INCOME TAX - Double taxation relief - Schedule D Case V - Whether income of a UK resident partner in a Jersey partnership from the partnership trade is exempt from UK tax as the commercial profits of a Jersey enterprise - Whether the result of the appeal is affected by the enactment of section 62 Finance (No.2) Act 1987, (now section 112 Income and Corporation Taxes Act 1988) - Section 497(1) Income and Corporation Taxes Act 1970 (now Section 788(3) Income and Corporation Taxes Act 1988)

THE SPECIAL COMMISSIONERS

MAURICE KEITH PADMORE (No.2) Appellant

- and -

THE COMMISSIONERS OF INLAND REVENUE Respondents

Special Commissioners: MR T H K EVERETT DR J F AVERY JONES CBE

Sitting in London on 23 May 2000

Mr Peter Whiteman QC instructed by Messrs Sharp Parsons Tallon, Chartered Accountants, for the Appellant

Mr Launcelot Henderson QC, instructed by the Solicitor of Inland Revenue, for the Respondents

DECISION

Maurice Keith Padmore ("Mr Padmore") appeals against the refusal by the Board of Inland Revenue of his claim to relief from income tax under section 788(3) of the Income and Corporation Taxes Act 1988 ("the 1988 Act") and paragraph 3 of the Arrangement scheduled to the Double Taxation Relief (Taxes on Income) (Jersey) Order 1952 (SI 1952 No. 1216) ("the Arrangement") for the years of assessment 1987-88 to 1998-99 inclusive. In this decision any reference to section 788(3) of the 1988 Act is to be taken in relation to the year of assessment 1987-88 as a reference to its statutory predecessor, namely section 497(1) of the Income and Corporation Taxes Act 1970 ("the 1970 Act").

The agreed question for our determination is whether the decision of the Court of Appeal in - Padmore v Commissioners of Inland Revenue - (1989) 62 TC 352 that

Mr Padmore was entitled to exemption from United Kingdom income tax in respect of a share of the profits of an independent Jersey commercial enterprise known as Computer Patent Annuities ("CPA") by virtue of what is now section 788(3) of the 1988 Act and Article 3(2) of the Arrangement is affected by the enactment of section 62 of the Finance (No.2) Act 1987, now section 112(4) and (5) of the 1988 Act.

There is no dispute as to the facts in this appeal. They are the subject of an agreed statement of facts which was the only relevant evidence. Three bundles of documents were produced at the hearing (two of which appeared after the conclusion of the hearing) but none of them was opened before us.

The facts

The agreed statement of facts reads as follows:

1. Mr Padmore is a partner in an independent commercial enterprise known as CPA which was established in Jersey on 1 April 1969. The background to the commercial undertaking of CPA is as follows. For the better protection of their property, the owners of inventions take out Letters Patent in many different countries. These have to be renewed from time to time, but the frequency with which they have to be renewed varies greatly from country to country; anything between one and twenty years. The same is true of the registration of Trade Marks and Designs. Many firms of Patent agents and Trade Mark agents provide a service to their clients, reminding them of the need to renew and effecting renewal if desired. Such a service is of limited value if it is not absolutely reliable and its provision is not a simple matter for Patent and Trade Mark practitioners.

2. CPA was accordingly established to carry on the business of furnishing a worldwide renewals service in connection with Letters Patent and (since 1976) Trade Marks and Designs and other equivalent forms of incorporeal property. Its clients are the owners of such property, and a number of them have been introduced to CPA by Agents who have discontinued their own renewals services.

3. CPA has throughout been a partnership (or, more accurately perhaps, a series of partnerships) and the Deed currently governing it is dated 1 October 1999. It (and indeed each of the preceding partnership Deeds) contains a clause declaring that it shall be construed in accordance with the laws of Jersey.

4. The partners in CPA are numerous: there are now 297 or more. All are either Chartered Patent Agents or Members of the Institute of Trade Mark Agents or the equivalent bodies in other jurisdictions, particularly Australia, New Zealand, Hong Kong and Singapore. 223 are partners or employees in various firms of Patent and Trade Mark Agents practising in the United Kingdom and are resident and domiciled in the United Kingdom for tax purposes. The business of CPA has, however, always been carried on from its offices in St Helier, Jersey, and its day-to-day business is dealt with by three managing partners who are Jersey residents. General meetings of the partners are held in Jersey (but nowhere else) four times a year, or more frequently as occasion demands. At those meetings, policy matters are discussed and the decisions taken are therefore implemented by the Jersey resident managing partners. It is common ground that the control and management of the business of CPA is situated abroad for the purposes of section 112 of the 1988 Act, previously section 153 of the 1970 Act.

5. Mr Padmore has been one of the CPA partners since 1 February 1976. He was for more than twenty years employed by a London firm of Chartered Patent

Agents at their Birmingham office, and he qualified as a member of the Institute of Trade Mark Agents in 1966. Since 1 April 1994, he has been a partner in that firm following a decision of the relevant professional bodies to allow their members to enter into a partnership with members of the other professional bodies. He has at all material times been resident in the United Kingdom.

6. Subject to paragraph 7 below, it is common ground that CPA has never done business through a permanent establishment in the United Kingdom.

7. On 1 August 1986, CPA acquired an 80% interest in the United Kingdom resident partnership which trades under the name Trade Marks Directory Service ("TMDS"). The business of TMDS is to provide a trade mark watching service to clients throughout the world. It operates from offices at 12 Cork Lane, London, EC1A 9RT (formerly Theba House, 49/50 Hatton Garden, London, EC1N 8YS). Management and control of TMDS is exercised in the United Kingdom. Its profits and income are assessed to United Kingdom income tax and are exempt from Jersey income tax under the provisions of the Arrangement. United Kingdom income tax was assessed on TMDS and paid by that Partnership in the years up to and including 1996/97. The proportion of assessable profits and income which is attributable to CPA was separately identified and was further distinguished as to the total amounts attributable to the United Kingdom resident and United Kingdom non-resident partners of CPA. In 1997/98, and subsequent years, individual partner details have been prepared and all partners, whether resident or non-resident, have self-assessed accordingly. It is common ground that the facts contained in this paragraph 7 have no relevance to the appeal before us.

8. By letters dated 10 November 1999 and 14 December 1999, Mr Padmore's accountants, Messrs Sharp Parsons Tallon, wrote to the international division of the Inland Revenue claiming on their client's behalf relief from United Kingdom income tax in respect of his share of the profits of CPA for the years of assessment 1987/88 to 1998/99 inclusive by virtue of section 788(3) of the 1988 Act and paragraph 3(2) of the Arrangement. That claim was refused by Mr Waters of international division on behalf of the Board of Inland Revenue by letter dated 19 January 2000; and it is against that refusal that Mr Padmore now appeals.

9. On 19 May 1989, the Court of Appeal unanimously held affirming the decision of Peter Gibson J (as he then was) that Mr Padmore was entitled to exemption from income tax under section 497 of the 1970 Act and paragraph 3 of the Arrangement in respect of his share of the profits of CPA for the years of assessment 1975/76 to 1981/82 inclusive.

10. Subject to paragraph 7 above, the facts upon which the Court of Appeal reached its decision in - Padmore - are in all material respects precisely the same as those which apply to the present appeal. Thus, the facts set out in paragraphs 1-6 above constitute the entirety of the facts upon which the Court of Appeal reached its decision, updated as and where necessary to take account of events occurring since that decision: see in particular 62 TC 352 at pages 355-356. Such events together with the facts set out in paragraph 7 above, do not affect the essential factual basis upon which the Court of appeal reached its decision.

11. In accordance with the decision of the Court of Appeal in - Padmore - , a number of further matters are now common ground between the parties. Those matters are set out below, together with the appropriate reference in the report where the authority for the relevant statement is to be found:

(a) there is no difference of substance between the relevant taxation law in the United Kingdom and in Jersey (page 374H)

(b) CPA as a partnership which is controlled and managed in Jersey is resident in Jersey for the purposes of Jersey tax and income tax is assessed and paid there in the firm's name accordingly (pages 357E, 374I, 378A and C and 382B).

(c) As a matter of Jersey law, CPA is a partnership and as such is a "body of persons" within the meaning of the Arrangement (pages 377D and 381E).

(d) CPA is not resident in the United Kingdom for the purposes of the United Kingdom tax and subject to paragraph 7 above has never done business through a permanent establishment in the United Kingdom (pages 377G and 382I).

(e) CPA is accordingly a resident of Jersey and not a resident of the United Kingdom for the purposes of the Arrangement (page 377G to page 378E).

(f) CPA carries on a commercial undertaking for the purposes of the Arrangement and the profits in question are accordingly commercial profits for those purposes (page 376F).

(g) The share of profits to which a partner of CPA is entitled constitutes "commercial profits of a commercial enterprise or undertaking carried on by a resident of Jersey" and is thus within the terms of article 3(2) of the Arrangement (page 380C to F and page 383F).

12. By the same letters to international division dated 10 November 1999 and 14 December 1999, Messrs Sharp Parsons Tallon also claimed on behalf of certain other United Kingdom resident partners of CPA ("the Participating Partners") relief from United Kingdom income tax in respect of their respective shares of profits of CPA for the years of assessment 1987/88 to 1998/99 inclusive. Those claims were also refused by Mr Waters of international division on behalf of the Board of Inland Revenue in the same letter dated 19 January 2000. It has been agreed by each of the Participating Partners and the Board of Inland Revenue that the final decision in relation to this appeal of Mr Padmore will be applied to the outstanding appeals of each of the Participating Partners for all the years of assessment in dispute.

The contentions of the parties

Both Mr Whiteman and Mr Henderson submitted written skeleton arguments which will be available to the Court should this appeal proceed further. It is therefore necessary only for us to summarise briefly each party's contentions.

The main plank of Mr Whiteman's argument is that section 788(3) of the 1988 Act overrides the provisions of section 112(4) of the same Act. The result is that tax treaties have effect "notwithstanding anything in any enactment" but this provision is itself "subject to the provisions of this Part". Therefore, he argued, the only way to override a tax treaty by legislation was to put the legislation in Part XVIII of the Act. An example of such a provision can be seen in the decision of Vinelott J (this point was not appealed) in - Sun Life Assurance Company of Canada v Pearson - [1984] STC 461 at 516c, although neither side referred us to this decision. Because a provision of Part XVIII gave double taxation relief only to a resident, a treaty non-discrimination provision giving relief to the permanent establishment of a non-resident was ineffective, because it took effect subject to

the restriction in Part XVIII that only residents were entitled to relief. However, Mr Whiteman accepted that specific legislation not contained in Part XVIII would be effective if that were clearly the intention of Parliament. He distinguished - IRC v Collco Dealings Ltd - (1962) 39 TC 509 and - Woodend (KV Ceylon) Rubber and Tea Co Ltd v Ceylon Commissioner of Inland Revenue - [1971] AC 321.

He also characterised the Inland Revenue's attempt to rely on a statement by Mr Norman Lamont in the debates on the Finance Bill on second reading on 15 July 1987 as reported in Hansard as "entirely misconceived" and "an improper use of the relaxed rule introduced by - Pepper v Hart - (1992) 65 TC 421".

Mr Henderson's main argument for the Commissioners was that the clear purpose of section 62 of the Finance (No.2) Act 1987 (consolidated as section 112(4) and (5) of the 1988 Act) was to reverse the decision of the High Court in - Padmore - and to override the provisions of the Arrangement (and other double taxation agreements in similar form) insofar as they would otherwise relieve from UK income tax or CGT a UK resident partner share of the income or capital gains of a non-UK resident partnership. In Mr Henderson's submission the language of section 62, on its true construction, achieved its purpose clearly and unambiguously; but again if there was any doubt on the point, Hansard resolves it in the Revenue's favour.

Mr Henderson placed reliance upon - Collco - and upon - Woodend. - He placed particular reliance upon - Woodend - as he pointed out that the section of the Double Taxation (Relief) Act of 1950, which gave the force of law in Ceylon to the 1950 UK/Ceylon double taxation agreement, did so "notwithstanding anything in any other written law", (although this fact is not mentioned in the judgment of the Privy Council).

Mr Whiteman's reply was brief, as forewarned as to the main points of the Inland Revenue's case by Mr Henderson's skeleton argument which had been made available to Mr Whiteman in advance of the hearing, he had dealt with most of those arguments in his opening.

The legislation

Section 497(1) of the 1970 Act where relevant reads as follows:

"497. Relief by agreement with other countries

(1) If Her Majesty by Order in Council declares that arrangements specified in the Order have been made with the Government of any territory outside the United Kingdom with a view to affording relief from double taxation in relation to income tax or corporation tax and any taxes of a similar nature imposed by the laws of that territory, and that it is expedient that those arrangements should have effect, then, subject to the provisions of this Part of this Act, the arrangements shall, notwithstanding anything in any enactment, have effect in relation to income tax and corporation tax insofar as they provide -

(a) for relief from income tax, or from corporation tax in respect of income, or

Section 62 of the Finance (No. 2) Act 1987 provides as follows:

"Provisions having an overseas element

62.-(1) At the end of section 153 of the Taxes Act (Partnerships Control Abroad) there shall be added the following subsections

(4) In any case where -

(a) a person resident in the United Kingdom (in this subsection and subsection (5) below referred to as "the resident partner") is a member of a partnership which resides or is deemed to reside outside the United Kingdom, and

(b) by virtue of any arrangements falling within section 497 of this Act (Double Taxation Relief) any of the income or capital gains of the partnership is relieved from tax in the United Kingdom,

the arrangements referred to in paragraph (b) above shall not affect any liability to tax in respect of the resident partner's share of any income or capital gains of the partnership.

(5) If, in a case where subsection (4) above applies, the resident partner's share of the income of the partnership consists of or includes a share in a qualifying distribution, within the meaning of Part V of the Finance Act 1972, made by a company resident in the United Kingdom, then, notwithstanding anything in the arrangements, the resident partner (and not the partnership as a whole) shall be regarded as entitled to that share of the tax credit in respect of the distribution which corresponds to his share of the distribution"

(2) Nothing in subsection (1) above affects -

(a) the determination of any Commissioners or the judgment of any court made or given before 17th March 1987, or

(b) the law to be applied in proceedings on appeal to the Court of Appeal or the House of Lords where the judgment of the High Court or the Court of Session which is in issue was given before that date,

but, subject to that, the amendment made by subsection (1) above shall be deemed always to have been made."

Conclusions

We will deal first with the attempt by the Crown in this appeal to rely upon an extract from Hansard.

In our judgment we accept Mr Whiteman's contention that the attempt by the Crown to introduce reference to Parliamentary material is misconceived in this instance.

In - Pepper v Hart - Lord Browne-Wilkinson said at page 483G:

"In my judgment, subject to the question of the privileges of the House of Commons, reference to Parliamentary material should be permitted as an aid to the construction of legislation which is - ambiguous - or - obscure - or the literal meaning of which - leads to an absurdity." - (Our emphasis).

On our understanding it is common ground in this appeal that neither the Appellant nor the Respondents contend that the words used in section 62(4) are ambiguous or obscure or that their literal meaning leads to an absurdity. Accordingly we hold that in this appeal there is no basis for the introduction and reliance upon Parliamentary material.

We are left therefore with the question of whether section 497(1) overrides section 62(4).

It is trite law and common ground in this appeal that Parliament cannot bind its successors and therefore it was open to Parliament if it so wished to negative the effect of section 497(1) of the 1970 Act as construed by the Court of Appeal in - Padmore - . The question is was Parliament's attempt effective?

In our judgment it was, despite Mr Whiteman's well argued case before us. While legislation contained in Part XVIII undoubtedly overrides a tax treaty, this says nothing about the legislation in question which is not contained in that Part. This must depend on the intention of Parliament in enacting section 62. That provision clearly deals with the case of a United Kingdom resident partner in a non-resident partnership and states unambiguously that a tax treaty shall not affect any liability to tax in respect of the resident partner's share of any income or capital gains of the partnership.

If Mr Whiteman is correct, the only possible result is that section 62 and its successor are of no effect whatever. Such a state of affairs can sometimes exist, as was demonstrated in - IRC v Ayrshire Employers Mutual Assurance Association Ltd - (1946) 27 TC 331 but such failures by the legislature are rare and we do not believe that an example of such a failure can be found in the present appeal.

It is abundantly clear from section 62(2) that the legislature planned to overturn the decision of the Court of Appeal in - Padmore - for the future and in our judgment we hold that its attempt was successful.

The appeal fails and as this is a test case properly so called the effect of Mr Padmore's failure before us will impact upon the other partners of CPA in accordance with paragraph 12 of the statement of facts above.

We adjourn this hearing to enable the parties to agree figures and on their being reported to us we will formally determine the assessments.

T H K EVERETT

DR J F AVERY JONES CBE

SPECIAL COMMISSIONERS

Released 21st June 2000

SC 3023/00

Authorities cited but not mentioned in the decision

- Chevron UK Ltd & Others v CIR - [1995] STC 712

- Penang and General Investment Trust Ltd & Ramsden v IRC - (1943) 25 TC 219

- Commissioners of Inland Revenue v Joiner - (1975) 50 TC 449

- Farrell v Alexander - [1977] AC 59

- NAP Holdings UK Ltd v Whittles - (1994) 67 TC 166

- Fleming v Associated Newspapers Ltd - (1972) 48 TC 382

- Restorick v Baker - (1971) 47 TC 116

- Salomon v Customs and Excise Commissioners - [1967] 2 QB 116

- R v Secretary of State for the Home Department, ex parte Brind - [1991] AC 696