification of the shares in DHL. At the material time, the shareholdings in that company were as follows:

	Issued	*Held by Mr Castledine*
'A' ordinary shares £1	1,895,482.00	94,775
'B' ordinary shares £0.01	20,019.85	1,001
Deferred shares £0.01	2,043.54	nil
Totals	1,917,545.39	95,776
£1 preference shares	165,088,062.00	6,785,137

4 If the deferred shares are counted as 'ordinary shares' Mr Castledine held 4.99% of the share capital of DHL; if the deferred shares are excluded from the reckoning, Mr Castledine held exactly 5% of the company's share capital. In the former case, Mr Castledine would not have qualified for the relief on a strict reading of the legislation; in the latter case, he would qualify, even on a strict reading. The question in this case then is: do the deferred shares count as 'ordinary share capital'?

5 A witness statement made by Mr Castledine indicates that he is the commercial director of Park Resorts Limited which was acquired by DHL in March 2007. Mr Castledine retired in September 2007 leaving loan notes in DHL under an existing financial structure. In Mr Castledine's absence however the business did not prosper and he was called back in December 2008 to assist in rescuing it from bankruptcy. The rescue was successful, but it included a restructuring of its finances in which Mr Castledine was allocated 5% of the ordinary shares, which he still holds. On 29 July 2011 and 31 July 2012, Mr Castledine disposed of loan notes in DHL worth £600,303 and £505,009 respectively, the disposals giving rise to the chargeable gains in respect of which relief is now sought.

6 The rights attaching to the deferred shares are prescribed by article 5.7 of DHL's Articles of Association. Under this article, the deferred shares have no voting rights and no rights to dividends: their sole value is in the right to be redeemed at par on a capital realisation after at least £1,000,000 has been distributed in respect of each B ordinary share. Given that there were at the material time 2,001,985 B shares in issue, the deferred shares had, according to Mr Castledine, in reality no rights.

7 Mr Castledine explained that the class of deferred shares was created as a mechanism for removing B ordinary shares from the senior management team of DHL, which had been awarded to them while they were working, when they left the company. This was done on legal advice that it avoided potential problems associated with other mechanisms for removing shares from shareholders, such as forcing them to sell back to the company. Under article 14.1-4, ordinary B shares are automatically converted into deferred shares in the case of four 'conversion events', namely the bankruptcy, death or leaving of employment of the holder or in certain circumstances in an insolvency; such converted shares are then automatically transferred to the Employee Benefit Trust for a nominal consideration.

8 Mr Castledine said that "the commercial objective was to find a way of removing the individuals as shareholders of the company, removing any influence over the running of DHL or receiving any financial benefit from the company"; the intention was, he said, "to strip the shares of economic value". Under this scheme, Mr Castledine himself could not hold deferred shares as he continued to be an employee of the company, though he was no longer a director of it. The notes to DHL's Consolidated Financial Statements and Directors' Report for the years to 31 March 2011, 2012 and 2013 all however show the deferred shares classed as 'ordinary shares'.

9 The rights of the various classes of shares, in what is a fairly complex and evolving structure, fit together as follows –

Share class	Voting rights	Income rights	Capital rights
Preference	None, save for matters affecting class	12% fixed and cumulative (=£19,810,567pa)	First call on assets, to repay at par plus any accrued dividends
A Ordinary	One vote per share, save in relation to any Key Change	Once Pref. shares are paid, may receive a dividend up to the Threshold Amount	Next call on assets, to pay up to the capped Threshold Amount
B Ordinary	One vote per share, in relation to any Key Change 80% in favour is required	None, unless or until the Investors have received Proceeds equal to the Threshold Amount	The balance of any remaining assets
Deferred	None	None	Redemption at par, but only once each B Ordinary has received a distribution of £1m
Investors		Threshold Amount	
means GIP Group, any holder of Initial Loan Notes from time to time, any holder of A Ordinary Shares from time to time, any holder of Preference Shares from time to time, any Affiliate of any of them and any transferee of any of them		means the greater of (i) the sum (if any) which it would be necessary to add to the Cash Flows as an amount received by the Investors as at the Reference Date so as to ensure that the IRR is at the Specified Rate and (ii) £0.01	

10 Whilst the structure is complex and the rights attaching to any class far from normal, the overall aim is clearly to create a hierarchy whereby the likelihood of receiving anything diminishes as one moves down the various classes of shares. The accounts show deficits on the Profit and Loss Reserves of £167,620,000 in 2010, £122,553,000 in 2011 (flattered by an exceptional write back of £68,050,000 due to a reclassification of the preference shares as equity and hence a write back of previously accrued dividends), £160,214,000 in 2012.

Legislation

11 Section 169S(3) and (5) of the Taxation of Chargeable Gains Act 1992 provides:

> (3) For the purposes of this Chapter "personal company", in reference to an individual, means a company –
> (a) at least 5% of the ordinary share capital of which is held by the individual, and
> (b) at least 5% of the voting rights in which are exercisable by the individual by virtue of that holding.
> . . .
> (5) In this Chapter –
> . . .
> "ordinary share capital has the same meaning as in the Income Tax Acts (see section 989 of ITA 2007).

12 Section 989 of the Income Tax Act 2007 contains the following definition:

> "ordinary share capital", in relation to a company, means all the company's issued share capital (however described), other than capital the holders of which have a right to a dividend at a fixed rate but have no other right to share in the company's profits.

Submissions

13 For the taxpayer, Mr Woolf submitted in essence that parliament would never have intended to categorise as ordinary shares holdings which had none of the characteristics of an ordinary share, or even of a preference share, and were shares only in name. Mr Woolf conceded that, at first sight, the terms of the two sections in question appeared straightforward and without ambiguity, but that it was well established that in applying any statute the court had to have regard to a number of canons of construction; it would not do to read the statutory provisions in a facile, superficial manner.

14 The first authority to which Mr Woolf took us was the decision of the Upper Tribunal in *Berry v RCC* [2011] STC 1057. Albeit that that case was concerned with tax avoidance, the essential purport of the tribunal's decision was that purposive construction remained appropriate to a taxing statute as much as to any other type of legislation.

15 Mr Woolf relied especially on the formulation by Lewison J at [31] of the various principles which emerged from the *Ramsay* line of authorities.

16 From this the propositions could be seen that: (i) the court must not infer a purpose in legislation without a proper foundation for doing so; (ii) the interpreter is not confined to a literal construction of the words; (iii) the interpreter is looking for the relevant fiscal concept; (iv) if parliament refers to a commercial concept it means to refer to one which is real rather than illusory; (v) the facts must be viewed realistically. Other considerations referred to in the same paragraph more closely related to tax avoidance schemes in particular.

17 The Court of Appeal's decision in *Pollen Estate Trustee Company Limited v RCC* [2013] STC 1479, which was not concerned with tax avoidance, reinforced this message. At [24] to [26] in particular the correct approach to construction was considered and the universality of it emphasised. It was reiterated that the interpreter was not confined to a literal interpretation of the words used, but must have regard to the context and scheme of the Act in question. That included a power to correct evident drafting errors and in particular to give effect to the legislator's clear intention. Thus paragraphs [26] and [49]:

> **[26]** This approach applies also to taxing statutes. In *Luke v IRC* [1963] 1 All ER 655 at 664, [1963] AC 557 at 577 Lord Reid said:
>
> 'To apply the words literally is to defeat the obvious intention of the legislation and to produce a wholly unreasonable result. To achieve the obvious intention and produce a reasonable result we must do some violence to the words. This is not a new problem, though our standard of drafting is such that it rarely emerges. The general principle is well settled. It is only where the words are absolutely incapable of a construction which will accord with the apparent intention of the provision and will avoid a wholly unreasonable result that the words of the enactment must prevail.'
>
> **[49]** Despite Ms Tipples's objections it seems to me there is a sufficient 'policy imperative' to justify the reading I favour. I believe that it is also consonant with the approach of Lord Nicholls in *Inco Europe Ltd v First Choice Distribution (a firm)* [2000] 2 All ER 109, [2000] 1 WLR 586. We are not parliamentary draftsmen; and it is sufficient that we can be confident of the gist or substance of the alteration, rather than its precise language. In substance what this means is that the exemption would apply as regards that proportion of the beneficial interest that is attributable to the undivided share held by the charity for qualifying charitable purposes. I do not see that this gives rise to any conceptual uncertainty or to any insuperable practical administrative problems. In my judgment this reading is necessary in order to give effect to what must have been Parliament's intention as regards the taxation of charities.
>
> There has been no principled reason advanced why a charity should be exempt from SDLT in the situations to which I have referred at [19], above but not be entitled to any relief at all on its proportionate undivided share in a jointly acquired property. Not to afford a charity relief in such circumstances would, in my judgment, be capricious.

18 In *O'Rourke (HMIT) v Binks* [1992] STC 703 the Court of Appeal had already endorsed such an approach, especially at 709 where Scott LJ, having referred to various authorities, said:

> The approach indicated in these passages justifies, in my judgment, implying into section 72(4) the natural limitation as to its scope that would correspond with the obvious intention of the legislature, namely, that the subsection should apply only to cases where the amount of the distribution was, in comparative terms, small.

19 The general principles were very recently affirmed yet again by the Court of Appeal in *Eclipse Film Partners No 35 LLP v RCC* [2015] STC 1429 where, at [110], the court made it clear that "There is no special rule for interpreting tax legislation"; that *Ramsay* had "marked the end of an unduly literal interpretative approach to tax statutes"; that "the new approach was to give the statutory provision a purposive interpretation in order to determine the nature of the transaction to which it was intended to apply"; and that this had "brought the interpretation of tax statutes into line with general principles of statutory interpretation and required notice to be taken of the reality of the transaction in issue".

20 The decision in *Collector of Stamp Revenue v Arrowtown Assets Limited* – a decision of the Court of Final Appeal of the Hong Kong Special Administrative Region on 4 December 2003 – was cited by Mr Woolf as persuasive authority, and of which it had not been suggested that the decision was incorrect. It was a tax avoidance case in which there was no question but that the scheme implemented had been devised with the sole purpose of exploiting a tax relief. It had been held, at [157], that:

> The words "issued share capital" in the section, properly construed, mean share capital issued for a commercial purpose and not merely to enable the taxpayer to claim that the requirements of the section have been complied with.

21 Although the case concerned a very plain tax avoidance scheme, Mr Woolf submitted that the principles applied were common to the other cases he had referred to in requiring the court to have regard both to the reality of the facts in question and to the obvious intention of the legislation.

22 In *BUPA Insurance Limited v RCC* [2014] SSTC 2615 the Upper Tribunal had enlarged at [65] – [69] upon on the observations of Lord Millett in *Arrowtown*:

> **[65]** As we have recorded above, Mr Bramwell advanced a submission that any transaction effected solely for tax avoidance purposes was to be ignored and as Bupa Finance had acquired shares in CX Re solely for tax avoidance purposes, the shareholding should be ignored. Mr Bramwell relied on the judgment of Lord Millett in *Arrowtown*.
>
> **[66]** We hope that we do not weary the reader by repeating that we do not consider that Mr Bramwell is entitled to make that submission. And we record that we are unclear as to whether Mr Bramwell's submission was in the alternative as to his other submissions as to why Bupa Finance's contractual obligation to pay Earn-Out Consideration to Tawa deprived Bupa Finance of a beneficial entitlement to distributions made by CX Re, or whether the finding of a sole tax avoidance purpose on the part of Bupa Finance was critical to his submissions to engage a purposive construction of s 403C at all. Neither did Mr Bramwell reconcile his submission to proposition (vii) (using our numbering) we

have set out in para [64], where Lewison J articulates the directly contrary proposition (see also *SPI* [2005] STC 15 , [2004] 1 WLR 3172 (para [26]) per Lord Nicholls). However, it is unsatisfactory to leave the matter in suspense and we consider it sensible to decide the point as a matter of law, as this case may go further.

[67] Put shortly, in *Arrowtown*, non-voting shares with no commercial content were issued by a company in order artificially to create a group, for stamp duty purposes. The non-voting shares were held not to constitute 'issued share capital'. Mr Bramwell relied on para [157] of Lord Millett's judgment, in which Lord Millett observed:

'[157] … The words "issued share capital" … properly construed, mean share capital issued for a commercial purpose and not merely to enable the taxpayer to claim that the requirements of [the provisions which confer stamp duty relief] have been complied with. It follows that the [shares] … are not "share capital" within the meaning of [the relevant provisions], and should be disregarded when calculating the proportions of the nominal share capital owned by [the respective shareholders].'

Thus, said Mr Bramwell, Lord Millett was deciding that shares issued solely for a tax avoidance purpose ('merely to enable the taxpayer to claim that the requirements of [the relieving section] have been complied with') were properly to be disregarded. We do not consider that Lord Millett decided this at all. In *Arrowtown*, shares were issued by one company to another artificially to create a stamp duty group but were effectively valueless. They had a right to dividends only in a year in which the net profits of the issuing company exceeded a sum larger than the gross national product of the USA and a right to a distribution on a winding up only after the holders of all of the other shares had received a distribution of HK$100,000 billion per share (see para [62] of Lord Millett's judgment). At para [151] of his judgment, Lord Millett identifies the question as:

'… not whether "share capital" is a legal or commercial concept, but whether share capital with the characteristics of the [relevant shares] **and** issued for the sole purpose of complying with the statutory formula were within the contemplation of the legislature …' (Emphasis added.)

At para [152], Lord Millett observed:

'The shares were created and issued in order to meet the qualifications for exemption from stamp duty … They had no other purpose … they had no commercial content at all. They carried no rights to dividends or capital on a winding up. If shares are considered as a bundle of rights, they had barely even a shadowy existence.'

And at para [155], Lord Millett observed that whether or not relief is available:

'… depends on whether the test is satisfied in circumstances contemplated by the section, that is to say where it can be said that the bodies are genuinely associated so that the transfer does not involve a significant change of ownership.'

[68] Lord Millett, in 'disregarding' the non-voting 'B' shares clearly did not do so on the sole ground that they were issued for the tax avoidance purpose (or no commercial purpose). Rather, Lord Millett expressly identifies their lack of 'commercial content' and, we consider, therefore identifies that they were only issued for tax avoidance reasons. But it is not the absence of commercial purpose (or the presence of the tax avoidance purpose) which led to Lord Millett

> disregarding the shares. Rather it was the lack of 'commercial content' which was, of course, informed by the absence of any commercial purpose. Indeed, it is difficult to see why, if Mr Bramwell's submission was correct, Lord Millett bothered to consider the 'commercial content' (or its absence) of the non-voting shares at all. And it would follow equally, on Mr Bramwell's submission, that shares issued for a tax avoidance reason with substantive rights (that is with more than 'shadowy' rights to dividends and rights on a winding up) would also be 'disregarded', for which we can discern no rational basis in principle or authority.
>
> **[69]** We therefore reject Mr Bramwell's proposition that transactions effected solely for tax avoidance purposes are properly to be disregarded for that reason alone, in construing tax statutes purposively.

23 In *Astall & Anor. v RCC* [2010] STC 137, the Court of Appeal, albeit in the context of a tax avoidance scheme, also found it appropriate to apply the wording of the statute having regard to the purpose of parliament in accordance with "the usual principles of statutory interpretation" and Arden LJ explained, at [44]:

> **[44]** Is a purposive interpretation of the relevant provisions possible in this case? In my judgment, there is nothing to indicate that the usual principles of statutory interpretation do not apply and accordingly the real question is how to apply those principles to the circumstances of this case. In my judgment, applying a purposive interpretation involves two distinct steps: first, identifying the purpose of the relevant provision. In doing this, the court should assume that the provision had some purpose and Parliament did not legislate without a purpose. But the purpose must be discernible from the statute: the court must not infer one without a proper foundation for doing so. The second stage is to consider whether the transaction against the actual facts which occurred fulfils the statutory conditions. This does not, as I see it, entitle the court to treat any transaction as having some nature which in law it did not have but it does entitles the court to assess it by reference to reality and not simply to its form.

24 A similar approach could be seen across the spectrum with the Court of Appeal in *Tower Hamlets LBC v Miah* [1992] 1 QB 622 addressing housing legislation. In that context, Neill LJ said at 629:

> Paragraphs 4 and 6 [of Schedule 1 to the Housing Act 1985] demonstrate to my mind that where the occupation of the dwelling house is to be on a short-term basis, the special status of a secure tenant is not conferred. The argument on behalf of the defendant involves the proposition that someone who occupies the house as a licensee from the local authority has a security which is not available to a tenant in precisely similar circumstances, though it is right to say that Mr. Seaward was prepared to accept that in a sense it is an illusory security because although as between himself and the local authority the licensee may be secure, if the head licence between the local authority and the owner is determined then the owner of the property can recover possession against the licensee - that is the homeless person - as a trespasser. That may be so, though I have an anxiety in my mind as to whether it is consistent with section 82 of the Housing Act 1985 for the local authority itself to determine such a licence and therefore bring to an end indirectly a secure tenancy or licence which it has itself created.
>
> But it is unnecessary to explore that matter. It seems to me that it is unsatisfactory, when one is considering the proper meaning of paragraph 6, to see whether there is some other way in which the matter can be dealt with. I find it

> impossible to accept that Parliament intended that a person who was a tenant might be prevented from becoming a secure tenant by reason of the provisions of paragraph 6, but that someone who held the lesser status of a licensee should remain a secure licensee. It seems to me that though the word "leased" is used, the exception in paragraph 6 must have been intended by Parliament to cover circumstances where, provided the other conditions in the paragraph are satisfied, the owner of the house has made it available to the local authority either under a lease or a licence agreement. As I see it, the word "leased" is used to indicate that the interest of the landlord local authority is to be a lesser interest than the freehold. But a leased dwelling house includes a dwelling house held under a lesser interest such as a licence.

25 Turning to other sources, Mr Woolf drew our attention to the definition of "shares" at section 540 of the Companies Act 2006 which said that the word "means share in the company's capital". Though that Act did not define "capital" the term was well enough understood as meaning the monies put up by the shareholders to establish and run a business. There therefore had to be some quantifiable sum of money related to each share whose existence would entitle the holder to certain rights – typically a share in profits, voting rights or at least rights to the return of capital in a solvent winding up.

26 In this case, the deferred shares, deliberately, did not entitle their holders to any of these rights: no profit share, no voting rights and an entirely illusory right to the return of capital. They were shares only in name. Preference shares, did have rights to share in profits but were excluded from the definition in section 989 of the 2007 Act, no doubt because they had much the nature of loan capital and were comparatively risk-free. An entrepreneur, by contrast was someone who took risks with his own money and the conditions for relief in section 169S reflected that: a requirement for a 5% holding in the ordinary share capital and 5% of the voting rights in that capital.

27 If the deferred shares were reckoned as ordinary shares, the obvious intention of parliament would be defeated by a technicality and it was inconceivable that, if the boot were to be on the other foot, the Revenue would not so contend. Mr Woolf referred to the description of what is meant by shares in the 25th edition of *Palmer's Company Law* at 6.001 to 6.043 and submitted that nothing equivalent to the deferred shares was mentioned.

28 The evident conclusion was that if parliament had adverted to the possibility of instruments like the deferred shares here they would have been excluded from the definition of ordinary share capital. Parliamentary legislation could not provide for every possibility and the legislature was entitled to rely on the courts to interpret it in accordance with the accepted practice shown by the cases.

29 For the Crown, Mr Hall submitted that the legislation was perfectly straightforward, was not ambiguous, and did not produce a result which was at odds with an intention parliament must have had, but defined an easily applied dividing line giving rise to no uncertainty. There was no need, and no justification, for the tribunal to go beyond the plain words of the statute.

30 Expanding on this argument, Mr Hall submitted that the only intention which could properly be attributed to parliament was an intention to establish a dividing line for eligibility for the relief; the nature of dividing lines was that they had to be clear and predictable and, necessarily, they would create hard cases close to the line. The specifics of shares issued by companies being almost infinitely variable, reflecting the commercial circumstances in which they are issued, it would be impossibly complicated for a definition to seek to provide for them all; parliament had therefore chosen a simple and unmistakeable test which leaving no room for uncertainty.

31 Mr Hall relied on the warning given by Lord Hoffman in the *British Tax Review* that "It is one thing to give a statute a purposive construction. It is another to rectify the terms of highly prescriptive legislation to include provisions which might have been included but are not actually there"; [2005] BTR 197 and cited with approval by Lewison J in *Berry* at [31]. It would be possible to cite other definitions of ordinary shares, for example that in section 560(1) of the Companies Act 2006, but a different definition had been used here and the tribunal should not interfere with it.

32 Mr Hall traced the origins of the section 989 definition back to section 42(3) of the Finance Act 1938 where it appeared in very similar, if not identical, terms. Surprisingly, no authority could be found bearing on this wording in spite of its long use. The conclusion Mr Hall invited us to draw from this was that the plain meaning of the words had never been contested and that a gloss on them was thus the less likely to be appropriate after all this time.

33 Within the definition of "personal company" in section 169S, there were two distinct limbs, each of which had to be satisfied for the relief to be available. Thus, limb (a) focussed on the size of the individual's holding, prescribing an exact figure to be met. The requirement was that the holding had to be "at least" 5% of the ordinary share capital – not "almost" 5% or "approximately" 5%. Limb (b) of the test by contrast focussed on a necessary characteristic of the shares at issue, namely that they should also carry "at least" 5% of the voting rights in the ordinary share capital. No basis for the application of the *de minimis* rule was therefore present – nor did it fall within the Revenue's Statement of Practice 15 on the 'rounding' of figures generally.

34 Beside the views of Lord Hoffman in the British Tax Review, another non-binding source of authority was cited by Mr Hall, namely the seventh edition of *Bramwell on the Taxation of Companies* where it was said at 21-09 that "Shares which carry no dividend rights at all also constitute ordinary share capital" – though Mr Woolf pointed out that this opinion did not appear in the current edition of the work.

35 Turning to the case law, Mr Hall took us first to the observations of Lightman J in *Spectros International Plc Madden (HMIT)* [1997] STC 114 at 136, where the learned judge adverts to the approach adopted by the courts with regard the interpretation of the term used by the parties to a transaction. Recalling that the law respects the freedom of the parties to a transaction to frame and formulate their agreement as they wish, the judge continues:

> ". . . so long as the form adopted is genuine, and not a sham, honest and not a fraud on someone else, and does not contravene some established principle of public policy, the court will give effect to the method adopted. [. . .] If the terms of the document are clear, that is the end of the question.

36 This, said Mr Hall, is pertinent to the provisions of article 14 under which ordinary B shares are automatically converted into deferred shares on the happening of certain events. That is what the company had chosen to do, to convert one type of ordinary share to another, and that choice and manner of doing it must be respected. Mr Castledine had made it clear that the objective of this mechanism was commercial and there was no basis for interfering with a commercial decision freely taken by the parties. The notes to the accounts for three consecutive years were consistent with this understanding of the status of the deferred shares as ordinary shares. A leading firm of chartered accountants, with a statutory obligation to state the position correctly, had put their name to this.

37 In *Arrowtown* the court had found that the shares at issue had been created artificially and it had been admitted by the parties that they had no commercial purpose, which distinguished the case entirely from the present where the deferred shares existed for an avowedly commercial reason. *O'Rourke* was a case in which words had been read into the statute by the Court of Appeal in the context of what was there considered to be an ambiguity but, again, it was distinguishable from the present case where the statutory wording contained no ambiguity and could not have been plainer.

38 *Astall* was, like *Arrowtown*, a tax avoidance case in which the Court of Appeal had sought to give the statute a purposive construction and to disregard what it described at [34] as "peripheral steps inserted by the actors that are in fact irrelevant to the way the scheme was intended to operate", a situation wholly different from the genuine and commercially motivated existence of the deferred shares. The court's closing words at [60] were in point: "It is emphatically not [the court's] function through purposive interpretation to fill in gaps in the legislation". There was no question of there being a gap in either of the sections relevant.

39 In the Upper Tribunal's decision in *BUPA*, Mr Hall relied on the reordered summary of the *Ramsay* line of authorities at [64], points (vi) and (vii):

> (vi) 'However, the more comprehensively parliament sets out the scope of a statutory provision or description, the less room there will be for an appeal to a purpose which is not the literal meaning of the words.'
>
> (vii) 'A provision granting relief from tax is generally (though not universally) to be taken to refer to transactions undertaken for a commercial purpose and not solely for the purpose of complying with the requirements of tax relief . . . However, even if a transaction is carried out in order to avoid tax it may still be one that answers the statutory description . . . In other words, tax avoidance schemes sometimes work.'

The decision, at [68], also clarified that what Lord Millett had been referring to in *Arrowtown* was 'commercial content' rather than 'commercial purpose'.

40 Following Lord Millett's reasoning in that case, the important factor here was therefore that the division of the shareholdings in DHL reflected the commercial needs of the company and should not therefore be set aside as artificial or meaningless. The comments by Lord Millett at [55] and [56] of *Arrowtown* made it clear that that case was concerned with the complete absence of commerciality in the situation.

41 Finally, the discussion in *Pollen* by the Court of Appeal concerning the construction of the provisions for charities relief from stamp duty land tax did not assist the taxpayer. There, again, the question of purposive construction had been in issue and Mr Hall relied on the observations of Lord Nichols, quoted at [25]:

> 'It has long been established that the role of the courts in construing legislation is not confined to resolving ambiguities in statutory language. The court must be able to correct obvious drafting errors. In suitable cases, in discharging its interpretative function the court will add words, or omit words or substitute words … This power is confined to plain cases of drafting mistakes. The courts are ever mindful that their constitutional role in this field is interpretative. They must abstain from any course which might have the appearance of judicial legislation. A statute is expressed in language approved and enacted by the legislature. So the courts exercise considerable caution before adding or omitting or substituting words. Before interpreting a statute in this way the court must be abundantly sure of three matters: (1) the intended purpose of the statute or provision in question; (2) that by inadvertence the draftsman and Parliament failed to give effect to that purpose in the provision in question; and (3) the substance of the provision Parliament would have made, although not necessarily the precise words Parliament would have used, had the error in the Bill been noticed. The third of these conditions is of crucial importance. Otherwise any attempt to determine the meaning of the enactment would cross the boundary between construction and legislation …'

42 The tribunal, submitted Mr Hall, could not be "abundantly sure" of the three matters which Lord Nichols had considered crucially important to be present before a departure from the strict words of the statute could be justified. There was no evidence here of parliament's purpose other than the obvious and very general intention to create a relief: the terms in which it had chosen to establish the relief were plain enough, and to add anything else would in effect be to legislate where parliament had chosen not to.

Conclusions

43 The arguments put to us seem quite evenly balanced and we are conscious indeed that a first instance jurisdiction must be "absolutely sure" of its ground as it ventures into the territory of statutory interpretation, especially where, as Mr Hall submitted, the statutory language is apparently categorical and without ambiguity.

44 In the first place, the definition at issue in section 989 of the 2007 Act can hardly be said to be characterised by an 'error', which has lain undiscovered since 1938 – its long and unchallenged existence suggests indeed the contrary. And, as though to reinforce this concern, the intention that the definition should be taken as broad and comprehensive appears to be emphasised by the words in parenthesis 'however described'.

45 It would appear that parliament is here making it clear that there are to be no fine distinctions or special exceptions in the matter; that a simple, broad brush, easily workable, approach is mandated. Moreover, there is no explicit evidence of parliamentary intention relevant to the point we have to decide; and it is questionable whether even if there had been such evidence in the form, for example, of Notes on Clauses or extracts from Hansard, it would have been proper for the tribunal to take it into account.

46 An argument based on the second of Lord Nichols's criteria – inadvertence on the part of the draftsman – must likewise face the objection that there is nothing on the face of the legislation to suggest that, in consciously adopting a long-established definition for the purposes of entrepreneur's relief, parliament's action was 'inadvertent'.

47 To these considerations must also be added the further objection that the creation of the class of deferred shares was openly commercial, and perfectly genuine. There can be no serious suggestion that article 14 of DHL's Articles of Association was a fraud on any person or class of persons, or otherwise a falsity of some kind. On the contrary, it has all the appearance of being a carefully devised means of ensuring the wellbeing of the company in the case of share-incentivised employees ceasing to play a part in it, or indeed becoming its rivals after they have left.

48 Why should such a proper and lawful measure be found at odds with a presumed intention of parliament? Would not the gloss for which Mr Woolf contends fall foul of the warnings we have seen against judicial legislation? And, above all, would the application of the legislation in its plain meaning really lead to a result which cannot have been intended, or which is absurd or unreasonable? What is wrong with a fiscal statute defining matters in terms which are apt to make for straightforward administration, and to offer taxpayers the maximum of certainty?

49 It is, perhaps, almost in the nature of tax legislation to create anomalies and hard cases, and it is not the function of the courts to exercise a supervision over the doings of the legislature to ensure that they are undertaken with respect for general concepts of one kind or another. Considerations of human rights and European Community law apart, parliament has an absolute discretion in the areas in which it intervenes and its dictates must be followed.

50 The authorities to which Mr Woolf has drawn attention, however, do require that whatever provisions parliament has enacted must be interpreted according to certain criteria. The first of these is that no difference is to be made between the construction of fiscal statutes and statutes dealing with other areas of the law. And a close corollary of this is that the same approach applies whether the case involves an avowed tax avoidance scheme or not. This much is apparent from most of the cases which have been cited, but if specific authority is wanted it may be found in the statements of the Court of Appeal in the very recent case of *Eclipse Film Partners* mentioned at [19] above.

51 Over 20 years previously that court had already, in *O'Rourke*, sought to give effect to what it saw as the obvious intention of the legislature, and the same approach has repeatedly been the rationale of the decisions in every other case which Mr Woolf has cited. In 2013, the same court cited with approval the words of Lord Reid in the 1963 case of *Luke v IRC* that-

> The general principle is well settled. It is only where the words are absolutely incapable of a construction which will accord with the apparent intention of the provision and will avoid a wholly unreasonable result that the words of the enactment must prevail.

52 Lord Reid had referred in that case to "the obvious intention of the legislation" and to a literal reading of it producing "a wholly unreasonable result" defeating that intention. In the present case, it could be argued that parliament's definition of a person entitled to entrepreneur's relief envisages someone who has, as it were, a full-bodied risk stake in the company in question: 5% of the ordinary share capital and 5% of the voting rights relating to it. Preference shares are excluded.

53 The policy here could be that an entrepreneur is a risk-taker rather than an investor, while the holder of preference shares tends more to the latter category; the relief would then be seen as encouraging and stimulating entrepreneurship as distinct from secure, or relatively secure, investment. And it is notable moreover that, in defining the characteristics of an entrepreneur for this purpose, the legislation has focused on voting rights and participation in the equity of a company.

54 As we have noted, however, there has been no specific evidence before the tribunal to support the suggestion that parliament intended more than the legislation stated, and to place weight on these speculations means introducing to the statutory definition a layer of meaning which is not apparent at first reading; it also risks producing an unwelcome degree of uncertainty, with the all administrative problems which could follow. In wording which has been used for so long, without it appears any need for the addition of refinements to its meaning, we have hesitated to venture into these areas of potential difficulty.

55 It may indeed be that the logic of the clear cut distinction implied by the 'all in, unless specifically out' approach of the legislation is that debt-like instruments are to be excluded, but to include instruments which bear some risk of no return. In that case, there would be little difficulty in viewing the way that the shareholdings of DHL have been structured consistently with such an understanding. Looking at the situation in the round must imply more than a narrow focus on those B ordinary shares that happen already to have been converted into deferred shares, and must require seeing the share structure overall in its commercial context. And in that context, it is clear that the different classes of shares are in fact integrated parts of a complex financial engineering package to allocate risk and reward between various parties.

56 So we return to the underlying question: can parliament have intended that shares such as the deferred shares in this case should be reckoned as part of the ordinary share capital of the company?

57 Mr Woolf can point to the apparent absurdity of shares with no rights at all to participate in the profits of the company, with no voting rights, and with the right to return of capital only when £20,001,985,000,000 is distributed in respect of the B shares – which makes the case of the deferred shares here nearly identical with that of the shares held in *Arrowtown*.

58 But, as we have noted, DHL's accounts showed deficits on the Profit and Loss reserves of £167,620,000 in 2010, £122,553,000 in 2011 (flattered by an exceptional write back of £68,050,000 due to a reclassification of the preference shares as equity and hence a write back of previously accrued dividends), £160,214,000 in 2012. This, on an 'economic reality' test, suggests that the A and B ordinary shares are no more likely to get any return of any sort than the deferred shares, because they are swamped by the preference shares. In that perspective, it is difficult to see the deferred shares as quite so exceptional and Mr Woolf would have it.

59 The concern expressed by Lord Reid was that the interpreter of a statute should not be required "to apply words literally [and] to defeat the obvious intention of the legislation and to produce a wholly unreasonable result". Applying this legislation in accordance with its plain meaning, however, does not in our view produce such a result, either in this case or in general. The value of shares in a limited company may be affected by a multiplicity of factors, some emerging from legal constraints and some relating to commercial circumstances, so that it would not be surprising if parliament had decided not to address possibilities so many and so various, but to draw a simple, clear and predictable distinction.

60 The concern expressed by the Court of Appeal in *Eclipse* about an unduly literal interpretative approach to tax statutes, and the need to give a statutory provision a purposive interpretation in order to determine the nature of the transaction to which it was intended to apply, does not seem to us to point towards an open-ended speculation as to where parliament intended to draw the line with regard to the meaning of 'ordinary share capital'. The reason for this conclusion is that the arguments so persuasively advanced by Mr Woolf on the facts of the present case will not suffice to establish an interpretation of the statute which could be applied generally, without the need for a particular investigation in every instance of the value, or lack of it, of ordinary shares which are *prima facie* within the definition.

61 Bearing in mind the explicit warnings by Lord Nichols in *Pollen* against judicial legislation, we do not feel able to depart from the plain meaning of the legislation at issue. We accordingly conclude that the deferred shares in this case do fall within the meaning of 'ordinary share capital' in section 989 of the Income Tax Act 2007 as applied to entrepreneur's relief, and that appeal therefore does not succeed.

Appeal rights

62 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.

63 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.

MALACHY CORNWELL- KELLY
TRIBUNAL JUDGE

RELEASE DATE: 1 MARCH 2016