TRANSFER OF ASSETS ABROAD - whether defence in TA 1988 s.741 applies - whether test is subjec objective - subjective - formation of Bermuda holding company - whether bona fide commercial tran designed for tax avoidance - whether various transactions are associated operations - whether an in be the transferor of assets made by another individual - appeal allowed - TA 1988 s.739, 741

THE SPECIAL COMMISSIONERS

RORY KERR CARVILL

Appellant

- and -

THE COMMISSIONERS OF INLAND REVENUE

Respondents

Special Commissioner: DR J F AVERY JONES CBE

Sitting in public in London on 8, 9, 10, 11, 12, 15, 16, 17, 18, 19 November 1999, 2, 3, 4 February

Miss E Gloster QC and Mr G Goodfellow of Counsel instructed by Slaughter and May for the Appellan

Mr P Vallance QC and Mr R Singh of Counsel instructed by the Solicitor of Inland Revenue for the Re

DECISION

Introduction

1. This is an appeal by Mr R C Carvill against assessments made under section 739 of the Taxes the years 1993/94 to 1995/96. There have been previous proceedings in 1994 before a Spec Commissioner (Mr Everett) relating to the same issue for the years 1987/88 to 1992/93, whi decided in favour of the Crown. Following those proceedings the Appellant applied to the cou number of amendments to be made to the case stated, which the court declined to make. Th are reported at [1996] STC 126. In consequence, the Appellant abandoned any appeal from decision. Although this appeal covers the same ground as the earlier one, I have had the ben two ring binders of additional documents which have been found since the earlier hearing an

heard several additional witnesses.

2. I shall use the following abbreviations: International Holdings: R K Carvill (International Holdings) Holdings: R K Carvill (Holdings) Limited; International: R K Carvill (International) Limited; Limited Co Limited; Inc: R K Carvill Inc; Personal Services: R K C Personal Services Limited.

3. I had evidence in the form of witness statements from the Appellant, Mr Keith Tuson, the Appellan companies' tax adviser, Mr Peter Kirby, joint managing director of Limited, Mr Kenneth Copelston, director of Limited, Mr Thomas Hearn, former President of G L Hodson & Sons and later a director International Holdings, Mr Robin Jackson, Lloyd's underwriter, Mr Raymond Salter, Lloyd's reinsur Mr Donald Koziol Jr, director of Inc, Mr Robin Spencer-Arscott, from the Bermuda insurance indus except for Mr Copleston, Mr Koziol and Mr Spencer-Arscott gave oral evidence. The Revenue calle witnesses, Mr John Stoker and Mr Roy Harris who gave oral evidence.

4. The documentary evidence consisted of 12 ring binders.

5. In brief, in 1982 the Appellant transferred his 59% shareholding in Holdings, a UK resident compa International Holdings, a company resident in Bermuda. The issue in this appeal is the liability of to tax under section 739 of the Taxes Act 1988 on dividends paid by Holdings to International Hol years under appeal, and in particular, whether the defence in section 741 applies.

Reinsurance broking and the Appellant's commercial strategy

6. I shall start by setting out my understanding of how, in broad outline, the Appellant and his c operated. The operating companies are reinsurance brokers and Limited is a Lloyd's reinsura specialising in the US market. The particular business on which it concentrates is treaty exce reinsurance, that is to say reinsurance of losses over a limit, rather than a proportion of the (quota share), on the casualty side i.e. dealing with claims like medical negligence rather tha physical damage. An insurance company in the US will approach a US reinsurance broker to which it has taken on by writing insurance policies. A proportion of the risks will be reinsured US, principally at the time at Lloyd's but also with European reinsurers. The US reinsurance b approach a Lloyd's reinsurance broker such as Limited to place a proportion of the risks at Ll elsewhere outside the US. Limited therefore obtained its business from US reinsurance broke producing side of its business) and used its expertise in placing the risks at Lloyd's and elsew Europe (the placing side of its business). The reinsurance business is a people business which building up of a relationship with the US broker being able to reinsure their risks, and also bu relationship of trust with the underwriters as a person who does not mislead the underwriter risk. It is obvious that Limited was completely dependent on US reinsurance brokers for its b

7. The Appellant's business strategy was to put his companies in a position to compete for the entire business of the US insurance company. This involved not only being in a position to compete with reinsurance brokers on the production side, but also on the US placing side, since, if they took ov business previously carried on by the US reinsurance brokers, they would need to be able to place the reinsurance in the US as well as the half in the UK and Europe which they were already doing. was a dangerous process because at the beginning their entire business came from a small tight c US reinsurance brokers. The Appellant and his companies wanted to be in a position to compete w reinsurance broker which was part of an organisation that linked up with a UK reinsurance broker that in future it sent all its Lloyd's reinsurance business to its UK affiliate. At the same time they a continue to receive business from the other independent US reinsurance brokers. If these US rein brokers thought that the Appellant's companies were putting themselves in a position to compete footing with the US reinsurance brokers, the Appellant's companies would be in danger of losing t immediately. The danger was not only in the US. Rival UK reinsurance brokers were also keen to s in the hope of getting business for themselves. A necessary part of the strategy consisted of getti US insurance companies so that, if the US reinsurance broker merged with a UK broker, Limited w position to go to the US client insurance company and compete for the business. While there was whom the Appellant could not afford to upset, this was difficult. A further difficulty was that the ab risks in the US required a US presence, but this would be construed by the US reinsurance broker indication that they were preparing to compete. The Appellant's group was the only reinsurance b

attempt this strategy. It was described by Mr R A G Jackson, a Lloyd's underwriter who wrote a lo for the Appellant as a very risky venture. He also regarded the strategy as risky to himself becaus have lost the underwriting business if the Appellant had not succeeded.

8. In commercial terms, if the strategy succeeded the benefit was that the Appellant's companies wo entire brokerage (15 per cent of the reinsurance premium), rather than the one-third of the broke Limited obtained (the US reinsurance broker customarily taking two-thirds). Limited's one-third re reinsurance placed in London, which was about half the risk, so that Limited received about 2.5 pe the reinsurance premium of 15 per cent paid by the US insurance company. If the strategy failed, Appellant's companies would lose their business, either immediately, if they upset the US reinsura or in the longer term, if the US reinsurance broker merged with a UK reinsurance broker which wo receive all the US broker's business.

Whether the test in section 741 is subjective or objective

9. The Appellant's case is that it is accepted that section 739 applies in one respect although the contend that there are other relevant transfers and associated operations, which I shall deal The Appellant contends, however, that the defence in section 741 applies. I shall look at whe in section 741 is subjective or objective as an initial question since it will determine what fact relevant. This section provides:

"Sections 739 and 740 shall not apply if the individual shows in writing or otherwise to the satisfacti Board either—

(a) that the purpose of avoiding liability to taxation was not the purpose or one of the purposes for v transfer or associated operation or any of them were effected; or

(b) that the transfer and any associated operation were bona fide commercial transactions and were for the purpose of avoiding liability to taxation."

10. Miss Elizabeth Gloster QC for the Appellant submits that section 741 imposes a subjective tes in the Appellant's mind in carrying out the relevant transactions. Mr Philip Vallance QC for the contends that the test is an objective one, relying on the following passage in Lord Nolan's sp Willoughby v IRC 70 TC 57 at page 116E-G:

"Where the taxpayer's chosen course is seen upon examination to involve tax avoidance (as oppose mitigation), it follows that tax avoidance must be at least one of the taxpayer's purposes in adopting whether or not the taxpayer has formed the subjective motive of avoiding tax." (my italics)

11. This statement seems, with respect, hard to fit with Lord Nolan's definition of tax avoidance: avoidance within the meaning of Section 741 is a course of action designed to conflict with or evident intention of Parliament" (at p.117A). One would expect that evidence of the designer of action was relevant. Lord Nolan in the passage quoted may have been merely summarising Revenue's contentions. The paragraph from which it is taken begins: "In order to understand drawn, submitted Mr Henderson [counsel for the Crown], it was essential to understand what by 'tax avoidance' for the purposes of section 741." The passage quoted above may have bee the Revenue's argument. It certainly does not fit with Lord Nolan's summarising the findings in the taxpayer's mind only two paragraphs earlier (at p.116A-C). The issue in Willoughby wa Special Commissioner was correct in law in applying a subjective test.

12. My reasons for preferring Miss Gloster's contention that the test is subjective are first that this is s authority, including Herdman v IRC 45 TC 364 at 405, Philippi v IRC 47 TC 75 at 111, 112 (dealin infirm taxpayer could provide evidence of his purpose) and IRC v Pratt 57 TC 1 at 49D ("a person sought to avoid liability to income tax"). There are also numerous dicta supporting a subjective te Vestey v IRC 54 TC 503 at 583H-584B, 585A-B, 589F-590B, 601A-D, 602F-G, and I am not aware before Willoughby in which there is any suggestion of the test being objective. Secondly, the ordi

of a purpose test is that it is subjective. If it is not subjective it is hard to understand why Parliam have defined in section 739 that the individual is taxed if he has the necessary power to enjoy the non-resident (assuming that the terms of the section are otherwise satisfied), and then said in sec that did not apply if the individual did not have the purpose of avoiding tax. It would have been si that section 739 applied if the circumstances were such that the individual avoided tax (section 7 example of such an approach). In many cases it may be obvious why a taxpayer does something concerned with the creation of a Bermuda holding company and in order to know whether this is c conflicting with the evident intention of Parliament one needs to know why the taxpayer set it up. subjective test I am following the same approach as this tribunal in Beneficiary v IRC [1999] STC should also record that Miss Gloster referred to Hansard in 1938 to show that the Solicitor-Genera Parliament that the test was subjective. Although this was not objected to by Mr Vallance I do not ambiguity in the section which would entitle me to rely on Hansard.

13. I propose therefore to approach this case by determining what was the purpose in the Appellant's directors' minds in carrying out a particular transaction. Any other approach seems impossible to circumstances of this case.

Facts

14. Before setting up on his own, the Appellant worked for C T Bowring & Co Limited (Bowrings) 1967 in their US reinsurance side dealing mainly with the six largest US reinsurance brokers. worked in Seattle from 1967 to 1969 for John F Sullivan & Company, then the fourth or fifth reinsurance broker, in the casualty market in the US, during which he acquired his knowledg market and, more importantly, met their client insurance companies. He then returned to Bo became a senior director on the North American side. He foresaw that Bowings were likely to by Marsh McLennan which would mean that, while Bowrings would be the recipient of all the McLennan group US business, including the reinsurance business of Guy Carpenter, the reins owned by Marsh McLennan, other US reinsurance brokers would no longer do business with B they were part of a rival US reinsurance broker. The opportunity for selling their services to c reinsurance brokers would therefore become negligible.

Limited and Holdings

15. The Appellant decided to set up on his own with two colleagues from Bowrings, Mr Copplesto Innocenti, and they formed Limited in March 1977, starting business in that company after th period expired on 21 April 1977. Holdings took over Limited on a share exchange in July 197 Americans mainly from John F Sullivan & Co, including Mr Jack Sullivan and Mr Gerry Sullivan small investment in Holdings. The business started slowly, partly because it took them two y become Lloyd's brokers owing to objections made by Bowrings. The Appellant was earning le had done at Bowrings. In the first accounting period of the 16 months to 30 June 1978 he ea and the group made a loss of £28,391. In fact, the Marsh McLennan-Bowrings merger did no 1979, but the Appellant's prediction about the market was correct. As a result of the merger, business from 30 to 40 US brokers was lost to Bowrings, and Limited managed to acquire so large matter came to Limited from G J Sullivan and Associates, the Californian Hospital Assoc

16. It was also clear to the Appellant that other such mergers could take place in which case Limited business of the US reinsurance brokers that acquired a UK affiliate, i.e. that the US reinsurance br merged with a UK reinsurance broker would no longer send business to Limited but would channe business to their UK associate. There would be exceptions if the US insurance company insisted th reinsurance broker continued to use Limited, but in the long term, it was likely that all the busines up with the UK associate of the US reinsurance broker. US reinsurance brokers actually tried to ac Appellant's companies threatening that if he did not sell they would divert all the business to a UK the Appellant wished to remain independent. There were a small number of US reinsurance broke one of the witnesses, Mr Hearn (former President of G L Hodson & Son), as a tight, small commun or so specialist firms. Most of them, perhaps ten, dealt with Limited, and if they all merged with U Limited would have no business. In fact, mergers of all the main US reinsurance brokers later took 1982 about 85 per cent of the Appellant's business came from the main US reinsurance brokers; t

than 3 per cent.

International

17. The first Bermudan company set up by the Appellant was International in which the Appellan cent of the shares and Holdings the remaining 49 per cent. Originally Holdings had acquired a and retrospective consent was obtained under section 482 of the Taxes Act 1970 for 51 per c transferred to the Appellant. International was formed in 1980 to enter into the Californian H Association contract because the US reinsurance broker, G J Sullivan and Associates, who ha business from Bowrings to limited, were reluctant for Limited to take the whole brokerage im when the work might have to be done over the next 10 or more years and there was no certa Limited, a new company, would be there in 10 years' time. The reason why it was necessary continue to handle the business in the future was that all communications relating to the rein will have been placed in many different markets go through the reinsurance broker.

18. About this time, the Appellant and the other directors of Limited were considering their future stra decided in some way to move the strategic centre of their operations to Bermuda.

19. On 11 January 1982 Neville Russell, Limited's auditors and the Appellant's accountants, sent the R domicile questionnaire which had been signed by the Appellant on 15 December 1981 asking the I confirmation that the Appellant was domiciled in Ireland. There was no evidence about what was t making this application. The Revenue asked some further questions in connection with the applica March 1982 which Neville Russell answered on 22 June 1982. The Revenue confirmed their accept Appellant's non-domiciled status on 2 September 1982.

Engagement of Mr Tuson

20. On 29 January 1982 Limited placed an advertisement in the Financial Times for a corporate t consultant stating " We are looking for a specialist to advise on UK and international tax matt develop long-term strategy in this area….Applicants must show the ability to provide construc advice and implement their proposals…." Mr Keith Tuson, who was then Group Taxation Mana Samuel Group plc, applied for the post and following two interviews, the second of which incl interview with the Appellant, started on a part-time basis of about one late afternoon and ea say three hours, a week from 1 April 1982. From September 1982 he set up on his own with main client. He started acting for the Appellant personally as well as Limited in October 1982

21. There is an unsigned board minute of Holdings of 5 July 1982 at which it is stated that Mr Tuson p paper which suggested that a new international holding company should take control of Holdings w considered. It was resolved to make clearance applications under sections 464 and 482 of the Tax and section 88 of the Capital Gains Tax Act 1979. No copy of this paper has been found and Mr Tu considered that it consisted of his speaking notes. Mr Tuson prepared a memorandum on 12 July s possible tax strategy and suggesting Bermuda as the location for a new holding company (Interna Holdings). He was under the impression at the time of writing this paper that the group's purpose money box company overseas out of which investments could be made from dividends received fr subsidiaries, rather than the active holding company which occurred, and which distributed divide Appellant much later. It was not the Appellant's intention to have a money box company and the understanding seems to have been caused by Mr Tuson being new to the job. The memorandum c following passage:

"Although the objective of the revised structure would be to enable profits to be earned free of tax o free of UK tax, it is not essential that the ultimate holding company should itself be based in a tax h conceivable that the ultimate holding company could itself be based in a "respectable" tax jurisdictio not tax foreign income and that the profit making activities could be established under a tax haven c Although there are a number of respectable locations which would be suitable, none has any logical justification…I suggest that we proceed on the basis that Bermuda would be the location for Interna Holdings."

22. Mr Tuson sent this memorandum to Neville Russell on 14 July 1982 and had a meeting with t July. Further drafts of the clearance applications were sent by Mr Tuson to Neville Russell on saying that he hoped to submit them in two weeks time. There is a file note that they met or and amongst the points made was whether the Appellant's "possible non-domicile status" sho mentioned in the applications, which shows that the Revenue's domicile letter of 2 Septembe reached Mr Ingmire, the corporate tax partner in Neville Russell, although it had presumably received by the partner responsible for the Appellant's personal affairs. The clearance applica made on 9 September 1982. The applications contain the following commercial reasons:

"In view of these factors [the factors referred to included that the company was increasingly involve business from the US, and the risk of losing its business through associations between US and UK br considered that in order to create further opportunities for the growth of the Group as a whole and o Company's [Limited's] business in particular, the Group should become more directly involved in the of business in the United States. However, given the existing connections which [Limited] has with U and the severely detrimental effect which a precipitate breaking of those links would have on [Limite the Group cannot openly and directly establish a U.S. broking activity in competition with existing br

It is proposed, therefore, that to overcome this problem while still achieving the desired result, Inter Holdings should be formed and located in Bermuda and should issue its shares in exchange for the e in Holdings. From its base in Bermuda, International Holdings would then be able to procure in the U business for [Limited] without being seen to compete with established U.S. brokers."

23. Clearances were duly received on 23, 27 and 30 September 1982.

24. A letter was sent to Lloyd's on 2 August 1982 asking for their approval for Holdings to be owned b Holdings. It was also proposed that International should be owned by International Holdings. Lloy they had no objections on 11 August 1982.

Formation of International Holdings

25. An initial approach was made to Conyers Dill and Perman, the Bermuda lawyers, on 6 Octobe formation of International Holdings in Bermuda which was incorporated on 10 December 198 same day, it was resolved to carry out a share exchange issuing shares in International Holdi exchange for the shares in Holdings held by the Appellant (the Old Majority Shares) and the (the Old Minority Shares), the shares in International Holdings being referred to as the New M New Minority Shares respectively. At the same time the Appellant bought the shares of the U shareholders in Holdings, giving him 59 per cent of the equity and 63 per cent of the votes. T was completed on 4 January 1983. The decision to transfer their shares was a collective one discussion with some of the shareholders needing to be convinced of the merits of the reorga the Appellant said in his witness statement: "I had a lot of persuading to do on this, because undertaking and, of course, I had no legal right to compel anyone to exchange their shares, decision that we took to go to Bermuda was agreed by all and the exchange of shares really thereafter."

26. On 29 December 1982 Limited entered into a brokerage sharing agreement by which Internationa entitled to one-third of the brokerage. In relation to business specified in the schedule, which inclu California Hospital Association, payment to Limited was to be made by instalments. Part of the co that agreement was that International Holdings procured that the Appellant's services were made Limited without charge.

27. The first directors of International Holdings were the Appellant, Mr Copleston, Mr Charkin (all direc Limited), the Appellant's father Mr W V Carvill, Mr Jack Sullivan, Mr J A Perman and Mr R S L Pear partners in Conyers, Dill & Pearman (Bermuda lawyers) and Mr N J Holbrow (Bank of Bermuda). J who was a leading US reinsurance broker who had then taken early retirement, joined the board o Holdings, accepting the offer of appointment as a director on 21 December 1982. His directors' fe plus a bonus at the directors' discretion. He was responsible for bringing very considerable busine

group, including one of their largest clients, the Farmers Insurance Company, the largest insurer i which his father was chairman. The board meeting of 23 May 1983 mentions that he had made in Holborn Agencies of New York, Hartford Speciality and Terra Nova. A bonus of $300,000 was vote meeting of 20 October 1983.

28. The board of International Holdings met four times a year, meetings normally lasting 3 days, inclu management meetings and a formal board meeting, although there were some other meetings at formal business was carried out which were attended only by the Bermuda resident directors. At a meeting on 23 May 1983 it was decided that a stronger presence in North America was needed an consideration was given to acquiring an established intermediary about which Mr Sullivan said gre needed in case US intermediaries tried to retaliate. Instead, Mr Wybar and another executive were employed by (but not as directors of) International Holdings spending time in the US but without having any office there. Mr Wybar would spend a minimum of 90 days per annum in the US. The A described Mr Wybar as very influential. At the same meeting Mr Wybar had reported that there wa in confidence in Lloyd's in the US on account of recent disclosures. Another aspect discussed was risks back into the US. Mention was made of other introductions by Mr Sullivan which could lead t Finally, there was a discussion of a report in the Wall Street Journal concerning Bermuda and the expressed that if there was increased adverse publicity for Bermuda the company might need to r US.

29. At the International Holdings board meeting on 27 September 1983 Mr Tom Welstead was appoin He was an influential person in insurance (rather than reinsurance) in the US having been preside company; his reinsurance experience was in the field of marine reinsurance. The meeting of 20 Oc records that Mr Welstead had been influential in arranging a meeting with Home Re which had res business for Limited. The first direct business, which I understand to mean business not obtained broker, with Western Employers of Chicago, obtained through Mr Sullivan, was reported to that m

30. By the end of the first year of International Holdings four Americans had been appointed directors and substantial business had been attracted through their work.

The Appellant's remuneration arrangements

1. At the time of setting up International Holdings the method of remunerating the Appellant wa is first necessary to describe the previous arrangements. The Appellant did not want to disclo remuneration in the accounts of Holdings. The reason was that competitors would be able to client's attention to the high level of remuneration and suggest that they should not do busin Appellant's companies. The way this was achieved was that he was not a director of Holdings received his remuneration through a company called The Cut Limited which charged the remu Limited. There is no figure for the Appellant's remuneration in the accounts of Holdings for th to 31 December 1981, or thereafter. The Revenue were made aware of the arrangement whi effect. Before the Revenue confirmed his non-domiciled status the Appellant was claiming the deduction for the proportion of his time spent outside the UK under paragraph 2 of Schedule Finance Act 1977. Doubts seem to have arisen in about 1982 about the Appellant being a sha of Holdings which I presume would mean that the remuneration had to be shown in Holdings After the reorganisation, it was determined that all his remuneration should be funded from I Holdings and no disclosure is made in the accounts of that company presumably because Ber does not require it.

2. The Appellant entered into an employment contract with International in September 1980. No cop available but it is clear from the accounts of International, which were produced for the first time that salaries were paid and I find that payments were made to the Appellant. I also find that the c for duties performed abroad because the tax returns (Form 11K for a non-domiciled person) cover the year ended 5 April 1982 show nil against International in the column headed "amount receive but with the column headed "amount paid" left blank, implying that the remittance basis was cons apply, and no remittances had been made. Mr Tuson produced a schedule showing figures for rem from International of £43,340 for 1981/82 and £123,489 for 1983/84 but he could not produce an documents for this information. Such figures were capable of being within the salaries shown in th

and I accept them. The figures were not known to the Revenue before the hearing.

3. On 4 October 1982, which was after he knew that the Revenue had confirmed the Appellant's non status, Mr Tuson wrote to Mr Moscrop of Neville Russell suggesting that the Appellant be employe International Holdings for non-UK duties, on which he expected to be taxed on the remittance bas new non-resident company incorporated in Jersey, Personal Services, for UK duties, on which he e receive the foreign emoluments deduction of 25 per cent. That deduction was abolished for a pers Appellant's position in the Finance Act 1984 with effect from 6 April 1984. In fact that deduction w the Revenue and as it had been abolished for the future the Appellant did not pursue the claim. M does not deal with which company bore the cost of his remuneration. A note of a meeting betwee of the UK and Bermuda companies of 13 December 1982 dealing with The Cut mentions that the e problem about shadow directors would disappear since all the Appellant's income would be derive International Holdings. A corollary of this is that no deduction could be obtained against Limited's Appellant's remuneration for UK duties which directly benefited Limited. On 29 December 1982 th entered into employment contracts with International Holdings for non-UK duties and with Person UK duties. On the same day a secondment agreement was entered into between Personal Service International Holdings stating that Personal Services would make the Appellant's services availabl and that International Holdings would pay Personal Services 105 per cent of the expenses incurre Services in employing the Appellant. International Holdings' obligation to make the Appellant's ser to Limited without charge is dealt with in the brokerage sharing agreement (see paragraph 26 abo

4. There is a note of a meeting on 25 June 1985 in Bermuda in which the suggestion is noted that th UK services should be provided in future by The Cut Limited instead of Personal Services. It appea disclosure of names would be required in the International Holdings accounts. Nothing came of thi

Formation of Inc

1. The International Holdings board meeting on 20 October 1983 resolved to take US tax advice an office in the US. A note by the Appellant to Mr Passmore, the financial controller in Londor later records that they were thinking of opening an office in the Chicago area as the home of direct client. This would, he stated, appear less aggressive than opening in New York. In Nov an offer was made to Mr Koziol who was an insurance rather than reinsurance executive, of a with International Holdings for four weeks during which he could visit London. This was follow December with a proposal of a 12 months consultancy to give consideration to the opening o office in the US at a fee of $90,000 plus a share of the group's profits.

2. At the International Holdings board meeting of 15 February 1984, it was resolved to open a US of establish a US corporation which for US regulatory reasons would be a subsidiary of Limited but w subsidiary of International Holdings (this happened in 1985 following section 482 Taxes Act 1970 office was in Itasca, a suburb of Chicago. At the meeting of 17 July 1984 it was recorded that the had been accepted by the US insurance market but without enthusiasm. Mr Welstead said that for the opening of the office had been the talk of the US insurance market. During 1984 further introd by Mr Welstead were noted and it was recorded that he was spending over one quarter of his time business of the company. He was later employed full-time by Inc. An agreement was made betwe Limited under which Limited agreed to pay Inc 110 per cent of the costs incurred by Inc plus a fee brokerage earned over $1m. International Holdings took over Limited's obligations under that agr meeting of 9 October 1984 it was reported that Inc had an office with three staff.

3. The meeting of 15 January 1985 discussed a draft letter the Appellant had written to seek to reass reinsurance brokers that Inc would not try to solicit the US client but Mr Sullivan thought that sen dangerous.

4. An exchange of correspondence in March 1985 restricted International Holdings' share of brokerag cent of the costs (which included payment for the Appellant's services), any excess profit being pa The reason for this change was so as not to restrict the profits available for distribution to employ This was formalised in a contract between the two companies dated 22 July 1985 which also provi brokerage split between them was two-thirds of the brokerage on risks placed in the UK and Euro to Limited and the balance to International Holdings subject to the cap of 110 per cent of expense

to certain contracts produced through G J Sullivan & Associates Inc (which included the California Association) and through G L Hodson & Son Inc the brokerage was to be spread over a period wit receiving in total two-thirds in the first year and the whole thereafter.

5. Mr Jack Sullivan resigned as a director on International Holdings at the meeting on 16 July 1985 a become a director of a new US reinsurance broking company with his brother Jerry Sullivan which perceived as a conflict of interest.

6. The International Holdings board meeting of 15 April 1985 recorded that the Sedgwick Group was the Fred S James Group which included John F. Sullivan Co. This was likely to result in loss of bus Appellant's group. The Appellant said that they lost 88 contracts in one week as a result of this m Striffler of John F Sullivan was offered employment. This was the first sign of open competition wi reinsurance brokers because Mr Striffler was well known: it was no longer possible to disguise wha doing. This point came to be described during the hearing as "gloves off".

7. The group was extremely successful in competing with US reinsurance brokers after gloves off as from the following figures extracted from the group consolidated figures in £000.

	1984	1985	1986	1987
Turnover	6,796	11,958	19,870	23,185
Of which brokerage	3,457	7,636	13,673	14,409
Expenses	(6,516)	(11,767)	(14,579)	(15,292)
Of which salaries	4,586	7,172	8,305	8,135
Other costs e.g. exchange losses	(31)	(268)	(287)	(1,178)
Profit before tax	249	(77)	5,004	6,715
Tax	(155)	(253)	(1,770)	(2,494)
Profit available for distribution	94	(330)	3,234	4,221
Dividends paid				5,832

1. There is a large rise in both income and expenses starting in 1985 and becoming much more in 1986, presumably because there was less than a full year from gloves off in 1985 and the building up from then. The effect of capping bonuses (see below) is that salaries rose much n than income and other expenses, resulting in significant profits for the first time from 1986. T paid was funded almost entirely from dividends received from Holdings of £3,380,000 provid 1986 accounts of Holdings and £3,450,000 provided for in the 1987 accounts, total £5,830,0

Further events relating to International Holdings

2. Sir Michael Edwardes became a consultant to International Holdings from 7 January 1986. Mr the Appellant's brother who is a Dublin lawyer was appointed a director from 10 November 1 meeting on 4 November 1988 the appointment of Mr Lyman Baldwin who was about to retire of Hartford Re was discussed and in view of the sensitivity of the appontment with US compa resolved to offer a 3 month consultancy. His appointment as a director was approved at the n February 1989. The meeting of 25 July 1990 resolved to offer a directorship to Mr Tom Hearn President of G L Hodson in the Corroon & Black group.

3. Thomas A Greene, the US intermediary, severed relationships with the group in January 1990 as t the activities of Inc. The board of International Holdings noted at the meeting of 8 February 1990 was open to approach their clients, and that they were well placed to fulfil the aspirations of the A

clients.

4. Following a memorandum of 18 October 1985 from Mr Tuson the brokerage split was amended, w no other US intermediary, to one-third to Inc, four-ninths to Limited, and two-ninths to Internatio

5. Throughout its existence, the board of International Holdings determined the group policy with ea subsidiaries reporting to it.

Payment of bonuses and the decision to pay dividends

6. From the start of Limited, all the profits other than those needed for the business had been d bonuses to employees. Originally shares were issued to employees and bonus distributions w proportion to the number of shares held. At first these were voting shares but from 1979 nor shares were issued so that the Appellant could keep control of the company. In 1980 it was d issue any more shares, and profit-sharing units were given to employees. By 1984 the result business meant that very large amounts were being distributed as bonuses. The Appellant sa employee's half-year bonus could be sufficient to buy a house.

7. Mr Tuson wrote a memorandum on 29 October 1984 proposing fixed and variable profit-sharing u concerned about the deductibility of large bonus payments and put forward the suggestion of payi On 7 March 1985 the Appellant wrote a memorandum entitled "super profit plan" stating that he w super profit-sharing percentages in advance. In a memorandum of 25 April 1985 Mr Tuson pointe because of the phased reduction in corporation tax and the ending of the earnings ceiling for emp insurance contributions it would become more tax effective to pay dividends rather than bonuses This seems to be a theoretical exercise since at the time no employees held shares in a UK reside was not directed to the Appellant's position taking dividends from International Holdings since UK into account in the dividends suggested. That note also looks at changing the policy of paying out as bonuses and consequently the possibility of Limited paying dividends to International Holdings funds could be invested to produce a return free of tax". At this stage therefore there was no sugg International Holdings distributing any dividends to the Appellant. In an accompanying memorand looked at the possibility of the employees other than the Appellant selling their shares in Internati to an employee trust from which bonuses would be paid. There is another memorandum from Mr finance director of Limited, suggesting a redemption of the non-voting shares in International Hol changing the profit-sharing arrangements.

8. Next the Appellant wrote a memorandum on 2 July 1985 to the founder shareholders proposing co them by an earnings stream for life in exchange for the Appellant owning all the shares in Interna Holdings. He makes the point that there was no intention to sell the company but if it were sold fo members would retain the right to share in the proceeds. Mr Tuson followed this up the next day w memorandum setting out how the reorganisation could be implemented. He included a statement anticipated that the minority shareholders would accept the offer, which turned out not to be the the Appellant following discussions on 8 August 1985 records that it is extremely unlikely that the sold but, if it were sold, profit-sharing units would rank equally with the shares. Negotiations over must have continued as Mr Tuson wrote a memorandum on 30 October 1985 suggesting that an e acquire the employees' shares in International Holdings. At the board meeting of International Ho January 1986 it is recorded that it was not acceptable to the employee shareholders that the comp acquire their shares and that an employee trust was being considered which Conyers, Dill & Pearm instructed to draft. A further note by Mr Tuson of 15 February 1986 again refers to a proposed em and a note of 22 September 1986 again looks at the alternative of the company purchasing its ow final proposal is contained in an undated memorandum from Mr Tuson which was apparently writt November 1986. This consisted of the purchase by International Holdings of its shares held by em than the Appellant at their asset value, plus an undertaking given by the Appellant to an employe before entering into any transaction by which his ahareholding would be reduced below 50 per cen sell at par the same proportion of his shares as the proportion of the group profits distributed to e other than the Appellant. He would also leave by will more than 50 per cent of the shares to the e A draft of an employee trust was tabled at the board meeting of International Holdings on 9 Febru an engrossment for execution was tabled at the meeting on 27 April 1987. The trust is dated 17 J

Appellant's undertaking was given on 26 November 1987.

9. The purchase of own shares required an alteration to the memorandum of association of Internati which required the votes of the voting shareholders. This took place on 30 December 1986.

10. Following the purchase of the New Minority shares bonuses to the former shareholders were capp level increased by inflation.

11. At the International Holdings board meeting on 17 July 1984 it was declared that Mr Bassett, a di Limited, had announced that he intended to resign within the next twelve months to pursue busin outside the insurance field. At the meeting on 16 July 1985 the purchase by the Appellant of Mr B was recorded.

12. On 19 December 1986, Mr Tuson wrote a memorandum suggesting that, now that the Appellant v shareholder in International Holdings, they should reconsider paying the Appellant by way of divid International Holdings rather than bonus. This would give approximately an 11 per cent increase i income. There were some complications such that, if he did not take a bonus from International H profits would be increased above 10 per cent of its expenses and so further profit would be made and that ACT would be payable on dividends paid by Limited. The Appellant did not take the oppo increasing his income in this way. Secondly, Mr Tuson suggested that as Limited will make profits whole profits will not be paid as bonuses, dividends be paid to International Holdings in order to a corporation tax on the income generated from such profits. The benefit in terms of retained profit dividends was minimal after one year if minimum ACT was payable, and worse than retaining prof maximum ACT was payable, although in such case by the end of the second year it roughly broke calculations were on the basis that International Holdings retained those dividends rather than pa Appellant. A further memorandum of 13 February 1987 discusses whether to pay dividends from Holdings or to retain the profits for reinvestment in which case a further holding company is sugg

13. At the International Holdings board meeting on 27 April 1987 it was reported that a profit for 198 expected in Limited and that a dividend would probably be paid for the first time. It was decided t UK position was finalised before considering International Holdings' own dividend policy. At the m July 1987 it was in fact resolved not to pay a dividend. An interim dividend for 1987 was, howeve be paid on 16 November 1987 of £2,381,880 (the 1986 dividend from Holdings was £2,380,000).

Findings of the Appellant's purpose from the facts

1. The essence of the dispute between the parties is how International Holdings contributed to t commercial strategy. The Revenue accept the whole of the Appellant's strategy as being com as they cannot understand how International Holdings fits into it, they contend that Internati was something inserted by Mr Tuson for tax reasons which may have come to play a comme These tax reasons were said to be the obtaining of the remittance basis for the employment non-UK duties, the foreign emoluments deduction for the employment income for UK duties, remittance basis for dividends paid by International Holdings out of dividends paid by Holding corporation tax reduction which was not made clear to me (originally the avoidance of capita was put forward but this is not now pursued). As I understood the Revenue's position by the case it was that they accept that, if there was a good commercial reason for setting up Inter Holdings in Bermuda, obtaining these tax benefits would not be tax avoidance. Accordingly, t I have to determine is whether International Holdings was set up for commercial or tax reaso this stage make my findings of fact without regard to whether something is a bona fide comm transaction or is tax avoidance within section 741, and I shall return to consider these points

2. I can understand the Revenue's difficulty in following the reasons given in the clearance applicatio paragraph 22 above, particularly the last sentence ("From its base in Bermuda, International Hold then be able to procure in the United States business for [Limited] without being seen to compete established U.S. brokers"). It is difficult to see how International Holdings solves the problem of c the US without being noticed. Mr Vallance's much repeated question "why Bermuda?" was trying t answer to this question. To the Appellant's side, no doubt because they did not come to the probl

from the clearance application, the relevant question was "why not Bermuda?" Indeed Mr Kirby sa question from Mr Vallance "you keep asking the question why Bermuda? I am afraid I ask the que else would you have us put it?" I shall return to this point.

3. The Appellant set out his reasons for needing a Bermuda holding company in his witness statemer

We decided that if we were to succeed in our attempt to source our own business as well as place it be done by establishing the Group as an international group and one that was perceived as being loc London or the USA. Certainly, we had to operate in both territories but I wanted the companies to o sister companies under an international board. I did not want either London or the USA to be seen a with the other as servant. From my own experience of working in the USA and the UK, I knew that t recipe for trouble with American and British personnel. I saw this happen when March McLennan too Bowrings.

1. I think that the important words are perceived and seen. The Appellant explained the rationa Bermuda holding company that he intended to have a board of International Holdings compri producers and London placers of reinsurance, and because the Americans regarded productio important part of the business, it would not have worked if the Americans had been subordin London board. Mr Vallance made much in cross-examination of the apparent lack of logic of t position since he was the owner of a private company and he was well known to be based in the reality was that the UK predominated. As I am applying a subjective test, what matters is Appellant thought, not whether this could be justified logically. In determining the Appellant's have to put myself in his mind which is particularly difficult as he was pursuing a strategy un Lloyd's reinsurance brokers and which was obviously highly risky. It is therefore particularly h a description of the Appellant by others who worked with him. Mr Kirby described the Appella management style as "closer to Churchill than Hitler" and described him as a thoughtful man thought-through vision of what he was trying to achieve. He also described the Appellant as a powerful personality who likes to get his own way but will listen to others. Having heard the A the witness box for over two and a half days and having heard the other witnesses, I accept business strategy was the real reason for the Bermuda holding company, and that it was not avoid tax. If one looks at the minutes of the board meeting of International Holdings, which i important as a contemporary record, a strong impression is given of senior American and Bri meeting on neutral territory and determining the strategy of the group in circumstances whe strategy was difficult to achieve and a mistake could have ruined the business. I did not see suggesting that the Appellant used his shareholding control to achieve a particular result. In perception had become the reality. Another example where the perception was regarded as i others can be seen in the proposal made in the board meeting of International Holdings on 8 for a joint venture with G J Sullivan & Associates Inc (which in fact never happened) to devel classes of reinsurance business including financial guarantee business, where it was recorded Sullivan felt that "by using Bermuda it would not be politically embarrassing to one or both o was explained by the Appellant as meaning that neither would be seen as the junior partner.

2. The conclusion I have reached was that the Appellant from the beginning saw the end result as it but did not clearly see how to reach it. He certainly foresaw the link-ups between US and UK reins brokers and the loss of business to which this would lead. He foresaw the need for a US operation ability in the US reinsurance market. This required two types of Americans, those who could open facilitate procuring business, and those who would work in placing the risks in the US market. I he evidence about who was or was not regarded as a "big hitter", that is, a leading producer of reins business for the group. It seems to me that the Appellant and his co-directors employed those wh considered would best further his commercial strategy and it should not matter to me how they w categorised. He considered that for commercial success the end product needed to have a holding neutral country which was neither the US nor the UK when all the other competing reinsurance br would later become, US companies owning UK subsidiaries or (to a much smaller extent) vice vers not have worked if the Americans had been subordinated to a London board. The Americans who doors would, he considered, not wish to be seen to be working for a UK organisation. As the Appe they would not easily be characterised by their fellow Americans as selling out to the UK oppositio on the board of a Bermuda company. There was serious rivalry between US and UK reinsurance b

time because UK brokers had access to the important Lloyd's market. Meetings of International H be meetings on neutral terrritory of US and UK people where neither country dominated. A holdin Bermuda was a feature in attracting Mr Sullivan, Mr Welstead and later Mr Hearn. I accept that th any tax benefits, was the reason for setting up International Holdings.

3. Bermuda had an additional advantage that at the margins it was possible to place business in the from there without going through a US broker. This was a subsidiary purpose of having a holding Bermuda before the formation of Inc.

4. In accepting the evidence of the witnesses in the light of the contemporary documents, particular minutes of International Holdings, I should set out my reasons for accepting that tax did not featu Appellant's decision. So far as dividends are concerned the choice was between paying bonuses o 1982 this meant that either the employee paid income tax at 60% (we can assume that all the se paid tax at the top rate), or that dividends were paid out of profits which had borne tax at 52%. I marginal £100 of profit in Limited and takes the Appellant's shareholding to be 60%, instead of hi by paying dividends via International Holdings which he did not remit he could increase his after t from £24 (a bonus of £60 less tax of £36) to £28.80 (a dividend of 60% of the after-tax profit of £ increase in income so long as he did not need to remit it. On the other hand, the other employees 40% holding in total paid the investment income surcharge and lost the benefit of the dividend ta resulting in £4.80 after tax as dividend instead of £16 after tax as bonus, a loss of 70%. I cannot the Appellant, who, I have found. set up International Holdings in order to have a management st designed to motivate his staff, would have put them at this disadvantage if dividends had been in not think that dividends can have been in his mind when Limited had never paid any in the past; t that Holdings paid dividends was after the commercial success following gloves off. If the Appellan the result of his success was that bonuses would be capped with the consequence that dividends w which I do not find that he did, he would surely not have allowed the employees to transfer their s International Holdings. So far as the purchase of own shares by International Holdings is concerne from the facts I have outlined in paragraph 7 onwards that this was not done in order to enable di paid to the Appellant but as part of the lengthy process of tidying up the bonus arrangements. Th started in 1984 well before there were profits out of which dividends could be paid. It is relevant t much later, it was pointed out to the Appellant that he would be better off by 11% by taking his re dividends (see paragraph 12) he did nothing about it.

5. Nor do I find that obtaining the tax benefits of the employment arrangements were any part of th the transfer of the Appellant's shares to International Holdings. The income out of which the Appe remuneration was paid was derived from profits of International Holdings. While there is some art Personal Holdings employing him for UK duties, as there had been earlier with The Cut Limited, th that there was no corporation tax deduction at 52% (of which the Appellant bore 59% of the addi corporation tax), he expected to obtain the foreign emoluments deduction of 25% of 60% tax, so extremely tax inefficient. The only rational reason for it was that the Appellant was keen not to ha his remuneration in the accounts of the UK companies. If Personal Services had not existed, he w obtained the foreign emoluments deduction for his employment by International Holdings.

6. The arrangements for employing him outside the UK were a successor of his employment with Int a new holding company was not necessary in order to achieve them. Therefore it cannot have bee the transfer of the Appellant's shares to International Holdings to enable him to obtain the remitta his remuneration for non-UK duties; he was already receiving that benefit. (The application of the basis to this income is still, I understand, in dispute).

7. There are other features which do not suggest that the reorganisation was tax driven, the most st the capping of International Holdings' profits to 110% of its expenses. Mr Vallance suggested that showed that the Appellant was being careful not to take the tax savings to excess in order to redu of attack by the Revenue. I do not think that this is a correct description of the Appellant's approa

8. Finally, the passage I have quoted from Mr Tuson's memorandum of 12 July 1982 in paragraph 21 "Although there are a number of respectable locations which would be suitable, none has any logi commercial justification…I suggest that we proceed on the basis that Bermuda would be the locati International Holdings." confirms what all the witnesses said, that Bermuda was not Mr Tuson's ch location for a holding company but something which the directors had already decided. I understa

saying that on tax grounds he would have chosen a different jurisdiction for a holding company, p with tax treaties, but that there were no jurisdictions which had the commercial justification of Be he was approving the directors' choice of Bermuda.

9. In summary in relation to the tax benefits, the Appellant's purpose, that is the end result which he achieve, was to have a holding company in a neutral country to direct the group's strategy. Interr Holdings provided a vehicle for his non-UK employment which would be taxed on the remittance b a natural consequence of having the company, rather than "the", or even "a", reason for it. Perso was not a necessary part of that transaction but, because it gave him the foreign emoluments dec cost of no corporation tax relief against UK profits, its purpose cannot have been to save tax, but been in order to avoid disclosure of his remuneration in the accounts of the UK companies. The pa dividends in the future was not something which the Appellant had in mind at the time of setting u International Holdings.

10. Since I am disagreeing with the more experienced Special Commissioner who decided the case at hearing I have re-read his decision to see if there is anything in it which suggests to me that I am making these findings on the evidence before me. I had several advantages over Mr Everett. First to many of Mr Tuson's documents which were found by the auditors after the earlier hearing; miss of the tax adviser must have raised suspicions when a major issue in the case is whether the arra wholly commercial or partly inserted by Mr Tuson for tax reasons. I found Mr Tuson a very helpful did not say anything other than what I expected to hear from a tax adviser, as opposed to the arc avoidance scheme, whereas Mr Everett said that he could not accept his oral testimony at face va reason was that Mr Tuson said that he was called as a witness at the previous hearing at the last was dealing in 1994 with his recollection of events of 1982 without the benefit of his documents. the benefit of hearing more witnesses. I would single out Mr Kirby as being particularly helpful as explain the strategy in a way the Appellant never seemed quite able to do. Finally, the pervious h eight days whereas mine lasted 13 and with the benefit of Mr Vallance's extremely detailed cross- have been able to go into the facts in greater depth. I have fully taken into account Mr Vallance's the previous decision means that I should approach the evidence with a degree of caution and rel common sense, probability and contemporary documents than on people's recollection of events o

11. I must, however, return to the "why Bermuda?" question and the meaning of the sentence in the application setting out the commercial reasons for the reorganisation: "From its base in Bermuda, Holdings would then be able to procure in the United States business for [Limited] without being s compete with established U.S. brokers". I do not think that Mr Vallance ever received a satisfacto the question how International Holdings achieved this, probably because there is no answer. It is that, as a known UK figure, it did not make any difference whether the Appellant approached the via a Bermuda company, particularly a Bermuda holding company whose main function was to dir in both countries, rather than one having any facilities to assist in procuring business in the US. T for the Bermuda company before "gloves off" was to attract such people as Mr Sullivan and Mr We would help form the strategy for the group to penetrate the US market without losing their busine having successfully achieved that, its function was to direct the strategy of the group from a neut US and UK directors in which neither country dominated. The statement in the clearance applicati misleading in suggesting that the purpose of the holding company was to procure business in the gloves off when it seems to me that its important function was deciding how to set about procurin it is also misleading in making no reference to its directing function after Inc had been formed. A subsequent problems might have been saved if the clearance application had explained the comm in the way that came out in the evidence. The moral is that explaining commercial reasons should newly appointed tax advisers and the auditors.

Section 739 of the Taxes Act 1988

This provides:

(1) Subject to section 747(4)(b), the following provisions of this section shall have effect for the pur preventing the avoiding by individuals ordinarily resident in the United Kingdom of liability to income means of transfer of assets by virtue or in consequence of which, either alone or in conjunction with

operations, income becomes payable to persons resident or domiciled outside the United Kingdom.

(2) Where by virtue or in consequence of any such transfer, either alone or in conjunction with asso operations, such an individual has, within the meaning of this section, power to enjoy, whether forth future, any income of a person resident or domiciled outside the United Kingdom which, if it were in individual received by him in the United Kingdom, would be chargeable to income tax by deduction that income shall, whether it would or would not have been chargeable to income tax apart from the this section, be deemed to be income of that individual for all purposes of the Income Tax Acts.

(3) Where, whether before or after any such transfer, such an individual receives or is entitled to re capital sum the payment of which is in any way connected with the transfer or any associated opera income which, by virtue or in consequence of the transfer, either alone or in conjunction with associ operations, has become the income of a person resident or domiciled outside the United Kingdom sh would or would not have been chargeable to income tax apart from the provisions of this section, be be income of that individual for all purposes of the Income Tax Acts….

1. The Appellant agrees that the transfer of the Old Majority Shares to International Holdings is assets by the Appellant within the section by virtue of which income became payable to Inter Holdings in the form of dividends on the Old Majority Shares which the Appellant as holder of Majority shares had power to enjoy. The Appellant contends that there are no other associate The Appellant also contends that the exemption in section 741, which I have set out above, a

Reasons for the decision

2. Miss Gloster in her closing submissions helpfully listed the issues which needed to be determi shall follow these with some variations caused by my findings of fact.

Issue 1. Whether, as a matter of law, the Appellant can be treated as "the transferor" for the purpos 739 in relation to all the shares in Holdings

3. In other words, was the Appellant the transferor of the Old Minority Shares owned by other c employees which were transferred to International Holdings as Mr Vallance contends. It is cle transferor for the purposes of the section can in some circumstances be wider than merely th makes the transfer himself. An example is a transfer by a company which is wholly owned by concerned, as occurred in Congreve v IRC 30 TC 163. In IRC v Pratt 57 TC 1, the issue arose three taxpayers who between them owned 12,268 out of 42,400 shares in a company and of were three of the eight directors of the company, were the transferors for the purposes of thi an asset sold by the company. The Revenue contended that each of them as a shareholder a had concurred with the disposal to sell the asset and therefore had a "hand in" and was "asso the transfer and had "procured" the transfer. This was rejected by Walton J on the ground th could not on their own, either as directors or shareholders, have procured the company to do an individual to be the transferor in relation to a transfer by another individual would be a co extension of this principle. However, there might be cases where, as a matter of fact, one ind influence over another was so strong that he was the transferor of the other's shares but this be an exceptional case. Accordingly I propose to proceed on the basis that it may be possible one individual to be the transferor of an asset transferred by another individual, and move on the facts.

Issue 2. Whether, as a matter of fact, on the evidence the Appellant did "bring about" the transfer o Minority Shares

4. Mr Vallance contends that the Appellant was the transferor of the Old Minority Shares. In ord this was an exceptional case where the Appellant did in effect force his will on the other shar to become the transferor of their shares, one would need strong evidence that this was so. O Appellant as majority shareholder and one of the founders of a company bearing his name w position of some influence. However, the influence did not go as far as telling other shareholo

do with their shares. Here the decision by the Old Minority to transfer their shares was one w
came to after discussion, having started with different points of view as to the merits of the t
is no evidence that the Appellant leaned on any of them heavily, for example, by threatening
if they did not. It is also clear that this was not the Appellant's management style. According
evidence that the Appellant did anything in relation to the Old Minority Shares which would m
transferor of them, and I find that he was not the transferor of the Old Minority Shares. The
transfer for the section, which is admitted by the Appellant, is the Appellant's transfer of the
Shares (I shall consider the 1986 repurchase of the New Minority Shares separately in Issue

Issue 3. In relation to the Appellant's transfer of shares in Holdings to International Holdings, what,
law, are the associated operations?

5. Mr Vallance separates the transfers to International Holdings into two: first the incorporation
subscription of shares in International Holdings, and secondly, the acquisition by Internationa
the shares in Holdings UK in exchange for its own shares. Miss Gloster treats this as a single
little difference between the two approaches in relation to transactions which are almost simu
I shall therefore treat these as effectively the same transfer, having already decided that the
transfer is by the Appellant in relation to the Old Majority Shares. The Revenue contend that
operations in relation to that transfer are first the purchase by International Holdings of the N
Shares in 1986 and the acquisition by the Appellant of Mr Bassett's shares in July 1985. In th
the Revenue contends that there are the following additional six associated operations:

6. 1. The incorporation of Personal Holdings

7. 2. The Appellant's contract of employment with Personal Holdings

8. 3. The provision of services by the Appellant to Personal Services

9. 4. The Appellant's contract of employment with International Holdings

10. 5. The performance of duties by the Appellant for International Holdings

11. 6. The Brokerage Sharing Agreement of December 1982.

12. The definition of associated operations in section 742(1) is:

"'an associated operation' means, in relation to any transfer, an operation of any kind effected by a
in relation to any of the assets transferred or any assets representing, whether directly or indirectly,
assets transferred, or to the income arising from any such assets, or to any assets representing, wh
or indirectly, the accumulation of income arising from any such assets"

13. In construing this provision I bear in mind that "It has been said more than once that [sectio
broad spectrum anti-avoidance provision which should not be narrowly or technically constru
Brackett 60 TC 134 at 148B per Hoffman J) and also that the definition of associated operatio
extremely broad. In Fynn v IRC 37 TC 629, 637 Upjohn J applied the ordinary use of languag
determine whether there was any relationship between two transactions. The assets transfer
Appellant's shares in Holdings (the Old Majority Shares); the assets representing them are th
shares in International Holdings (the New Majority Shares). On the ordinary use of language,
however wide a meaning one gives to the expression "in relation to", it is difficult to see how
transactions are operations which relate to either the Old or the New Majority shares. They e
different shares (such as the repurchase of the New Minority Shares or the purchase of Mr Ba
shares) or they do not relate to any shares at all (such as the employment arrangements or
sharing agreement). If I am wrong about this, they are not associated operations which are n
because no income becomes payable to International Holdings by virtue or in consequence o
transactions; the income, i.e. the dividends on the Old Majority Shares becomes payable to I
Holdings solely by virtue of the transfer of the Old Majority Shares to International Holdings.

these transactions give the Appellant power to enjoy the income of International Holdings; he power by virtue of holding the New Majority Shares which he obtained solely as a result of th

14. In particular, the purchase by the Appellant of Mr Bassett's shares in International Holdings (see p above) did not relate in any way to the Old or New Majority shares. Nor did any income become p International Holdings by virtue of the purchase; all International Holdings' income continued to b

15. The repurchase of the New Minority Shares in 1986 has no relationship with the Old Majority Shar asset representing them, being the New Majority Shares. The New Majority Shares owned by the remained as they were before and after the repurchase of the New Minority Shares and therefore is not an operation of any kind in relation to either the Old or New Majority Shares. The New Majo carried with them, rights which varied in extent according to the number of other shares in issue economic relationship not a legal relationship. Mr Vallance on the other hand, contended that the repurchase of the New Minority Shares was that the Appellant became entitled to the whole of the International Holdings, thus emphasising the economic relationship. I agree with the Appellant tha repurchase of the New Minority Shares is not an operation relating to the Appellant's New Majority reason why the Appellant can enjoy all the dividends paid by Holdings to International Holdings is anything which has happened to his shares but because the other shares have been repurchased entitlement relates to a smaller cake. The Appellant also contends that, even if the repurchase of Minority Shares is an associated operation, it is not a relevant one for the section because first the became payable to International Holdings by virtue of the transfer of the Old Majority Shares, bei dividends on the Old Majority Shares, remained unchanged, and secondly, the Appellant's power t income was unchanged by the purchase of the New Minority Shares. I also agree that even if it we associated operation it would not be a relevant one for the purpose of the section. The change rel Appellant's power to enjoy the income from the Old Minority Shares but since he was not the tran shares this is not within the section.

16. Nor is there any relationship between the six items listed above and the transfer of the Old Majori the asset representing them, the New Majority Shares because none of them relates to shares at

17. Accordingly, I hold that none of the transactions is an associated operation as a matter of law and are they are not relevant transactions because they do not contribute to income becoming payabl International Holdings or to the Appellant's power to enjoy that income. However, I should add th to my findings, that the purpose of the transfer was to avoid tax (assuming that these constitute within the meaning of the section) by means of any of the six listed items, then that would inevita one of the purposes of the transfer and therefore it makes little difference to the result under sect whether or not they are associated operations.

Issue 4. What, as a matter of law, are the constituent elements of the test which the Appellant has order to claim the exemption under section 741?

1. I have already dealt with the question whether the test in section 741 is subjective or objecti Appellant's primary contention is that paragraph (b) is applicable: "that the transfer and any operations were bona fide commercial transactions and were not designed for the purpose of liability to taxation". In view of my decision that there are no operations associated with the Old Majority Shares to International Holdings I apply this test to the transfer only (I shall dea question whether the 1986 repurchase is a transfer below).

2. There was not much difference between the parties about what constituted a bona fide commercia Miss Gloster contended that this was any genuine transaction which implements or facilitates a bu Vallance contended that the transaction must be in furtherance of commerce, i.e. a trade or busin follow these two meanings. Because of the dual test in paragraph (b) such a transaction may have avoiding tax.

3. There was less agreement between the parties about the degree of tax avoidance permitted in the "not designed for the purpose of avoiding liability to taxation". There is a significant contrast betw (a) of section 741, which refers to "the purpose or one of the purposes" being tax avoidance, and which refers to "the purpose" being tax avoidance. Miss Gloster contended that "the purpose" imp

had to be the sole purpose of the design of the transfer. Mr Vallance contended that the method c achieve the commercial objective must not be structured ("designed") for the purpose of tax avoi tax avoidance were a significant purpose of the design the taxpayer would not be able to satisfy t

4. The history of the legislation was referred to. Originally, in 1936 there was a single let-out provisi transfer of assets "effected mainly for some purpose other than the purpose of avoiding liability to Section 28 of the Finance Act 1938 changed this to the present wording of section 741 which in pa applies a more stringent test of one of the purposes of the transfer (and associated operations) no avoidance, and in paragraph (b) merely refers to the transfer (and associated operations) not bei that purpose. Clearly, this cannot mean one of the purposes for which it was designed being tax a because otherwise paragraph (b) would add nothing to paragraph (a). It is odd that Parliament di any level of purpose in paragraph (b) when it was replacing a test which depended mainly on tax a test in paragraph (a) depending on none of the purposes being tax avoidance. It was obviously paragraph (a) that a transfer could have more than one purpose and therefore in paragraph (b) c designed for more than one purpose. One must ask in paragraph (b) whether the transfer was des purpose of avoiding tax or not. This seems to me to require that the main purpose was not tax av because if one has to categorise a transaction as being either designed for the purpose of tax avo when it is clearly accepted that a transaction may be designed for more than one purpose, the on categorise the design into one purpose is to look at the main purpose of the design. I think, there Appellant's contention of sole purpose is too loose a test and the Revenue's contention of significa too stringent a test although it will in practice be difficult to determine the difference between a si main purpose. In view of my finding that tax was not a purpose of the transfer it makes no differe decision what degree of purpose is required.

5. There was also disagreement between the parties about what is tax avoidance, although both acc distinction between tax avoidance and tax mitigation originally proposed in IRC v Challenge Corpo AC 548. In Willoughby when construing paragraph (a) of section 741, Lord Nolan said "tax avoida meaning of section 741 is a course of action designed to conflict with or defeat the evident intenti Parliament". Mr Vallance pointed to the difficulty of this formulation that the taxpayer needs to sh that he has done something which the statute permits him to do. Although he did not put it in this v Dawson would be an example of a taxpayer using a relieving provision in a statute but still avoi because he was trying to use the relieving provision in circumstances for which it was intended. W mind, Mr Vallance contended for a somewhat narrow meaning of tax mitigation building on Lord T examples in Challenge which were all cases where the taxpayer's expenditure reduces his income him to a reduction in his tax liability. Miss Gloster contended that tax mitigation is not limited to c there are specific relieving provisions because there was no such relieving provision for bed and b transactions which were accepted in Ensign Tankers 64 TC 617 as being mitigation on the basis th loss had been suffered.

6. Tax avoidance is an extremely elusive concept and I propose to follow Lord Nolan's meaning of a action designed to conflict with or defeat the evident intention of Parliament. My understanding of saying is not, I think, much different from what Mr Vallance is contending. It is not enough to say a relieving provision then it is the evident intention of Parliament that the taxpayer should be enti whatever the circumstances. As Furniss v Dawson shows it is quite possible to mis-use a relieving give an example in the same area as this case, suppose the Appellant had formed Personal Holdin give him a non-resident employer in order to obtain the foreign emoluments deduction. If that co been funded entirely by the UK companies and had done nothing other than employ the Appellant the case that the Appellant would have been avoiding tax because he was misusing a relieving pro example of course is deliberately different from the facts of this case where Personal Services was non-UK profits with no corporation tax deduction for services which benefited the UK companies. I went as far as claiming that Parliament's purpose in enacting the foreign emoluments deduction w encourage, or at least not discourage, people from abroad to work in the UK so that someone in t position who had spent all his working life in the UK, could never qualify. While this may have bee Parliament's mind, I cannot accept that the relief was not available to a non-domiciled person wor UK resident employer whose remuneration is borne by a non-resident, however long the non-dom has been resident (I note that the amount of relief was reduced after nine years' residence). All th how difficult it is to discern the evident intention of Parliament but I do not think there is any subs disagreement between the parties if Lord Nolan's dictum is understood in the way I have suggeste taxpayer must do more than point to the existence of a relieving provision; he must be using, rath

misusing, the relieving provision in a way consistent with Parliament's evident intention.

Issue 5. Whether, as a matter of fact, the Appellant has satisfied the exemption under section 741(b

1. In the light of my findings above, I can summarise that the purpose of setting up Internation and accordingly the purpose of the Appellant's transfer of the Old Majority Shares to it, was t vehicle for the ultimate management of the group from a neutral territory and in the meantir vehicle for determining the strategy for setting up in the US. I have no hesitation in finding th bona fide commercial transaction. I find both that there was no tax avoidance purpose in the described, and that tax considerations did not form any of the Appellant's purposes in design transaction. Obtaining any tax benefits from the employment arrangements were not a purpo transfer but were matters which followed from it and for which a holding company was not ne None of the potential tax benefits, such as payment of dividends, was a purpose of the transf Accordingly I hold that the Appellant has satisfied the exemption in section 741(b).

Issue 6. Whether, as a matter of law, the repurchase of the New Minority shares by International Ho transfer of assets

2. The reason why Mr Vallance contends that the repurchase of the New Minority shares in 1986 of assets is in order to contend that the Appellant is the transferor of it by procuring the tran New Minority shareholders. The way this is put is that by virtue of this transfer together with associated operations of the original transfer (or, as the Revenue say, two transfers, see para above) in 1982, income becomes payable to International Holdings in the form of dividends f This seems rather a strained construction because all the income becoming payable to Intern Holdings had already done so by virtue of the transfer of the Old Majority Shares in 1982 whi purpose the Revenue have to regard as an associated operation. I need not pursue this beca against the Revenue on their contention that the Appellant was the transferor in relation to th Minority shares (see Issues 7 and 8) but had it been necessary for me to make a decision on would have concluded that this was not a transfer within the meaning of the section because meaning of the section too far to say that income becomes payable to International Holdings this transfer in conjunction with the associated operation when it was the associated operatio assumption that the 1982 transfer was an associated operation) on its own which had caused to become payable to International Holdings.

Issue 7. Whether, as a matter of law, the Appellant can be treated as the transferor in relation to th Minority Shares

3. This is the same point of law as Issue 1 in which I decided that it might be possible in an exc for an individual to be regarded as the transferor in relation to a transfer by another individua

Issue 8. Whether, as a matter of fact, the Appellant did "bring about" the transfer of the New Minori

4. The evidence on this point is strongly that the Appellant did not exert any influence over the shareholders to make this transfer. Indeed, negotiations went on between the decision to buy shares in July 1985 and its completion in December 1986 before the shareholders made their transfer their shares. Before the shareholders decided to do so the Appellant had to undertak employee trust at par (an enormous undervalue) the same proportion of his shares as the pr the group profit which had at the time been distributed to employees other than the Appellan agreed to leave by will more than 50% of his shares to the Employee Trust. It is clear that th transferred their shares as a result of a commercial bargain under which they were satisfied t were right. This was an independent decision made by the New Minority Shareholders after n discussion and it was certainly not a case of the Appellant influencing them into making the t such an extent that he could be regarded as procuring the transfers. I find that the Appellant matter of fact the transferor of the New Minority Shares.

Issue 9. What, as a matter of law, are the associated operations relating to the 1986 repurchase?

5. This issue does not arise as I have decided that the Appellant was not the transferor of 1986 shares and accordingly it is not a relevant transfer for the purposes of the section. However, decided that none of the operations which the Revenue contend are associated operations ar in relation to the New Minority Shares because however widely one construes "in relation to" any relationship.

Issue 10. The quantum of taxation

6. This does not arise in the light of my decision that section 741 is applicable but I will briefly c The Appellant contended that having decided that the only transfer bringing the section into the transfer of the Old Majority Shares to International Holdings, the only income caught by the income which became payable to International Holdings on such shares. The remainder c income became payable to International Holdings by virtue of the transfer by someone else a accordingly, not relevant to taxing the Appellant.

7. I agree with this. The income which is potentially taxable on the Appellant is the income which ha payable to International Holdings as a result of the transfer by him of the Old Majority Shares whi power to enjoy by virtue of his holding of the New Majority Shares.

8. Mr Giles Goodfellow for the Appellant and Mr Rabinder Singh for the Revenue addressed me on th whether the dividends on these shares should be grossed- up.

9. Mr Singh contended that the income which the section deems to be income of the Appellant is the Section 743(2) provides that "in computing the liability to income tax of an individual chargeable section 739, the same deductions and reliefs shall be allowed as would have been allowed if the in to be his by virtue of that section had actually been received by him". It follows that the position i if the Appellant had actually received those dividends. They would be grossed-up by the amount c and he would be entitled to the benefit of the tax credit. The position is just as if International Hol never existed.

10. Mr Goodfellow contended that the income which was deemed to be the Appellant's was the net inc company from all sources after deduction of any reliefs which would have been available to an ind comparable position. The income lost its original characteristics and became charged under Sched As an example of why this approach was necessary, suppose that there were a trading loss and so investment income. If it were only the investment income which was attributed to the Appellant a could not be attributed because it was not income, the result was unjust. There was still scope for of section 743(2) in giving effect to reliefs which were available against total income. The effect of is that because International Holdings is not entitled to the tax credit, the income is not grossed u charged to income tax at the lower rate.

11. It is not necessary for me to decide this point but I find Mr Singh's approach more attractive parti precisely gives effect to counteracting the advantage of the transfer. I agree, however, with Mr Go this approach does not deal well with losses, but that does not arise in this case.

Further findings of fact

12. I am anxious, having regard to the history of this case, to avoid the need for the case to be r for further findings of fact if a court should disagree with any points of law which I have decid propose, therefore, to make findings of fact based on the items which the Revenue contend a operations. If one takes the transfer of the Old Majority Shares and all the items in paragraph Revenue contend are associated operations together, I would still find under section 741(b) t bona fide commercial transactions and were not designed for the purpose of avoiding liability The transfer was made for the reasons set out above and in coming to my conclusion I have account all the contemporaneous other transactions even though I had decided that they wer

associated operations.

13. The purchase of Mr Bassett's shares was a separate transaction caused by his leaving and was a c transaction not designed for the purpose of avoiding liability to taxation.

14. I find for the reasons given above, that the 1986 repurchase was a bona fide commercial transact the profit sharing arrangements to be rationalised and was not designed for the purpose of avoidi taxation. The Revenue's interpretation of the 1986 repurchase is that it was a prelude to enabling be paid by Holdings UK to International Holdings and thence to the Appellant. While the other sha remained as shareholders of International Holdings, the effect of paying a dividend was disadvant them because they would lose the tax credit attaching to the Holdings UK dividend since the divid international Holdings was a dividend from a non-resident company. This is an aspect of the arran is extremely well documented. In the light of my findings above, the purpose was not to enable di paid. None of the purposes of the 1986 repurchase was the avoidance of liability to taxation. My d the purpose of the transfer is not therefore affected by the inclusion of these later transactions.

15. If on the same basis I were applying paragraph (a) of section 741 and I need to find whether avoi taxation was one of the purposes of any of these transactions looked at separately, my findings ar brokerage sharing agreement was a commercial agreement without any tax avoiding purpose (no made on the arm's length nature of this agreement); the purchase of Mr Bassett's shares was a c agreement without any tax avoiding purpose; my finding in relation to the 1986 repurchase is in p above. One of the purposes of the employment arrangements with Personal Services looked at se order to obtain the remittance basis for the remainder of his remuneration from International Hold if they had not existed and International Holdings had paid all his remuneration that would have c foreign emoluments deduction; one of the purposes of the employment arrangements with Intern Holdings looked at separately was to obtain the remittance basis for his remuneration for non-UK context of the arrangements generally, particularly that International Holdings bore the whole of t remuneration, obtaining these tax benefits were not a tax avoidance purpose, but was tax mitigat are available to persons in the Appellant's circumstances and he was not misusing the reliefs.

Conclusion

16. I therefore find that the Appellant has satisfied the provisions of section 741(b) in relation to (and, if it had been necessary to decide, every operation alleged to be an associated operatio accordingly I allow the appeal.

J F AVERY JONES

SPECIAL COMMISSIONER

RELEASED 20th March 2000

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