TC08018

Appeal number: TC/2018/01677, TC/2018/07905, TC/2018/07907, TC/2018/07909, TC/2019/03678, TC/2019/03679, TC/2019/03680, TC/2019/03689, TC/2019/03691 TC/2019/03692, TC/2019/03693, TC/2019/03694, TC/2019/03695, TC/2019/03696, TC/2019/03698, TC/2019/03699, TC/2019/03722, TC/2019/03725, TC/2019/03726, TC/2019/03729

INCOME TAX – tax effects of a partnership incentive plan - whether the appellants are taxable on sums allocated to a corporate member of Odey Asset Management LLP in the year of allocation – no – whether the appellants are taxable on sums received on reallocation of special capital to them in the year of receipt under s 687 ITTOIA 2005 (miscellaneous income) – yes – or under ss 773 to 778 ITA 2007 (sales of occupational income) – no – whether an amendment and various discovery amendments were made validly under s 29 and 30B TMA – appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

ODEY ASSET MANAGEMENT LLP — **Appellants**

FERAS AL-CHALABI

RALPH BECKETT

TIMOTHY BOND

ROBERTO CERVESI

RAJESH CHAUDHARY

DAVID FLETCHER

JAMES GRIMSTON

JAMES HANBURY

BRUCE HUBBARD

BENJAMIN LAMBERT

ORLANDO MONTAGU

TIMOTHY PEAREY

MICHELE RAGAZZI

MASSEY ROBOROUGH

ANDREW SANDLER

DAVID STEWART

JULIAN WOLFSON

- and -

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

TRIBUNAL: JUDGE HARRIET MORGAN

Sitting in public at Taylor House, 88 Rosebery Avenue on 15 to 20 July 2019

Mr David Goldberg QC, as instructed by Macfarlanes LLP, as Counsel for the Appellants

Mr Thomas Chacko and Mr James Kirby, as instructed by the General Counsel and Solicitor to HM Revenue and Customs, as Counsel for the Respondents ("HMRC")

DECISION

1. These appeals concern the tax consequences of arrangements operated by Odey Asset Management Limited ("**Odey**" or "**the Partnership**") during the 2011/12 to 2015/16 tax years for the remuneration of the members of Odey ("**the Members**") including the other appellants ("**the Plan**"). At all relevant times Odey carried on an investment fund management business.

2. In outline, under the arrangements Odey adopted a remuneration policy ("**the Remuneration Policy**") under which, for each relevant tax year, a proportion of Odey's profits which could otherwise have been allocated to and received by certain of the individual Members in that year were subject to a "deferral" mechanism whereby those Members could receive them only over two to three years if certain conditions were satisfied. I refer to the total sum of such profits for each tax year as "**the deferred share"** and the proportion of the deferred profit share "awarded" to each relevant Member as "**an individual share**":

(1) In each relevant tax year, Odey calculated and paid the individual shares to a corporate member of Odey, Partners Special Capital Limited ("**PSCL**"), which was specifically set up to play its role in the Plan and had no other purpose.

(2) Odey made recommendations to PSCL that it should exercise the discretionary powers given to it in the agreement governing the relations between the Members to (a) contribute each individual share "awarded" to each specified Member to Odey as "Special Capital" on the basis that Odey would invest that share in the Fund which the relevant Member managed, and (b) reallocate the Special Capital referable to each individual share to the named Member on specified dates over a two or three year period subject to the satisfaction of certain conditions in the Remuneration Policy on the basis that, following any such reallocation, the Members could withdraw the monies referable to the Special Capital from Odey.

(3) In all cases, PSCL acted in accordance with the recommendations made by Odey and, on having received a reallocation of Special Capital, the relevant Members withdrew the related monies from Odey.

3. The appellants' stance is that the individual Members are not subject to income tax (a) on the individual shares "awarded" to them in the tax year in which they were calculated and paid to PSCL and they were notified of the "award" ("**the year of allocation**"), or (b) on the funds they received when the Special Capital referable to the individual shares was later reallocated to them in the tax year of receipt ("**the year of receipt**").

4. HMRC said that, on the contrary:

(1) adopting a purposive approach to the construction of the relevant legislation, on a realistic view of the facts, each Member is subject to an upfront income tax on the individual share "awarded" to him in the year of allocation under s 850 of the Income Tax (Trading and Other Income) Act 2005 ("**ITTOIA**") (relating to the allocation of partnership profits); and

(2) alternatively, each Member is subject to income tax on the sums received when the Special Capital was allocated to him (a) under s 687 ITTOIA (relating to miscellaneous income), or (b) under ss 773 to 778 of chapter 4 of part 13 of the Income Tax Act 2007 ("**ITA**") (relating to the sale of occupation income).

5. The appeals are made in respect of a mixture of (a) amendments made by HMRC to the appellants' tax returns on the issue of closure notices, and (b) the issue of discovery assessments under s 29 of the Taxes Management Act 1970 ("**TMA**") and an amendment to Odey's partnership tax return for the tax year 2011/12 under s 31B TMA. As set out in Part E, the appellants argue that the discovery assessments and the partnership tax return were not validly made for a number of reasons.

6. The tribunal is asked only to consider whether there is in principle any additional income liability on the relevant Members and not to consider the amount of the liability. In summary, I have concluded that:

(1) For all the reasons set out in Part B, the appellants are not subject to income tax in the year of allocation on the individual shares "awarded" to them in that year (or by reference to any sums paid to them when in later years Special Capital was reallocated to them).

(2) For all the reasons set out in Parts C and D respectively:

(a) the appellants are subject to income tax in the year of receipt on the sums paid to them following the reallocation of Special Capital to them in that year under the provisions of s 687 ITTOIA,

(b) the appellants are not subject to income tax in the year of receipt on such sums under ss 773 to 778 ITA.

(3) For all the reasons set out in Part E, the amendment issued to Odey in respect of the tax year 2011/12 and the discovery assessments issued to Mr Fletcher and Mr Stewart in respect of the 2011/12 tax year and to Mr Feras Al-Chalabi, Mr Bruce Hubbard and Mr Pearey for the tax year 2013/14 are invalid.

Part A – Facts and Evidence

7. I have based the facts found in this section of the decision on (a) the documents contained in the bundles produced to the hearing, and (b) the evidence given by Mr Odey, Mr Pearey, Mr Stewart and Lord Roborough who attended the hearing and were cross-examined. I found them to be honest and credible witnesses and their evidence is accepted except where stated to the contrary. Their roles at Odey are described below.

Implementation and operation of the Plan

Implementation of the Plan – setting up PSCL

8. On 16 February 2011, a declaration of trust was executed by Ogier Trustee (Jersey) Limited which established a trust under Guernsey law named "The Partners Special Capital Business Purpose Trust" with the following express purpose:

> "to further the business of the Odey Asset Management Group, through holding and retaining shares in a single company incorporated in England and taking all reasonable endeavours to ensure that this company contributes all its profits, after tax and expenses to [Odey] as a special capital contribution".

9. On 17 February 2011, PSCL was incorporated in England to act as the vehicle referred to in the declaration of trust.

10. On 1 March 2011, Ogier Trustee (Jersey) Limited wrote to PSCL and stated that it would support decisions made by the directors of PSCL in order to promote the purpose set out in the declaration of trust.

11. On 2 March 2011, the directors of PSCL decided at a board meeting:

(1) to allot the entire issued shareholding in PSCL to Ogier Trustee (Jersey) Limited;

(2) that its proposed activity was to use any profits allocated to it by Odey, after paying expenses and taxes, to contribute to the capital of Odey via a special capital contribution account and to acquire shares in funds managed by the Odey group or shares in Odey Holdings AG (or such other assets as may be agreed from time to time), to transfer such shares after providing for relevant taxes and expenses to Odey (or to dispose of such shares and to contribute any cash generated by such disposal) on the basis that the reallocation of capital "will be upon consideration of recommendations from Odey's Remuneration Committee, which executes Odey's Remuneration Policy"; and

(3) to fulfil this activity by becoming a partner of Odey.

Remuneration Policy

12. On 17 March 2011, Odey introduced the Remuneration Policy and appointed a remuneration committee ("**RemCom**") to oversee the Remuneration Policy, which comprised the founder of Odey, Mr Odey, and two other members of the management team, Mr Fletcher and Mr Stewart (until his resignation as a member of Odey in 2012). The Remuneration Policy provided for two types of awards to be made to members, which I refer to as "**the Cash Award**" and the "**the Share Award**" and together as "**the Awards**".

13. On 30 March 2011, Odey sent PSCL a copy of the Remuneration Policy "for your consideration". Odey noted that the document had been produced in response to the remuneration code of the Financial Service Authority ("**FSA**") and that RemCom would like the directors of PSCL to consider its application when determining the potential reallocation of capital to partners of Odey.

14. The initial Remuneration Policy was "adopted" by PSCL by written resolution of its directors on 5 April 2011.

15. The Remuneration Policy was updated on 31 May 2011 and was "adopted" formally by PSCL by written resolution of its directors on 3 February 2012. The Remuneration Policy remained in this form until 23 January 2014 when it was revised again, but not to any material extent for the purposes of these proceedings.

16. The Remuneration Policy dated 31 May 2011 included the following:

(1) In the background section, details were set out of the introduction of the FSA's Code.

(2) "The remuneration structure is designed to attract, motivate and retain the best people to ensure good performance for the underlying investors in Funds, which in turn achieves success for the firm. The following sets out elements of the structure of the Remuneration Policy, including annual profit allocation/bonus awards, deferred profit allocation/bonus awards and annual drawings/base salary. However, <u>it is not intended that this award process, including deferral arrangements, should be contractual</u>."

(3) "[RemCom] determines performance related remuneration based on a number of factors. It is very hard to set Fund performance targets, given the volatile nature of markets, but as a general default position, Fund Managers can expect to receive half of any crystallised performance fees generated by the Fund they manage……"

(4) "Valuable focus is achieved through clear profit allocation/bonus targets. However, unduly narrow motivation to hit a specific target on a particular date can encourage excessively blinkered behaviour, which is negative for other business goals before/after the target date – eg in relation to risk taking, broader business development, long term sustainability; franchise value."

(5) "A 100% payout on a particular date is also directly bad for business continuity. The development of participants and their associated business tends to take place over a period of years; whereas a single profit allocation/bonus payment date means massive short term volatility in the retention incentive."

(6) "Profit allocation/bonus deferral is intended to help offset these disadvantages of particularly large single date profit allocation/bonus awards; without excessively de-motivating participants."

(7) It was explained that there were two types of "deferral", namely "Cash deferral" and "Share deferral".

(8) It was set out that:

(a) Cash Awards related to the following percentages respectively of "cash profit allocation/bonus" (i) 20% between £500,000 and £1 million, (ii) 25% between £1 million and £1.5 million, (iii) 30% between £1.5 million and £2 million, and (iv) 35% above £2 million. In the initial policy there was provision only for 35% of any cash profit allocation/bonus greater than £20 million.

(b) It was stated that the relevant sums would be "deferred" over two years and paid in two equal instalments on the first and second anniversaries on the basis that the cash was required to be invested in Funds managed by Odey and that the Cash Award would be lost if the Member was not a partner/employee at the "transfer date" but "thereafter inalienable".

(c) It was explained that such "deferred cash awards" strengthened "the alignment of interests between partners and our clients and fund investors, especially for partners responsible for performance. Requiring partners to "eat what you cook" further encourages a responsible attitude to risk taking".

(d) There was a note applicable to both Cash and Share Awards that the "payment of deferred cash and vesting of deferred shares is subject to the firm's ability to make such payments/vesting without limiting the firm's ability to strengthen its capital base when necessary. These figures are gross of tax".

(e) It was stated that Mr Odey "is the only partner exempt from the deferral process. He has motivation enough to remain at his own firm, as the firm's founder and majority shareholder".

(9) It was explained that Share Awards related to "bonus shares awarded in Odey Holdings AG" and that an "award" of such bonus shares:

> "allows for increased ownership in the business by partners. In determining the award of shares, [RemCom] takes into account a partner's contribution to the overall development of the business and creation of a long term sustainable franchise. To this end, the deferred vesting of bonus shares is over a three year period in which the shares are entitled to a dividend on the 1st/2nd/3rd anniversaries, but will be surrendered should the partner leave within the three year period. The Bonus Shares become Ordinary Shares with inalienable rights, after the third year, ie the partner keeps the shares should he leave. The subsequent sale of the shares by that partner follows the pre-emption rights as detailed in the shareholder agreement.

> All forms of deferral help to manage the key man risk as the retained element acts as a disincentive to leave and short notice and encourages behaviour based on creating a sustainable business."

(10) It was noted that RemCom is a subcommittee of Odey's Executive Committee ("**ExCo**") and that it would review the policy at least annually or as and when there are significant changes and that whilst RemCom is the "final arbiter in deciding deferral terms (including how deferred funds are invested)", the position set out above:

> "represents the default position; meaning any substantial variation will need justification, or agreement between the partner concerned and [RemCom]. The firm is too small to warrant an independent remuneration committee, nor does the RemCom report to another Board as the members of RemCom comprise of the three most senior partners."

(11) It was stated that: "In all cases deferred amounts will only be payable to the extent the firm has sufficient regulatory capital."

(12) It was explained how the Remuneration Policy complied with the applicable principles/rules in the FSA's remuneration code. These comments included the following:

(a) Under "Risk Management": "...Key man risk is a significant issue for the business but the use of a deferral mechanism helps incentivise key members to stay. Furthermore, the fact that the cash element of the deferred amount is re-invested into Funds managed by [Odey] ensures continued alignment of shareholders interest with those involved in managing the Fund."

(b) Under "Business Strategy": "The deferral element of the cash profit allocation and Bonus Shares encourages long term continuity over short term gain."

(c) Under "Capital": "In all cases variable and deferred amounts will only be payable to the extent the firm has sufficient capital."

(13) It was noted that the policy was drafted by Mr Pearey with input and critical scrutiny from senior management, particularly Mr Fletcher and Mr Stewart and that it was finally scrutinised and approved by RemCom on 31 May 2011.

(14) There was a list at the end of the Remuneration Policy of the Members "to whom the Remuneration Policy will apply".

17. I note that it is plain from the Remuneration Policy that Cash Awards were to be determined by RemCom (a) first deciding on the total "cash profit allocation/bonus" which a Member should receive according to his performance, and (b) applying the specified thresholds to determine the proportion of that amount to be allocated as the individual share which was subject to the Plan. However, the Remuneration Policy does not set out any equivalent procedure for determining the Share Awards. At the hearing Mr Odey said that he thought that there was a system for determining Share Awards and that about 35% of the profit allocation the Member would otherwise have received sounded about the right number. On the other hand, Mr Stewart said that the Share Awards were not based on any specified percentage and were entirely discretionary.

Agreement governing Odey

18. On 29 March 2011, a new agreement governing the LLP was adopted ("**the 2011 LLP Agreement**") which contained the material provisions set out below.

19. Odey's business was stated to be "to carry on the business of (1) managing and/or advising on investments; (2) marketing; (3) activities associated therewith; and (4) such other activities as [ExCo] may determine from time to time" (under clause 5). Under clause 8, subject to specified limited exceptions, ExCo was responsible for the management and control of the business and the affairs of Odey.

20. As regards contributions of capital:

(1) Under clause 10.1 Members were required to make ordinary capital contributions, as set out in a schedule, which represented the maximum amount which each Member was liable to contribute to the assets of the Partnership for the purposes of s 74 of the Insolvency Act 1986.

(2) Under clauses 10.4 and 10.5, if Odey required further funding, ExCo could make a call for ordinary capital and, if a Member (other than PSCL) did not comply with the request, ExCo could request all the other Members who had complied with the call to make further ordinary capital contributions pro rata to such Members' capital share on the date of the request.

(3) Under clause 10.12A headed "Contribution of Special Capital" it was provided that:

(a) any of the Members "may with the agreement of [ExCo] at any time make further contributions to the Partnership" which were not to comprise ordinary capital, in cash or in specie as Special Capital. Any such amount was to be credited to the relevant Member's Special Capital account and was subject to provisions as to reallocation and withdrawal set out in clause 10.12A;

(b) any such Special Capital "may, at the discretion of ExCo, be invested and reinvested by the Partnership in such assets …as [ExCo], in its sole and absolute discretion, may determine"; and

(c) any income arising or derived from monies in the Special Capital account or from assets in which such monies were invested and any income losses derived therefrom were stated to form part of the income profits or income losses of the Partnership which were to be allocated amongst the Members in accordance with clause 12.2 and 12.3.

21. As regards the reallocation and withdrawal of Special Capital:

(1) Under clause 10.12B headed "Reallocation of Special Capital" it was provided that:

> "…following receipt of a recommendation from [ExCo] that such member should consider reallocation of such interest in such Special Capital, any Member who for the time being has any Special Capital contribution credited to his Special Capital Account may, in his sole and absolute discretion, decide that all or any part of the interest of such Member in any Special Capital….should be reallocated to any other such Member or Members so that such Member or Members will, following such reallocation, acquire his interest in the relevant part of such Special Capital….and shall give notice of any such decision to [ExCo] (provided that no such reallocation shall be made by any such Member prior to the expiry of twelve months following the date upon which the Special Capital was initially contributed…unless [ExCo] shall specifically consent to a period of less than twelve months in writing.)"

(2) The amount of any Special Capital reallocated was deemed to be transferred to the relevant Member and debited from the Special Capital Account of the transferor and credited to the Special Capital Account of the transferee.

(3) Under clause 11.12C headed "Withdrawal of Special Capital" it was provided that any Member who had Special Capital credited to his account "may (in the case of PSCL with the prior consent of [ExCo] but subject always to the Law) withdraw all or part of such Special Capital" on giving notice. On expiry of the notice period, the amount to be withdrawn was stated to become a debt due and payable by Odey.

22. Clause 12 headed "Allocations of Income Profits" contained the following provisions of relevance:

(1) Under clause 12.1, ExCo was to determine the allocation of profits among the Members in accordance with the provisions of clause 12.2, including a final allocation following the end of each financial year by reference to a draft of the Partnership Accounts drawn up on respect of that year, after having, in good faith, made appropriate allowance to satisfy certain expenses and the obligation imposed on the Partnership by any regulatory body to maintain a minimum level of financial resources.

(2) Under clause 12.2 the income profits of the Partnership in respect of each financial year were to be allocated amongst the Members as follows:

(a) first, to Odey Asset Management Group ("**OAMG**"), in an amount equal to the interest on its ordinary capital contribution to Odey of £3 million at a fixed rate of 5% (subject to variation by mutual agreement). OAMG is an Odey group company and a member of Odey that provides support services to different entities within the Odey group;

(b) second, to OAMG in a sum equal to all amounts due to cover any service charge or equivalent payable by Odey to OAMG;

(c) third, to each of the Members of such fixed sums (if any) as may be been agreed (from time to time) between each of the Members and ExCo; and

(d) fourth, "the remainder of the profits, if any, shall be allocated amongst the Members in such proportions as [ExCo] may, in its sole discretion, determine".

23. Provisions relating to the departure of Members and winding-up of Odey included the following:

(1) Under clause 19 ExCo could remove a Member from Odey if they concluded that it would be in the best interests of Odey to do so and on serving a notice on the Member. ExCo could also remove a Member in a number of stated circumstances including where the Member was in serious or persistent breach of the agreement, the Member was guilty of misconduct or neglect, the Member failed to make a further ordinary capital contribution in full when called on to do so as set out above, an individual Member had a bankruptcy order against him or reached 65 or retired or died.

(2) Under clause 20, Members could resign from Odey on giving three months' notice.

(3) Under clause 25, Odey could be wound up on a determination by Members holding 75% of the capital shares or if an event occurred which made it unlawful for Odey to continue. It was provided that:

(a) "Save as required by law, no Member shall have any personal liability for the debts or obligations or losses or liabilities of the Partnership beyond their "Maximum Amount". If the Partnership is wound up, no Member or former Member shall be liable to contribute further to the assets of the Partnership."

(b) If the liquidation of the Partnership was conducted as a member's voluntary winding up in accordance with the Insolvency Act 1986, (i) the members were entitled to be allocated profits of the Partnership for the period from the start of the relevant financial year to the date of the resolution for the winding up, (ii) the assets remaining after paying liabilities were to be applied first in repaying £3 million to OAMG and then in returning to the members the sums standing to the credit of their ordinary capital accounts, (iii) any remaining assets were to be applied so that an amount equal to the aggregate of all Special Capital credited to the special capital accounts of all of the members (unless already subject to a notice of withdrawal) was to be distributed amongst the members in such proportions as "[ExCo] shall in its absolute discretion decide and notify to the liquidator provided that if [ExCo] shall not give any such notification within one month of being called upon to do so by the liquidator then such amounts shall be distributed amongst the Members in the same proportions as their respective Ordinary Capital contributions as at the date of dissolution or winding-up bore to the Ordinary Capital contributions of all Members at that time", and (iv) finally any remaining assets were to be distributed among the members pro rata to their respective Capital Shares.

Overview of the Award process

24. During the relevant period Cash and Share Awards typically operated as follows.

(1) In January of each year, RemCom met (a) to calculate Odey's provisional profit for the previous calendar year on considering the initial accounting figures and performance fee calculations and (b) to determine for each Member (i) his profit share for the relevant period for immediate receipt and (ii) any individual share to be allocated to PSCL and dealt with under the terms of the Remuneration Policy.

(2) As set out in the Remuneration Policy, RemCom worked out these two sums by (a) deciding on an overall notional profit allocation for the Member based on his performance in his role for Odey in the relevant period, and (b) applying the specified thresholds and percentages set out in the policy to divide this overall sum into its two constituent parts.

(3) The minutes of the meeting of RemCom recorded that Odey would make "a profit allocation" to PSCL of a sum equal to the aggregate of all individual shares comprising the "proposed cash deferred amounts set out by each Member's name" with a further recommendation that "the deferred cash (net of Corporation Tax) should be invested in [specified] Funds" under management by Odey in relation to each Member. It was also noted that RemCom would advise the directors of PSCL of this proposed split amongst the Members and potential reallocation by PSCL to those Members, "at the sole discretion of the Directors of PSCL and upon satisfaction of conditions as outlined in the Remuneration Policy".

(4) Following this (or around this time):

(a) RemCom notified ExCo that the deferred share decided on in the January meeting had been allocated to PSCL and that the "deferred cash will be reinvested (net of Corporation Tax) by PSCL into Funds managed by the Odey Group".

(b) Odey wrote to Members notifying them that (i) they "had been allocated a share of the Partnership income" in respect of the previous calendar year, (ii) "[i]n accordance with the deferral arrangements in the Remuneration Policy, the [individual share] will be invested, net of Corporation tax … in [Odey] Funds by [PSCL]", and (iii) the "deferral arrangements are subject to PSCL's policies and discretion, and PSCL will confirm the details to you in March". I note that the wording of these letters in some years contained differences which HMRC consider to be material to the correct analysis of the tax effect of the Plan as set out in Part B below.

(c) Odey wrote to PSCL to notify it of the allocation of the deferred share to it and stated that "[f]or the consideration of PSCL, [RemCom] proposes the following breakdown of this allocation and subsequent investment (net of Corporation Tax) which, in accordance with the Remuneration Policy, could be re-allocated to partners upon satisfaction of certain conditions", and the proposed breakdown was set out in a table showing the individual share for each specified Member and the Fund that individual share was to be invested in.

(5) Shortly after receiving Odey's letter, the directors of PSCL adopted a written resolution whereby it:

(a) acknowledged receipt of the allocation of the deferred share decided upon at the meeting of RemCom held in January;

(b) agreed to the potential allocation of awards to Members as detailed in the letter it had received from RemCom;

(c) agreed to retain sufficient funds to pay corporation tax on the deferred share and to reinvest the remainder in Odey Funds; and

(d) authorised Mr Odey to sign letters to the Members "confirming the Remuneration Policy and any potential awards that maybe [sic] made to [them]".

(6) In accordance with the above process, in each relevant year PSCL contributed the deferred share to Odey as Special Capital under clause 10.12(A) of the 2011 LLP Agreement. The contribution was credited to PSCL's Special Capital account and invested in Funds under management by Odey as shown in the breakdown prepared by RemCom.

(7) Usually in March of each year, once the final financial results for the previous calendar year had been determined, RemCom met to consider how to allocate any additional profit to that calculated and dealt with at the meeting in January. In most periods it decided that a proportion of these profits would be used to make Share Awards. Under the same procedure as set out in relation to Cash Awards, Odey paid the aggregate of any individual shares relating to Share Awards to PSCL but, in this case, RemCom recommended that PSCL should use the funds to purchase shares in OHAG, PSCL contributed the relevant sums to Odey as Special Capital and the monies were invested in shares in OHAG which Odey held as legal owner.

(8) Usually in March or April of each relevant year, PSCL wrote to Members to confirm the amount of their individual shares and to notify them that they would be paid the monies in respect of those shares, as regards Cash Awards, in two equal instalments over the next two years and/or, as regards Share Awards, in three equal instalments over the next three years. In the letters, PSCL also stated that:

(a) the steps set out above had been carried out;

(b) PSCL had received RemCom's letter(s) regarding the Awards and it:

> "will take this initial recommendation into account (and any further recommendations it may receive from time to time) when exercising its discretion over reallocations of [Special Capital]. For the avoidance of doubt, please note that PSCL is not bound by any such recommendation, that PSCL retains absolute discretion over reallocation of [Special Capital] and that you may not receive a reallocation…
>
> any recommended reallocations will not be made in your favour where you are not a member of [Odey] at the relevant reallocation date, other than at the absolute discretion of PSCL….
>
> it is unlikely that a reallocation of [Special Capital] will be made unless [Odey] retains sufficient Regulatory Capital, or in the event of the insolvency of [Odey], as the [Special Capital] will be available to satisfy any outstanding liabilities of [Odey]."

(9) In February or March of each subsequent year, Odey informed PSCL which of the Members remained members of Odey and confirmed that Odey had sufficient regulatory capital for the foreseeable future.

(10) In or around March and/or April of each relevant subsequent year, the board of directors of PSCL agreed to the reallocation of Special Capital to Members, in all cases in accordance with the initial recommendation made by RemCom unless, as was in accordance with the Remuneration Policy, the Member had left Odey by the scheduled vesting date, and:

(a) Special Capital was then reallocated from PSCL's Special Capital account to the Special Capital accounts of the relevant Members pursuant to clause 10.12(B) of the 2011 LLP Agreement.

(b) PSCL notified the relevant Members in writing of these reallocations.

(c) Members who received reallocations gave notice to withdraw their Special Capital in accordance with clause 10.12(C) of the 2011 LLP Agreement. To effect the withdrawal, as regards Cash Awards, the units in the Odey Fund referable to the Special Capital were transferred to the Member's Special Capital account and he was then able to redeem the units and, in the case of Share Awards, the relevant OHAG shares were transferred from Odey as legal owner to the Member pursuant to a share transfer agreement.

Odey's business and management structure

Nature of Odey's business

25. Mr Crispin Odey founded the business that was later carried on by Odey in 1991 funded with US$150 million of initial investment from Mr George Soros, GAM (another asset manager) and RCB (a pension fund). Odey was incorporated as a

limited liability partnership on 8 July 2002 initially as "Odey Partners LLP". Its name was changed to its current name on 30 October 2002.

26. Mr Odey said that from the outset, Odey's business was about bringing a strong entrepreneurial spirit to active fund management. He described the business as follows:

> "We have always taken a pragmatic approach to investing in a range of different stocks (shares, bonds, commodities etc.) and we take both long and long/short positions. Our funds are intended to be "total return funds", in that all of our investments positions are intended to generate returns (rather than simply mitigate the risk of other investments). This distinguishes Odey from other investment managers, which may sacrifice potential returns to ensure that they hold positions that have a primary purpose of mitigating potential losses.
>
> This approach reflects my attitude that Odey should always aim to seek out investments that deliver the highest returns to its investors by getting ahead of the market. This is all about identifying investment opportunities that will deliver returns that are significantly above benchmark for that investment cycle. This means that Odey's fund managers will often take a riskier investment approach, rather than just engaging in asset gathering. This does not mean that we take on risk for risk's sake but our investment approach is known for being "contrarian" compared to that of other investment managers. By this, I mean "going long" on an industry or stock others think will perform poorly or "shorting" an investment that others are talking up.
>
> When this investment approach is successful, it can be highly profitable. But conversely there are also significantly greater risks. This means that Odey has seen significant volatility in its business over the years as financial results have fluctuated (both for individual members and for the business as a whole). Funds we manage can gain or lose 20% of their value in a month, and funds that are successful in one year may need to be closed in the next."

27. Lord Roborough gave a similar description of Odey's business to that given by Mr Odey. He further explained that:

(1) The assets under management are split relatively equally between those two types of "long" and "long/short funds", and it is not uncommon for funds to specialise, for example, in a particular sector or geographical region. Long-only funds have relatively stringent investment restrictions and, in essence, only involve acquiring stock in the expectation that the stock will appreciate in value and so generate an investment return. "Long/short funds", by contrast, are subject to fewer investment restrictions, and involve both long positions and traditional "short" positions, which involve selling stock in a way that generates a return for investors. This may typically involve borrowing stock from a broker, selling it to the market at the market price, waiting for the price to fall, and then buying the same stock back on the open market at the lower price, and then returning the stock to the broker. The investment gain is basically the fall in value of the stock.

(2) Odey is an "active" investment management business, in that its fund managers make "active" investment decisions that are intended to outperform the market, rather than "passively" trying to replicate overall market performance.

(3) Like Mr Odey, he emphasised that Odey's business model involves risk.

(a) While Odey is commonly referred to as a hedge fund, in his view, it is more of an "absolute return fund" in the sense that Odey's fund

managers are expected to take positions based on whether they think those positions will generate profitable returns for their funds, rather than simply offsetting the risk of other positions that the funds might hold: "Put simply, we expect to make money with everything we do":

(b) This constitutes a high appetite for risk within the asset management industry and necessarily makes Odey's business more volatile than those of many of its peers: if fund managers make the right investment decisions, Odey's funds can be very profitable, but if they make the wrong investments, there is very little protection. This can be seen in the fluctuation in Odey's financial results over the last ten years, as profits (which are largely based on investment performance) have ranged from over £174 million in 2014 to just over £8.8 million in 2018. Lord Roborough had never considered a job in an asset manager like Odey to be a "job for life" - the volatility inherent in the business model means that even tremendously successful businesses do not exist indefinitely.

(c) This volatility also means that Odey has a slightly different investor profile from those of other similarly sized asset managers. Odey actively markets itself as having a more aggressive approach to risk, which is well known in the market: investors have to be willing to accept this greater risk (and the potential short-term losses) before investing.

28. Mr Pearey confirmed that the "great majority" of Odey's income is from management fees and performance fees. He explained that (a) performance fees are payable usually only where the fund "outperforms" its own performance or "high water mark" although there are some funds which need to outperform relative to a market but (b) management fees are payable irrespective of performance by reference to assets under management although the level of such assets is very dependent upon performance. He described the clients as the Funds themselves; that is whom Odey has investment management agreements with. The underlying investors invest in the funds and the investment management agreement determines the fees which the Fund pays to Odey. It was put to Mr Pearey that Odey did not make money simply from the profit margin on buying and selling investments in its own right. He said it did make money in that way, in effect, because that profit margin determines the performance of the Fund.

29. Mr Odey said that Odey's income predominantly comprised these fees. He said that performance fees tended to dwarf the management fees when they come in; performance funds are "much more profitable for the company, but only if we perform". It was put to him that Odey does not make money by the return on what it buys and sells but rather it makes money by the percentage fees it charges. He said: "Not really, because we are trading - the fund managers are trading shares, and bonds and currencies every day, all the time, and it is those returns which make the returns to the fund". He appeared to agree that the managers do not trade on their own behalf but rather for the investors although he noted that the managers are investors as well as they have their own monies in the Funds and so are trading on behalf of themselves, in part. He agreed that that growth would accrue to the managers or whoever else has invested in the Fund rather than to Odey itself.

Building up the Odey business

30. Mr Odey set out that when he started Odey in 1991, he was the only fund manager at Odey and managed certain long-only investments. In 1992 he launched Odey European Inc., a fund which focused on investments in equity and fixed income

markets in Europe. He was primarily responsible for the management of the fund and made the decisions about which stocks the fund should invest in.

31. He said that Odey was initially a very lean outfit, with a small number of employees. As the owner of the firm, he had various functions in addition to fund management, such as, sourcing fresh investment, which involved meetings with potential investors, recruiting additional research and analyst personnel, managing the small number of employees and dealing with some of the more practical parts of running a hedge fund such as regulatory compliance. Mr Simon Batten, who was with him at Odey from the start, assisted him with the day-to-day management of the firm.

32. Both 1992 and 1993 were successful years owing to the strong performance of Odey European Inc. The subsequent years were more difficult, partly as a result of the impact of the Federal Reserve interest rate increase in 1994 and the effect that this had on the long position on bonds that Mr Odey had taken. This led to many investors pulling their money out, including Mr Soros in 1997. Between 1994 and 1999, the clients he retained tended to be individuals and businesses with whom he had a close relationship. Notwithstanding this, over this period the Funds were profitable; they ultimately grew 400% from US$50 million to US$250 million.

33. By 1997, Mr Odey decided that he wanted to create a more organised and efficient enterprise with greater growth potential and from that time onwards he gradually delegated his managerial functions to a separate managerial team. How the management evolved is set out below.

34. By 1999, the business was performing successfully and had recovered to the same levels as the very early years. During the early 2000s, the business grew strongly in a relatively short period in part due to recruitment of fund managers and improvements in the research facilities made available to analysts, who supported the fund managers. Odey began to expand the investor base and increasingly received more investment from "asset allocators", such as Rothschilds, and retail investors (introduced through Hargreaves Lansdown).

35. The business continued to expand rapidly, in particular from 2010 to 2015, which Mr Odey and Mr Pearey attributed to Odey's response to the financial crisis. Odey's success in earning substantial returns for investors led to an influx of institutional and pension fund investors, who were keen to benefit from Odey's investment returns given the difficulties they faced in the wake of the "credit crunch". Mr Odey said that, "at its peak" in the financial year ending 5 April 2014, Odey generated profits of £174 million, with US$12 billion worth of assets under management across 35 different funds and 120 people working in the business (including 12 fund managers and between 18 to 24 analysts).

36. Mr Odey noted that Odey has had less success in more recent years. By 2018, profits had fallen to just over £8.8 million. Over the three years to 2018, the Odey European Inc. fund suffered losses of 60% over the three-year period to 2018 and the assets under Odey's management fell to US$4.5 billion. Mr Odey considered "these reversals in performance are an inevitable aspect of the way that Odey operates". He noted that in the last year Odey made a robust recovery, performing strongly in more volatile market conditions. The positions that he took in 2015 had begun to generate good returns and there were encouraging signs about the likely long-term performance of other investments. However, a number of institutional investors were concerned about the short-term volatility of the funds and had removed their investment.

Management structure during the relevant period

37. In 1998, Mr Batten was appointed Co-Chief Executive Officer and Chief Operating Officer ("**COO**") of Odey and Mr David Fletcher was appointed Chairman of Odey.

38. In 2001, Mr Pearey joined Odey to help support Mr Batten. Mr Pearey described his recruitment as:

> "part of the efforts to devise and implement a separate, organised and professional management structure that would help Odey's business function more efficiently as it became more complex, support further growth and relieve some of the management responsibilities from the co-founders".

39. In 2005, Mr David Stewart joined and became Chief Executive Officer ("**CEO**") of Odey. He continued in that role until 2012 when he left Odey (although he continued to be involved with the business after his departure). Mr Stewart said that his role was to drive Odey's growth further by using his managerial experience to put in place a more structured "corporate" approach using "clearer management processes" to ensure that the business could continue to operate effectively as it grew in size. He was also focused on expanding the business' appeal to more institutional investors like pension funds.

40. At some point in these years Mr Odey, Mr Batten and Mr Fletcher formed ExCo on which Mr Stewart later replaced Mr Batten. Mr Odey said that as a result:

> "managerial issues were no longer determined solely on his initiative but were considered and ultimately determined by ExCo, which would also consult with other members and people at Odey. We were a small business that was run out of one building at the time, and the roles of the different ExCo members overlapped based on what was needed. I was obviously still an important figure at Odey, especially on the investment management side, but the consequence of creating a more organised and efficient business was that I no longer assumed responsibility for every single decision as I might have at the very beginning. I would joke about how this was the beginning of the "rule of law" at Odey, as we began to adopt more formal management processes and made sure that there were several voices in the room other than mine when deciding what was best for the business and how things were going."

41. Mr Stewart said that ExCo met regularly, around twice a month or when required to deal with urgent matters. At various times, ExCo meetings were also attended by others in the business, such as Mr Pearey and Mr Orlando Montagu (who joined Odey in 2001 and eventually become Head of Marketing and Sales, with a particular focus on marketing Odey to private wealth managers). Mr Stewart described ExCo's role and interaction with members of Odey as follows:

> "ExCo was responsible for taking high-level management decisions on behalf of Odey. However, Odey was very much a partnership business and there was transparency with all the members, who would generally see whatever papers the management were considering (save for any elements that needed to be kept confidential between members). There were quarterly membership meetings at which decisions were put to members, who were given the opportunity to raise questions with ExCo and share their views about the management of the business. Members were also encouraged to, and did, raise matters with me and other members of ExCo outside formal partnership meetings."

42. Mr Pearey was appointed Chief Financial Officer ("**CFO**") in 2007 and COO in 2010 and held these roles throughout all periods relevant to this appeal. In these roles he was responsible, as CFO "for the integrity of Odey's financial records, providing up-to-date, accurate management information" and, as COO, for Odey's "operational

efficiency, providing responsive support services to the investment activities". Mr Pearey said that, in practice, he assumed responsibility for all of the systems and processes for the management of Odey as a whole, including those relating to the allocation of Odey's profits to Members and remuneration more generally in relation to both Members and employees.

43. When Mr Stewart left Odey in 2012, Mr Fletcher moved from his role as Chairman of Odey to the role of CEO. In 2015 Mr Fletcher left the role of CEO to become the Non-Executive Chairman and Mr Pearey then became Odey's Managing Director. Mr Pearey said that this role combines overall responsibility for managing the business, including sales and marketing and the Odey Wealth businesses.

44. Mr Pearey said that over time Mr Batten was the person who became increasingly responsible for the day-to-day operations of the business. Mr Odey made the key management decisions (particularly in relation to remuneration) but concentrated most of his time on managing the funds.

Expansion of offices and personnel

45. Mr Pearey set out that the business grew, in particular, as Mr Odey had set out, in the wake of the financial crisis from 2010 so that by 2014 there were offices in London, Guernsey, Geneva, New York and a UK Wealth business. He gave details of the growth of the personnel at Odey as follows:

(1) In 2001, Odey operated out of a single office and there were only 21 individuals involved with the business, including three fund managers managing eight funds with a total assets under management of US$300 million.

(2) In 2002, there were five individual Members, by 2007 there were nine individual Members, by 2009, twelve individual Members and by 2015, eighteen individual Members. There was one corporate Member until 2015 when there was four corporate Members.

(3) The total number of fund managers at Odey increased to nine in 2009 and twelve in 2014.

(4) The number of analysts grew from four to six in 2002 to eighteen to twenty-four in 2014, of which eight were Members.

(5) The trading desk grew from one trader in 2002 to six traders along with a treasury function to deal with foreign exchange transactions and portfolio financing in 2015.

(6) In addition to the management team described above, the team grew to include a full-time compliance officer plus assistant, in-house legal counsel, a head of HR, a team of at least four in finance including the CFO and COO, a financial controller and a number of assistants.

(7) The sales team comprised one full-time salesman and one person in client services in 2002 and increased to eight salesmen and four in client services by 2016. The team became more structured in terms of looking after certain territories globally (such as the US, Far-East, Central Europe and the UK) and client types (such as institutional, family office, private banks and wealth managers).

(8) The back-office teams comprised two individuals in 2002 but grew to six by 2016. They managed the trade settlement process and fund valuation reconciliation over an increasing number of funds.

(9) The IT team grew from one individual in 2002 to four in 2016, including an infrastructure engineer and two front-line support technicians. In 2013, Odey employed its first in-house programmer and now has a team of four

programmers responsible for developing reports across all areas of the business, including performance attribution, risk and portfolio composition.

46. Mr Pearey said that as a result of the expansion of numbers of persons involved in the business and roles within the business, "new and improved systems and processes have had to be put in place on the managerial side".

Role of managers, analysts and traders

47. Mr Pearey said that fund managers "operate relatively independently, with freedom to choose their own stocks, strategies and timelines". Mr Odey agreed that understanding what investments are going to perform well requires a considerable degree of skill and that he had hired intelligent people whose judgement he could rely on. He said new fund managers were recruited by coming across people; word of mouth; reputations in some cases.

48. Mr Pearey said that the analysts are responsible for producing research about potentially profitable investments for use by different fund managers. Some analysts specialise in particular sectors or companies of a certain size but, generally, they are given considerable freedom to seek out companies that are either over-valued or under-valued by the market. He said that the skills involved in being an analyst and a fund manager, are similar to a degree. He noted that many of the fund managers started their lives as analysts. That was a typical course but, in his view, not all analysts make good fund managers.

49. Lord Roborough had worked as both an analyst and fund manager for Odey and at the time of the hearing was Head of Research which involved overseeing analysts at Odey. He explained that analysts analyse and research particular companies and occasionally bonds and commodities as well. He accepted that requires a certain degree of judgment and is quite an intellectually demanding part of the business which also involves being able to persuade fund managers that they are right, as well as just having good ideas. He said that analysts have to communicate their conviction and build up trust. He thought that the skills involved in working as an analyst and a fund manager are "very similar" although they perhaps involved a different balance between the required skills.

50. Mr Pearey said that the role of the traders is to deal with the fund managers directly and execute orders pursuant to their instructions. Traders do not have (and have never had) discretion in respect of trades but "they are a key part in the investment process, ensuring that we get the best possible price in the market and providing the firm with market colour".

51. Mr Pearey confirmed that the Members were largely fund managers, analysts or management. He said that there were also some Members who were in sales and one Member who was a trader. That Member was the head of the trading desk: his job was primarily to ensure the best execution of trades, but there were other functions involved in terms of monitoring the portfolio.

52. Mr Pearey confirmed that at the relevant time all the core management team other than Mr Pearey himself had backgrounds in fund management. Mr Pearey was trained as an accountant.

Remuneration policy prior to 2011

ExCo's approach to profit allocation and remuneration

53. From 2001 until the implementation of the Plan in 2011, as provided for in the Partnership Agreement the allocation of profits to Members was determined by ExCo as was the remuneration of employees. Mr Odey described ExCo's approach as follows:

(1) ExCo looked at what the individual had generated in profits for Odey. This was generally more straightforward for fund managers (who were usually members) as their profit share was tied to the performance of the relevant fund and the performance fees the firm had received as a result. For analysts and those involved on the management side, it was more difficult to determine how far the individual had contributed to the performance of a particular fund or the business of Odey more generally and so there was no fixed approach (although this became more rigorous and based on data overtime).

(2) Decisions on remuneration followed a lengthy process over a period of months each year involving several meetings of ExCo. ExCo assessed each individual's performance with the benefit of reports (containing, for example, individual metrics and performance indicators) and first-hand accounts from ExCo's members.

(3) Mr Odey thought that it would certainly be fair to say that:

> "while my views were important during those discussions, especially on those individuals involved in the investment side of the business, they were by no means conclusive. If others on ExCo had dealt closely with an individual during the year under consideration then they would make their views clear. Decisions were taken by committee. This was necessary, given the growth of the business (and the corresponding increase in the number of individuals working at Odey) and the number of factors that had to be taken into account in determining who had contributed what to Odey's success."

54. Mr Stewart's description of how ExCo operated accorded with that of Mr Odey. He said that Mr Odey had an "eat what you kill" approach, which meant that a high proportion of remuneration was variable and linked to annual performance. In his view, given the volatility of fund manager performance, the approach taken to profit allocation could lead to a "feast or famine scenario where individuals could see radically different profit shares year-on-year". As regards the part he and Mr Fletcher played he said the following:

> "[We] were a key part of these discussions: we made sure that Crispin was being fair - which, generally he was - and argued the case for those individuals with whom Crispin had not worked as frequently (which was usually certain analysts). While Crispin was the loudest voice in these discussions (and, historically, had been the main decision maker), profit shares were decided by agreement while I was at Odey, and there were numerous occasions where decisions were based on input from David and me."

55. Mr Stewart said that over time, as more fund managers joined Odey, their input would also be sought over the appropriate profit shares and remuneration of people they worked closely with.

56. Mr Pearey explained that the initial profit allocations decided on by ExCo in January of each year were primarily based on the performance fees that Odey had generated during the previous calendar year. However, as Odey's financial year corresponds to the fiscal year ending on 5 April, the underlying accounting figures were not necessarily finalised by January, and Odey continued to generate income and profit until the end of its financial year (for example, in the form of management fees arising from January to March). There were, therefore, occasions where additional profit allocations were made in March or April. Mr Odey said that by January, ExCo had a pretty good idea of the figures but as the year end was in April "invariably we

are conservative at the December period, in terms of what we estimate for the management fee" which was not yet finally determined at that time.

Concerns with the approach to remuneration

57. Mr Pearey said that there were the following concerns with the lack of any formal remuneration policy or a deferral mechanism in respect of Members' profit shares:

(1) In his view, "to a degree, Members were inevitably focused on their performance in the current year alone and were not tied in beyond the current year". Whilst this approach made sense in the early years of the business when there were only a small number of people, as the business grew and became more complex, "the process and the underlying policies on remuneration, and, in particular, the absence of any deferral or long-term incentive mechanism, increasingly felt outdated and in need of a rethink". He said that, in this respect, "the remuneration policy and the process were no different from any of the other systems and processes at Odey; they were gradually reformed and professionalised during the 2000s".

(2) Management was concerned that there was no express requirement for any of Odey's fund managers or analysts to invest in the funds that they were involved with. He said such investment is important for two reasons:

(a) It is "a key part of aligning the interests of those making investment decisions with the interests of the fund investors themselves".

(b) From a presentational perspective "it is important for us to be able to demonstrate to clients that their fund managers have "skin in the game", as they often ask how much fund managers have invested in their own funds before investing".

58. Mr Pearey explained that in the early years Mr Odey invested his own monies into funds but other fund managers who came into the business did not share his willingness to do so. The management therefore introduced "ad hoc remuneration mechanisms" for certain Members that incorporated an element of deferral. Mr Pearey set out an example by reference to Mr Alex Griffiths a fund manager who he described as "generally resistant to investing material amounts in his own funds". In the early 2000s, Mr Griffiths launched a fund that invested exclusively in Japan which did very well from 2003 to 2005 and was, for a time, Odey's biggest fund with over US$1.2 billion of assets under management:

(1) In order to incentivise Mr Griffiths to maintain his performance as regards this fund, ExCo decided that a proportion of his post-tax profit share for 2004 (£300,000 of his total share of £2.4 million) should be invested into the Japan fund for a minimum period of three years during which time he would not be permitted to withdraw those monies. This triggered an upfront tax charge on the amounts invested in the fund, even though Mr Griffiths might not receive those amounts if he left Odey within the three-year period. He, therefore, insisted that Odey "gross-up" the £300,000 so that he could use the additional amount to pay the tax charge.

(2) The Japan fund had a particularly good year in 2005 and Mr Griffiths received a large profit allocation of £13.1 million. ExCo tried to get him to agree to invest a significant proportion of this back into the fund, but he refused.

(3) There was "a fierce debate at the time" and, in the end, it was agreed that £750,000 of his 2005 profit share would instead be used to purchase "bonus" shares in Odey's parent company, which paid dividends based on the overall

performance of the business. His entitlement to the shares vested over the subsequent three-year period, but if Mr Griffiths left during this period, he was not to receive the shares that had not vested, and any shares that had vested could be "clawed back" by Odey repurchasing them from him. As this also meant that Mr Griffiths had an upfront tax charge on the amount he was required to use to purchase the shares, he again insisted that the sum was "grossed-up" by Odey.

(4) This approach was followed in 2006, where £540,000 of his £1.05 million profit allocation was used to purchase such "bonus" shares. After that, the Japan fund's performance declined rapidly and Mr Griffiths left Odey in 2008 and the fund closed shortly after his departure. As a result, he did not receive any shares that had not vested at that time and Odey repurchased any that had (at less than the value they were issued at).

59. Mr Pearey said that there were disadvantages to the approach taken in relation to Mr Griffiths, in addition to the upfront tax charge described above: (a) it was administratively complicated, as Odey did not follow any formal process, and (b) it was not clear that Odey could legally enforce the deferral if this was challenged by the relevant Member.

60. Mr Pearey explained that around 2008/2009, Odey decided to introduce a formal "bonus" share scheme that incorporated a formal element of deferral. The arrangement was aimed at expanding Odey's ownership to Members who were not fund managers as a way of giving them a clearer financial interest in the long-term success of the business.

61. Mr Stewart also considered that there were a number of drawbacks with Odey's approach to remuneration and profit allocation prior to 2011. He said that the "ad hoc" approach became more difficult as Odey grew in size because the increase in members meant there was a greater need for transparency about how remuneration decisions were made across the wider team (particularly for analysts). He found it surprising that, save for the "bonus" share scheme, there was no real attempt to use remuneration to increase Members' personal investment in the long-term success of the business. In his view it was a mistake not to have such arrangements:

(1) He said that there was:

> "always a risk that star performers would find it easy to walk away from Odey after a good year. By the same token, there was also a chance that members would leave if they received a particularly low allocation. While we would not generally ask people to leave if they performed badly in one year - we recognised that in such a volatile investment environment performance should be judged over a number of years - members in that position would have little incentive to stay if offered more elsewhere."

(2) He was concerned about the lack of a formal requirement for fund managers to invest any of their remuneration in their own funds, essentially for the same reasons as Mr Pearey gave:

(a) His experience prior to joining Odey was that:

> "not only does such investment create a longer term incentive to remain at the firm (particularly if amounts must be invested for a minimum number of years), but it aligns the financial interests of fund managers with those of their investors. This is particularly important in an investment management business like Odey that takes investment decisions with more inherent

> risk, as it creates a different dynamic for fund managers when deciding whether the risk can be justified."

(b) Like Mr Pearey, he also thought such investment is important as a "marketing tool" for potential clients as it demonstrated that fund managers had "skin in the game". He noted that when approaching prospective institutional clients Odey prepared and submitted a "Request for Proposal", which disclosed details about the firm's remuneration structure, including incentivisation schemes. This was taken into consideration by prospective clients in deciding whether to engage Odey.

(c) He thought that the departure of Mr Griffiths provides a clear example of the issues that could arise as a result of Odey's failure to require fund managers to invest in their own funds.

(d) He recalled that there were other examples of informal arrangements between ExCo and certain Members (such as Mr Feras Al-Chalabi) that led to a proportion of their profit share being invested in the business. These continued to be unsatisfactory: they were administratively difficult; there was a lack of certainty about exactly what rights a Member had over those amounts; and "there was a lack of consistency about exactly who should be required to enter such arrangements, and in what amount, which opened the door to member pushback and accusations of unfairness". He understood that Members were liable for tax on these amounts even though they might never actually receive them.

62. Mr Stewart said that the experience with Mr Griffiths' fund led to the adoption of "more rigorous risk management procedures" and to an understanding of the benefits of introducing a more formal mechanism that would ensure fund managers had sufficient "skin in the game". While there was still general hesitation around introducing a formal mechanism there was an acceptance that, as more Members joined, Odey would need to introduce more formal arrangements that would apply more generally.

63. Mr Odey said that the policy prior to the introduction of the Plan was to a large extent consistent with his own views on what was fair and appropriate. He was not keen on the idea of a formal deferral mechanism:

> "Given the nature of the Odey business, members involved in the investment side assume a degree of risk as a result of the volatility in the performance of the funds that they are managing (and, by extension, their own performance). As a result, an individual's profit share often varied widely from one year to the next. If an individual had a particularly good year then it was fair in my view that they should receive the fruits of that labour, not least because the position could be quite different next year."

64. He continued, however, that he was aware from the rest of the management team had the concerns set out above, as was brought into focus, in particular, by Mr Griffiths. He recalled being content with the arrangements in respect of Mr Griffiths at the time because in his view "having a direct interest in the fund you are managing (and the wider business, in the case of the shares) provides valuable incentivisation by aligning your interests with those of investors and shows confidence in your own ability - it is what I have been doing for over 25 years at Odey". He was aware that Mr Pearey thought the outcome was unsatisfactory for the reasons set out above.

Taking advice 2009 to 2011

65. By 2009 as Odey's CFO, Mr Pearey considered that it was crucial to put in place formal mechanisms that reflected Odey's increasing size and need to

"professionalise" the business. His experiences with Mr Griffiths and others "prompted him to explore a deferral mechanism that would encourage individuals to remain with Odey and better align their interests with those of investors". He also said that "regulations were increasingly pushing Odey towards the type of remuneration policy that was eventually implemented" and:

> "Whilst he understood that a formal deferral mechanism "done correctly" would have significant benefits, it was important to ensure that it did not create excessive administrative issues, operated fairly as between the different members and was legally robust. We were also keen to ensure that members should not be subject to an upfront tax charge on amounts they may never receive."

66. At this point, therefore, he sought advice from a range of third-party advisers, about the potential incentivisation mechanisms that Odey could implement to meet these objectives including the big four accounting firms, lawyers and specialist tax advisers.

67. From July 2009, Mr Pearey discussed the proposals with Mr Fletcher (who was then the Chairman) and Mr Stewart (who was then the CEO). Mr Stewart said that the management team were "naturally cautious about otherwise agreeing wholesale changes to our remuneration structure and our remuneration policy". He noted that the proposal stayed at ExCo level, without any material involvement from Mr Odey, for some time as he, Mr Pearey and Mr Fletcher scrutinised the structure: they wanted to present it to Mr Odey only once they were sure it would satisfy Odey's requirements.

68. It was eventually decided to implement the Plan as put forward by Ernst & Young LLP ("**Ernst & Young**").

Reasons for the Plan

69. Mr Pearey set out the following reasons for the introduction of the Plan which Mr Odey and Mr Stewart concurred with. Mr Odey and Mr Stewart's specific comments are also recorded where relevant.

Incentivisation and retention of members

70. Mr Pearey said that the arrangements had clear advantages compared with the "ad hoc" systems used before as he considered was reflected in the wording used in the Remuneration Policy (see [13]):

> "The Plan presented a straightforward and certain mechanism: a proportion of Odey's profits were allocated to PSCL - and not the members - and were therefore available for investment in Odey Funds or in purchasing OHAG shares. PSCL then had a clear power to determine how to reallocate amounts to members in the future. The intention was that this would incentivise key members to remain at Odey and ensure its long-term success.
>
> The Plan was implemented to achieve the overarching commercial objectives summarised [below].
>
> Before the Plan, the fact that members received all their profits in respect of their previous year's performance meant that members would, to a degree, inevitably be concerned about their current-year performance rather than the long-term success of the business. Given the variable nature of Odey's overall profitability and the value generated by a member each year, the profit share for each member could (and often did) vary considerably from one year to another. There was also nothing to stop those members who received a very large profit allocation after a particularly successful year from leaving, as they received all of their profits (and the sums involved could be significant, i.e. greater than £1 million). While we had introduced the OHAG

bonus shares, given the volatility of a business such as Odey (which….. was riskier than most) this was a real concern and it meant that there was no in-built mechanism for incentivising members to remain at Odey. Conversely, it also meant that there were no real consequences if a member's performance subsequently deteriorated after payment of the profit share (although Odey could try to withhold OHAG shares or exercise any clawback rights it had)."

71. Mr Pearey added that if their performance sufficiently worsened, Members could be asked to leave the Partnership and, in that case, they would not be reallocated any Special Capital. Asking Members to leave for continued poor performance was Odey's longstanding approach. While the 2011 LLP Agreement provided that ExCo could remove a Member if it concluded that to do so would be in the best interests of Odey, in practice, Members usually preferred to resign voluntarily.

72. Mr Pearey emphasised that (a) because the deferred share was allocated to PSCL, the management had no doubts that the new arrangements were legally enforceable, and (b) it was a key part of the Plan that PSCL was to invest the relevant sums into Funds that the relevant Members worked on. As the sums were to be invested by PSCL in Odey Funds for a number of years before there was any reallocation of Special Capital, the long-term success of those Funds would directly impact on the amounts available for reallocation to Members. This would clearly align (on a formal basis) the interests of Members and their investors by ensuring Members had real "skin in the game". Mr Pearey considered that Members were much more likely to accept this as a necessary consequence of being a Member of Odey when presented under the arrangements, as a formal (legally robust) policy that simply operated as a matter of course than when presented to them on an "ad hoc" basis as previously.

73. At the time, Mr Pearey was aware of other forms of deferral mechanism but he considered that none of these were workable for an entity such as Odey. For example, one proposal that was implemented by listed companies involved awarding option shares in the listed company itself that would vest over time. However, if such a mechanism was implemented by Odey, it would not require investment in any Funds that the Members were running, and so it did not satisfy a key commercial objective.

74. Mr Stewart said that, as CEO, he felt much more comfortable once the Plan and Policy were implemented, predominantly because of the better alignment between the interests of Odey's clients and those of Members, as the amounts that Members could eventually receive would fluctuate with the performance of their funds. He was also pleased that Odey was able to articulate this to prospective institutional clients in the proposal stage.

75. Mr Odey commented as follows:

(1) Clearly, key individuals would be more inclined to stay at Odey if they knew that leaving would mean they would not receive any further amounts. Some Members had expressed concerns that London was becoming a less attractive place to work and that other international financial centres would soon be better placed to attract top talent in the asset management industry. The arrangements appeared to be one mechanism that would start to address this.

(2) The introduction of the Plan marked a clear shift from an informal understanding to a formal requirement for all Members to have at least some financial interest in the performance of Odey's Funds - Members were incentivised to preserve and to increase any amount that they could eventually receive by way of reallocation of Special Capital.

Regulatory environment

76. Mr Pearey said that the regulatory environment had "an enormous influence in the decision to implement the Plan":

(1) From around 2008 onwards, there was a sustained increase in the number of regulations that Odey had to take into account when operating its business, largely as a response to the global financial crisis and a general sense that the financial services sector required substantially greater regulation. Mr Odey said that he was aware of this increasing regulatory pressure at this time. Entities such as Odey were treated in the same fashion as the high-profile investment banks that had been directly implicated in the financial crash. Mr Pearey and Mr Odey considered that Odey is particularly exposed to regulation because many of its funds are "long-only UCITS", which are subject to greater regulation than other funds (particularly since 2010). Therefore, Odey "has often had to be ahead of the curve with its compliance and regulatory procedures".

(2) The particular concern of relevance was the proposal by the FSA (now the Financial Conduct Authority) to introduce a remuneration code within the financial service sector ("**the Code**"). In broad terms, the Code required certain financial entities to put in place arrangements for remuneration that were consistent with effective risk management such as the use of deferral mechanisms to encourage those involved with the business to take a more long-term approach to success and profitability. The more prescriptive rules set clear limits on the proportion of overall remuneration that should be variable (no more than 100% of fixed remuneration) and envisioned between 40% and 60% of that variable remuneration being deferred for a number of years (between 3 and 5 years).

(3) The draft Code was first published in early 2009 and was subject to various subsequent consultations. Initially it was proposed that the Code would apply only to the largest banks and building societies. However, from as early as March 2009, the investment management market was concerned about how the Code could apply to its business and Mr Pearey received updates from trade bodies warning of the possible consequences. The FSA acknowledged in a consultation paper published on 18 March 2009 that it would be good practice for all investment firms to look at introducing remuneration structures in line with the Code, which expressly included deferral mechanisms. This was a subject of considerable discussion in the industry.

(4) Mr Odey commented that the FSA's approach to this was "little more than a way of deflecting from their failure to prevent the financial crash as a result of not spotting the risks that were being taken at the time by the investment banking sector rather than by investment managers". He said it was "common knowledge" within the industry that the FSA, along with the European regulators, considered a prescriptive remuneration code to be an important tool in improving "effective risk management" in the financial sector in the wake of the banking crisis and that deferral of bonuses was seen as one way to achieve this.

(5) Mr Stewart said that from around March 2009 and onwards he recalled reviewing "Dear CEO" letters sent by the FSA that emphasised that mechanisms that allowed for variable remuneration were considered an important part of risk management. He noted that after the initial publication in

August 2009, there were further announcements from the FSA about encouraging deferral in the investment management sector and potentially expanding the scope of the Code in late 2009 and early 2010 and in July 2010, the FSA published a consultation that included the express suggestion of expanding the Code to cover investment management firms like Odey. He said that at this point, "the general view in the industry was that it was very likely that investment managers would need to start deferring en masse to ensure compliance with the [Code]…..At the time, it looked inevitable that Odey would need to comply with at least some form of the [Code]".

(6) Mr Pearey said that the further consultation published by the FSA on 29 July 2010 generated a significant amount of comments almost immediately. He thought that it was not clear from the consultation whether and, if so, how any extension of the Code would apply to an entity like Odey. Mr Pearey spoke to the IMA directly and wrote to senior members to notify them of the developments on 29 July 2010, explaining that Odey was likely to be in a "comply or explain" category but that this was far from certain. Odey's compliance officer provided a fuller explanation of the content of the FSA consultation to senior members on 30 July 2010, which again was unable to provide anything of real clarity as to how exactly it would apply. The uncertainty inherent in the proposals formed a key aspect of the IMA and the AIMA's response to the consultation.

(7) At this stage, Mr Pearey and other members of the management team at Odey considered that it was likely that the prescriptive elements of the Code could apply to Odey within the near future. Therefore, the decision was taken to explore whether the proposals which were already under consideration for the commercial reasons set out above were consistent with the objectives and requirements of the Code. It was hoped that, if Odey implemented a revised remuneration structure before the Code became compulsory, Odey would have greater flexibility to put in place something that better suited its business and way of operating than if Odey had to react quickly to the introduction of the Code. Mr Pearey's understanding was that the Plan satisfied key parts of the Code by incentivising Members to take a longer-term approach to investment and the overall success of the firm, while also better aligning the interests of Members with those of investors.

(8) Mr Odey recalled that Mr Pearey explained that the Code was necessary for regulatory purposes and explained his thinking on this at the time broadly as set out here. Mr Stewart said that as the Plan already satisfied the Code's key principles:

> "we decided to recommend to Crispin that the Plan be introduced. Our view was that it would be better for the business to introduce a remuneration policy and mechanism that fit our needs, which we could then adapt if we were required to adopt any of the more prescriptive elements of the Code."

(9) Ultimately, the Code was extended to the asset management sector from 1 January 2011, with firms being required to comply with it as soon as reasonably possible and not later than 1 July 2011. In the event, the most prescriptive aspects of the Code did not apply to Odey because its business was considered too small. However, Mr Pearey's view was that, in practice, Odey nevertheless had no choice but to implement some sort of deferral mechanism that gave effect to the core principle of the Code as regards effective and proportionate risk management:

> "This was in line with what Odey wanted to achieve as a commercial matter, but it was the regulatory environment that compelled Odey into actually implementing the Plan at this time and in this form. In any event, the FSA's attitude at the time (and that of European regulators and institutions) was such that many of us at Odey expected the more proscriptive aspects of the code to become mandatory."

Investor relations

77. Mr Pearey said that "the combination of Odey's growth and the changing regulatory environment led to ever greater demands from investors in the funds for Odey to have in place a remuneration policy with all the key aspects of long-term incentivisation and alignment of interests":

> "A fund manager is a "key person risk" to the business and investors want to be sure that, when they invest with a particular fund manager, that individual is motivated and retained so that he or she will continue running the fund for many years.
>
> Odey putting in place a policy and a mechanism that worked to attract, motivate and retain senior members of the team was a key aspect of professional investors' due diligence and part of Odey's progress to a more professional and institutional organisation, which attracted inflows from the larger asset allocators, such as pension funds."

78. He said that the following is a typical example of the type of question asked by investors regarding remuneration:

> "Could you please provide us more detail on analysts' compensation? Could you please include details on extent of deferral of bonuses (number of years), the % of bonus that is tied into the performance (over what periods) of portfolios or their individual ideas and the % range (as % of basic salary) that bonuses could be ?"

79. Mr Stewart also said that the investment of managers and analysts in their funds was also regarded as an important marketing tool for potential clients.

Flexibility in management of capital/funds

80. Mr Pearey said that the operation of the Plan also gave Odey considerable flexibility, as substantial sums were to be allocated to PSCL and so were available, if required, to provide protection in the event of a decline in business and/or to pursue further investment. He considered this was most relevant in three ways:

(1) The Plan ensured that Odey had sufficient regulatory capital:

(a) Odey is required to undertake an "Internal Capital Adequacy Assessment Process" each year to test whether it has sufficient regulatory capital for its level of expenditure. Typically, Odey is required to hold 25% of recurring expenditure as regulatory capital, although this can be increased by the FSA following any inspection (as they did in 2009 by increasing the requirement by 10% to 27.5%).

(b) As explained below, Odey had to certify to PSCL that it had sufficient regulatory capital before PSCL would make any reallocation of Special Capital to members. PSCL was careful to make clear to Members that it was unlikely that any reallocation would be made unless Odey retained sufficient regulatory capital after any reallocation.

(c) This mattered because Odey actually had a relatively low regulatory capital requirement compared to its peers and, even with the 10% increase in 2009, was susceptible to further increases.

(d) As it turned out, the FSA did not raise any material concerns about Odey's regulatory capital after 2009 but, as Odey's business was highly volatile, there was a real benefit to having these amounts available if needed.

(2) The Plan guarded against the risk of insolvency or any other exceptional circumstance (such as the incurring of a huge liability, for example as a result of trade error in a large foreign exchange order). In that case, Mr Pearey would expect Special Capital to have been made available in the interests of Odey as a whole. He said that, given Odey's "greater appetite for risk when making investments, these are not theoretical concerns". He noted that Odey had seen successful funds lose considerable value within a short space of time, for example over 20% of their value in a month, and, as set out above, has experienced considerable volatility in its financial results. He thought that in "this type of business environment with an elevated risk of insolvency, Odey's ability to rely on the special capital contributed by PSCL if needed should not be underestimated".

(3) Under the Plan, PSCL had the potential to accumulate considerable amounts over time where Special Capital was not reallocated to Members if, for example, they left the firm. PSCL had discretion to use these amounts to further Odey's wider business; it could retain the funds as a "pocket of cash" for use should an urgent business need arise for seeding new Odey Funds. For example, in 2016 £1.3 million of cash held by PSCL, which had been initially recommended for reallocation to Members, was not reallocated owing to their departure from Odey. On 4 October 2016, RemCom determined that this cash should be introduced as a Special Capital contribution to Odey, to be held and invested at the discretion of ExCo. In the event, this amount was used by PSCL to purchase shares in OHAG, that were then held by PSCL for six months before being reallocated to Mr Pearey and Mr Montagu as a one-off bonus share award.

81. Mr Odey commented that in a business such as Odey's, there is an inevitable risk of business failure. He noted that, for example, in 2016, Odey's profits fell by approximately 45% compared to 2015 (and approximately 75% compared to 2014). In his view, the advantages set out by Mr Pearey meant that PSCL had the potential to become a "font of capital" for the business that it could rely on when necessary. Whilst in fact Odey did not need to use any of the Special Capital for regulatory or insolvency purposes, Mr Odey thought it was clear in the conditions set out in the letters that he sent to Members as a director of PSCL that Odey was entitled to use these amounts in these scenarios if required, and that it had an even wider discretion that it could exercise if appropriate. He noted that there were occasions where "we were able to use PSCL's capital to make one-off payments" such as the reallocation to Mr Pearey and Mr Montagu in 2016.

Relevance of tax position

82. I have set out the evidence on the relevance of the tax saving in implementing the Plan below. I note that in his witness statement Mr Pearey said that he felt at the time (and still felt) that:

> "the Plan was necessary for the long-term sustainability of Odey, taking into account the lack of a remuneration policy and consistent process that had prevailed previously, the regulatory pressures in the aftermath of the global financial crisis, investor demand and the need for flexibility which any business requires. Any tax savings were of incidental importance compared with these other factors. This is further borne out by the fact that the

Remuneration Policy remains in place, although the underlying mechanism has changed."

Approval for the Plan

83. Mr Pearey said that, in light of all of the factors set out above, ExCo agreed that it was in the best interests of Odey's business to implement Ernst & Young's proposal in a way that gave effect to the principles of the Code. The Plan was first presented at a meeting of ExCo in 2009, which comprised Mr Odey, Mr Fletcher and Mr Stewart.

84. From the outset, Mr Pearey's view was that Mr Odey should oversee the Plan rather than be subject to it. As he was the founding Member of Odey with a very large amount of his own personal wealth and reputation invested with the business and its funds, the commercial objectives set out above did not apply to him. In addition, if Mr Odey was precluded from benefiting personally under the Plan, he could sit on the board of PSCL and continue to take a key objective role in its remuneration decisions. That would have been difficult if he had been subject to the Plan.

85. Mr Pearey's impression was that, while Mr Odey accepted that the Plan was necessary in light of the regulatory environment at the time, he had some personal reservations. He said that beyond expressing his personal views and agreeing that the Plan should be implemented, Mr Odey had very limited involvement in the process that led to the implementation of the Plan.

86. Mr Stewart also noted that whilst Mr Odey was not particularly keen on introducing the Plan, he understood its various commercial benefits and recognised that it was better to take a proactive approach to the likely regulatory changes. He concurred with Mr Pearey that, from an early stage, the view was that Mr Odey should not be part of the Plan because it was unnecessary:

> "All of our commercial concerns about incentivising and retaining members - and ensuring they had some "skin in the game" - did not apply to Crispin. His interests were already entirely aligned with the long-term success of the business, and he had large amounts of his personal wealth invested in his own funds."

87. Mr Odey said that when he became involved at a later stage, he thought it clear from the explanations that the management team gave him that a considerable amount of work had been done and advice taken. He understood that Mr Pearey spoke to others who worked in the "operations" side of the asset management industry, and that Mr Stewart attended meetings hosted by the FSA. Mr Odey said that the reasons set out by Mr Pearey for the introduction of the scheme, as recorded above, were those presented to him.

88. Mr Odey confirmed that he was not keen on implementing the Plan when it was first explained to him and recalled other Members also were not keen. Essentially his view remained as set out above. He was ultimately persuaded that, in addition to being unavoidable as a practical matter (due to the regulatory position), it was the best idea at the time due to the commercial advantages it provided. He noted that fundamentally it strengthened the rules regarding profit share in favour of the business over that of the other Members as, under the Plan, Odey and PSCL would continue to have control over potential reallocations of Special Capital for a number of years. As the founder and main shareholder of the business and the only Member not participating in the Plan this clearly put him in a better position relative to the other Members. While HMRC suggest that Members were entitled to the amounts allocated to PSCL from the start, Mr Odey considered "this was not the case; the money remained within the sole control of the business through PSCL".

89. Mr Odey noted that the Plan was not needed to incentivise him essentially for the reasons set out by Mr Pearey and Mr Stewart. He thought that he was also perfectly placed to oversee the Plan as a director of PSCL. It was for these reasons that his involvement in the decision to implement the Plan was relatively limited. He was only really involved when asked to sanction the Plan after much of the detail had already been agreed. After he agreed in principle to the Plan's introduction, it was put to the Members to decide whether it should be adopted. He was aware that, as part of this process, there were meetings that other Members attended where the Plan was discussed in more detail, but he did not necessarily attend them because they were not relevant to him.

90. Once the membership had agreed to implement the Plan and the new Remuneration Policy, the senior management team, and in particular Mr Pearey, were responsible for deciding the next steps and ensuring it was implemented correctly. Mr Odey's role in the operation of the Plan was principally concerned with RemCom's recommendations, board meetings and written resolutions of PSCL and the notification of Members thereafter.

Approval of the Plan by the Members

91. Mr Pearey noted that the Plan was initially presented to a meeting of the members in late 2009 as well as for final approval in a meeting in January 2011. Mr Stewart explained that in the meeting in January 2011 Mr Pearey presented the Plan to the general partnership for final approval, explained its commercial background, and confirmed that it had been agreed by all members of ExCo. Mr Stewart covered the regulatory background and why the Plan was consistent with the principles of the Code. He said the following as regards the view of Members:

> "Members were not particularly happy, particularly as it was made clear that they would have no right to amounts under the Plan and would not receive them if, for example, they left Odey. However, they were not really given any choice, and most were generally resigned to the Plan's introduction given the regulatory environment. I understood from talking to Members that the tax benefit on the amounts that they could ultimately receive softened the blow somewhat. However, they would have much preferred to have received a larger amount in their pockets straight away without any tax benefit, rather than having a sizeable amount made subject to the discretion of PSCL and placed at risk for a number of years. I note that HMRC say that amounts allocated to PSCL would inevitably be reallocated to the Members, but that is certainly not how I or any of the Members saw the Plan. Nor is that how it applied in practice."

92. Mr Pearey said that he "made it absolutely clear to Members that amounts that were allocated to PSCL under the Plan were at risk and they had no right to them". When he was asked if he told them that PSCL might refuse to give them that money, even if they were still at Odey and Odey was still profitable, he said he may not have put it in those explicit terms, but it was clear that the discretion belonged to PSCL ultimately. He confirmed that he explained the Remuneration Policy to the Members.

93. Mr Pearey thought it unsurprising that there were general concerns among Members about how the mechanism would operate in practice such as about how sums would be invested and over what period. He noted that there was something of a divide on the introduction of the Plan between (a) Members who had been involved with Odey since its early years, who were essentially opposed to the general approach of the FSA rather than the specific mechanics of the Plan itself, and (b) Members who had joined from banks and other larger institutions, who were broadly familiar with arrangements like the Plan as they had previously been subject to similar mechanisms.

There were also certain Members who had specific objections to the Plan. For example:

(1) One Member did not like the risk that, if Odey asked him to leave, he would lose both his role in the firm and any eligibility to receive Awards that were based on his historic performance.

(2) Another Member was particularly resistant to the idea that his individual share should be invested in his own Funds, on the basis that this would lead to him suffering a "double punishment" if he had a bad year: both his performance fees arising for the year and any amounts he was subsequently reallocated by PSCL would be reduced.

(3) Others did not like what they perceived as a liquidity mismatch between investors, who could redeem from a Fund on any given day, and fund managers, who were subject to a mechanism which saw them "locked in" for up to two years.

94. He said, however, by the time that the Plan was presented to Members:

> "they were generally resigned to the need for it given the approach of the FSA, increasing investor demand and the internal push at Odey to ensure people invested in their own funds. Addressing the tax position, i.e. avoiding an unfair charge for individuals who did not receive amounts by taking an efficient tax position, made the Plan more palatable, but I am certain that most Members would have preferred to have simply received greater amounts immediately with no tax benefit. I therefore disagree with any suggestion that the tax benefit was the primary motivation behind the Plan - Odey needed a mechanism such as this for commercial and regulatory reasons, and this is why, despite the general opposition, ExCo decided to implement it."

95. Lord Roborough's account of the introduction of the Plan accorded with that set out above. He explained that:

(1) During the summer of 2010, there were a number of meetings between different groups of Members and of the full Odey partnership, at which they discussed the general concern that the Code would be expanded to apply to businesses such as Odey. His understanding was that Odey's management team were sufficiently concerned that Odey might be caught by the Code that they decided to get ahead of the FSA and in 2009 began exploring potential remuneration structures with professional advisers.

(2) At the Members' meetings in early 2011, Mr Pearey suggested the Plan was being implemented, in large part, to respond to the increased regulatory pressure from the FSA. Mr Pearey said that the Plan allowed Odey to comply with the spirit of the Code while also giving Odey the flexibility to adapt the Plan if more stringent rules were introduced while bringing other commercial benefits for Odey, in particular, in its intended operation as an incentive and retention mechanism and in that it ensured Members had "skin in the game".

(3) While it was made absolutely clear by Mr Pearey that the individual shares were not the Members' money until the relevant amount of Special Capital had been reallocated, Members could all appreciate that they would now have at least a potential financial interest in the performance of Odey's Funds and so their interests were better aligned with the interests of investors. While this had, historically, been the case for fund managers - who were generally expected by investors and senior management to invest their own cash into their own Funds (and they usually did) - this had never been expected of analysts and

other Members who were not involved with investment management. As the business grew, with more fund managers and analysts, there was a need to formalise the expectation of managers and analysts taking a stake in the funds they were managing or advising.

96. Lord Roborough said that the Plan was explained to Members very much as a "fait accompli". He thought that it was clear that the decision had already been taken by the senior management to introduce it and the Members had no real say in whether or not the Plan was adopted. It was not a discussion. At this point, however, the Members were largely resigned to its introduction given the regulatory backdrop, and so there was never any need to seek third-party advice about it - "we had no choice but to accept it if we wanted to remain as members of Odey".

97. He also said that Mr Pearey explained the mechanics of the Plan in detail and repeatedly said that Members would have no right (whether legal or otherwise) to the amounts allocated to PSCL unless and until they were reallocated by PSCL in future years. He said that Mr Pearey was "absolutely clear that reallocations were at the discretion of PSCL but, under the Plan, there were clear circumstances in which a recommended amount would not be reallocated to Members", including:

(1) "if Members left Odey before they had been reallocated all of their recommended amounts (this was the one Tim concentrated on most, as it was important that members understood that anything that had not been reallocated to them at the time that they left would not be reallocated). This not only incentivised Members to stay but, as noted above, if a Member's performance continued to be poor or if his attitude to risk changed, it was open to Odey ask them to leave. In that case, no reallocations would be made and that would to a certain extent "correct" volatile performance (that is, a Member would not simply receive everything in a good year with no consequences for subsequent poor years)";

(2) "if Odey became insolvent and needed to use the amount to pay creditors, or if it needed to boost its regulatory capital"; or

(3) "if the relevant Member committed particularly serious misconduct".

98. Lord Roborough said that he always understood that the amounts under the Plan were at risk. As a result, he never factored a recommended amount into any of his financial decisions until he actually received it. He said that he did not know of any Members who thought any differently: "the fact that the amount was not yours and you may never receive it was made clear to us from the outset". He explained that Mr Pearey noted at the time that, as a consequence of Members having no right to receive amounts under the Plan, there would be a tax benefit in respect of those amounts. However:

> "this did not at all outweigh the fact that significant amounts might never be paid to Members. At best, Members were resigned to the need for the Plan and many Members were unhappy. I was entirely in agreement with this view of the Plan - I did not like it, and I thought it was fundamentally unfair that awards for past performance could now be dictated by future circumstances.
>
> As explained…. Odey is a volatile, results-driven business, so there is inherent uncertainty both as to whether Members will remain in a job at Odey in years to come and as to Odey's own financial performance (I had seen this first-hand given my experience at Bailey Coates and so I did not regard Odey's potential insolvency as being at all implausible). The reality was that, under the Plan, it was quite possible that you would not receive reallocations. I therefore disagree with the suggestion from HMRC that the main purpose or

> benefit for Odey when implementing the Plan was its tax treatment. The tax benefit might have helped "sell" the Plan to members (not that they had any choice in the matter) but I (along with all of the members I have spoken to) would have much preferred to receive a slightly smaller amount straight away rather than putting it at risk for the uncertain (and later) prospect of an amount that would be marginally larger as a result of a tax benefit."

99. Lord Roborough said that, apart from the formal communications that he received in relation to the Plan, he mostly contacted Mr Pearey's team about the Plan (they were responsible for overseeing it) to check administrative details. For example, he contacted them to confirm the date on which amounts could be reallocated to him. He knew that the amounts were not his until they were reallocated but, clearly, he was interested in whether or not he would ultimately receive them:

> "From my perspective, whilst the amounts under the Plan might not always have been enough in themselves to retain a member if there was a sufficiently good opportunity elsewhere, it was a significant tie to the business."

100. He added that there was no clear way for members to check on the performance of the investments made in Odey funds with the Special Capital. Odey's internal systems that allowed its Members to track their investments never treated amounts under the Plan as belonging to a member's portfolio until they were actually reallocated in subsequent years. However, given that the amounts were invested in the Funds that a Member managed (or advised) and given that Members could obviously track the performance of those Funds in general, it would normally be possible for an analyst or fund manager to have a good idea as to the value of the investment.

101. He was not involved in any decisions about those who left Odey during the relevant period but he thought that "PSCL's refusal to make reallocations to leavers, even "good" leavers, underlines the fact that amounts under the Plan were genuinely at risk, particularly if the conditions set out in the letters from PSCL were not satisfied".

102. He thought that as a Member he had signed the Remuneration Policy and read through it but as he was not part of RemCom or ExCo at that point, he had no input into it.

Operation of the Plan - allocation of profits

103. Mr Pearey said that RemCom determined the allocation of profits to Members in largely the same way as ExCo had previously in that allocations were made by reference to the performance of the relevant individuals. Mr Pearey occasionally sat in on meetings of RemCom as part of the Odey management team and his experience was that they typically involved discussions over several hours. He said that Mr Odey was an important figure on RemCom, owing to his status within Odey, but "he was not the only voice in the room at all and the decisions were the product of these discussions". As set out by Mr Pearey and Mr Odey:

(1) The starting point for deciding fund managers' profit shares remained a proportion of the amounts generated by their Funds. Mr Pearey agreed that their profit share was intended to reward them for managing the Fund successfully "as well as other things" and he noted that "Crispin Odey set up the firm to ensure that the investment debate is constant, and so we don't necessarily want fund managers operating in isolation, so sharing investment ideas is also factored in".

(2) Over time, RemCom also analysed in more detail the level of remuneration for other roles. For example, the initial profit share decisions for

analysts became much more focused on qualitative data, as Odey attempted to ensure that they received sufficient reward for ideas and research that generated significant revenue for the business (particularly if a particular analyst had originated an investment proposal). Mr Pearey agreed that this meant that RemCom looked at what ideas analysts had that had been successfully used and, in that sense, the profit share is a way of rewarding the analyst for having had good ideas and, as he added, also "ideas which then made it into the portfolio, and then generated good returns in the portfolio".

(3) The discussions during RemCom meetings took into account a Member's performance and contribution over the current year but also previous years. Mr Pearey said that given Odey's preference for risk-takers, this was thought to be a fairer balance between monitoring for continued good performance and not placing undue emphasis on a single bad year that could be a one-off. Mr Odey said that this had been the case prior to implementation of the Plan but was even more appropriate when the Plan was in operation, as the Plan envisaged reallocations over a longer period (rather than Members benefiting from what might be a single "bumper" year) so it was only logical to assess Members over a similar period (as a single bad year might well be a one-off).

(4) Mr Odey said that RemCom's recommendations to PSCL on potential reallocations of Special Capital were made after multiple meetings. RemCom would not, however, be expected to revise a previous provisional recommendation to PSCL because the individual's performance had declined in one year from what had previously been expected. If, however, an individual performed poorly over a sufficiently long period then, in practice, it was not necessary for RemCom to consider revising its previous recommendations to PSCL because the individual would leave Odey altogether and any Award would lapse.

(5) Mr Pearey agreed that the share paid to PSCL was "technically" not a reward for its work. He said that: "It is a Member of the Partnership, but its work is for the furtherment of the group". He also agreed that the deferred share allocated to it each year was calculated as a series of slices of the potential rewards for the Members. Mr Odey agreed that the deferred share was not based on PSCL's performance but on the Members' performance. Mr Stewart also seemed to accept this when he said that at RemCom:

> "there was a bonus allocation. Then, by definition, because we had a formula, an amount would have been calculated which would have been aggregated between all the different Members - but in this case we are just talking about one Member - towards PSCL. That is how that formula would have worked."

Operation of the Plan - PSCL's role

104. The directors of PSCL were Mr Odey and Mr Philip Norman throughout the relevant period. Mr Philip Norman was not a Member and had no involvement with RemCom.

105. As noted, PSCL held board meetings or made written resolutions in January and March of each year following RemCom's recommendations to PSCL. Mr Odey said in his witness statement that:

(1) He attended PSCL board meetings or considered PSCL written resolutions three to four times a year.

(2) Odey typically wrote to PSCL prior to any board meeting at which reallocations of Special Capital were to be considered to confirm the Members

that remained at Odey although he was generally aware of this in any event. If any Awards had lapsed due to the departure of a Member from Odey, so that there was not to be any reallocation, the board made separate resolutions on what should be done with the sums representing the lapsed Awards.

(3) Decisions on whether to follow RemCom's previous provisional recommendations regarding reallocations of Special Capital were made at board meetings:

(a) As he was both a director of PSCL and a member of RemCom throughout the relevant period he was obviously aware of and agreed with the recommendations from RemCom to PSCL. However, it was by no means the case that the PSCL board meeting simply "rubberstamped" the recommendations from RemCom, if only because, as he was a PSCL director and had a clear view of Odey's business as well, if he considered that a change needed to be made, he was very well placed to do so. I note, that when Mr Odey was questioned at the hearing on one occassion he stated that there was no need for PSCL to "rubber stamp" a matter. I took him to mean, however, that it was an unnecessary formality on that occasion and not as an acceptance that PSCL did not usually consider RemCom's recommendations.

(b) The board meetings invariably started with a general update and discussion on how Odey was performing and whether anyone had left the business. That formed the necessary background to RemCom's recommendations on potential reallocations, which were then discussed. I note, however, there was little indication of any such discussion in the minutes of the meetings and Mr Odey was questioned about this at the hearing as set out below.

(c) Mr Odey was conscious that he was acting in a different capacity as a director of PSCL and these discussions were an important way of ensuring that it was appropriate for PSCL to accept RemCom's recommendations. The directors took their "responsibilities seriously and the decisions we made were important. However, given the preparation leading up to meeting, these board meetings were relatively straightforward".

106. Mr Odey noted that the fact that PSCL accepted RemCom's initial recommendations did not necessarily mean that Special Capital would ultimately be reallocated. For example, if the relevant Member had left Odey at the intended date of reallocation then any potential Award would lapse. This was consistent with the commercial objectives for the Plan, as it was directed at retaining key individuals. He referred to cases where Members had left Odey as set out below.

107. Mr Pearey co-ordinated the circulation of some of the paperwork regarding PSCL and often attended its board meetings as they were an important part of the managerial side of the business. He said that, given the "substantial discussions" that took place within Odey and RemCom before any recommendations were made, there was little reason for PSCL not to follow the recommendations of RemCom. However, he never felt that the PSCL board were simply signing off on RemCom's recommendations without any proper consideration. In his experience, the directors were well aware that they were acting in their separate capacity as directors of PSCL and, therefore, separate consideration was given to RemCom's recommendations. He noted that neither director had any financial interest in amounts subject to the Awards,

and both were well placed to evaluate whether the recommendations should be followed.

108. Mr Odey emphasised that in the letters which he sent to Members in his capacity as director of PSCL it was made clear that they would not necessarily receive a reallocation of an Award.

109. Further evidence on how PSCL operated is set out below (see [150] to [189]).

Operation of the plan in detail

Awards for 2011/12

110. In 2011/12, in total £1,730,000 of Odey's profits for that period were paid to PSCL in two tranches (a) in respect of Cash Awards, of a total of £880,000 and (b) in respect of Share Awards, of a total of £850,000.

111. In relation to the Cash Awards:

(1) On 5 January 2012, as recorded in minutes of the meeting, RemCom agreed to allocate the sum of £880,000 to PSCL comprising of specified cash deferred amounts and to recommend that it should invest "the deferred cash (net of Corporation Tax)" in specified funds for potential reallocation to specified Members (as set out in a list). It was noted that RemCom would "advise the directors of PSCL of this proposed split amongst LLP members and potential reallocation by PSCL to these members, at the sole discretion of the Directors of PSCL, and upon satisfaction of conditions as outlined in the Remuneration Policy".

(2) On 2 February 2012:

(a) RemCom produced a note to ExCo which included the following statement:

> "In accordance with the Remuneration Policy, the Remcom, has allocated a profit share totalling £12,500,000 to members of [Odey]. Of this sum £880,000 has been allocated to [PSCL] for deferral purposes. The deferred cash will be reinvested (net of Corporation Tax) by PSCL into Funds managed by the Odey Group. A further profit allocation to [OAMG] is expected by the year end."

(b) On behalf of Odey, Mr Fletcher wrote to PSCL to advise of the outcome of the RemCom meeting including the amount of the deferred share, and how it could be reinvested and reallocated amongst the Members on "satisfaction of certain conditions".

I note that the bundles did not contain any examples of any letters from Odey to the Members notifying them of the Awards made in this year.

112. On 3 February 2012, the directors of PSCL passed written resolutions to (among other things) (i) adopt the Remuneration Policy, (ii) acknowledge receipt of the sum of £880,000 as a profit allocation (gross of corporation tax), (iii) agree to the potential allocation awards to Members in accordance with RemCom's recommendation, and (iv) retain sufficient funds to pay the corporation tax charge due on the profits allocated to it. It was noted in the minutes that PSCL had received £880,000 "for value" and that RemCom advised on how the allocation could be invested and re-allocated to current partners of Odey on "satisfaction of certain conditions". Mr Pearey confirmed that the reference to "conditions" here and in the other documents was to the conditions set out in the Remuneration Policy (namely, remaining a Member of Odey and Odey having sufficient regulatory capital.)

113. In relation to the Share Awards:

(1) On 22 March 2012, as recorded in the minutes of the meeting of RemCom, RemCom agreed to allocate the sum of £850,000 to PSCL "for deferral purposes" on the basis that it should be invested in bonus shares of OHAG according to RemCom's proposed allocation among Members. It was noted that PSCL would receive a copy of the minutes detailing the proposed split among Members and potential reallocation by PSCL to these Members, "at the sole discretion of the Directors of PSCL and upon satisfaction of conditions as outlined in the Remuneration Policy".

(2) On 16 April 2012, the directors of PSCL passed written resolutions in substantially the same form as the minutes of the meeting of 3 February 2012 in relation to the Cash Awards.

114. In letters dated 3 and 13 April 2012, PSCL wrote to the relevant Members notifying them of (a) the Awards for 2011/12 so far as relevant to the particular Member, and (b) amounts of Special Capital which had been reallocated to Members for 2010/11 following a board meeting of PSCL on 7 March 2012. As regards the Cash Awards relating to 2011/12, it was stated that:

(1) Following receipt of the deferred share, PSCL "chose to re-contribute a part of its profit allocation" to Odey as Special Capital, after providing for corporation tax and ongoing expenses and that the Special Capital had been credited to its account in Odey and would be used to purchase investment assets as set out in the letter.

(2) PSCL had received an initial recommendation from RemCom that PSCL should "earmark" a specified amount of its Special Capital for potential future reallocation to the Member in connection with Odey's member incentive scheme for the year 2011/12 as set out: a specified amount of pounds worth of units to be allocated to the Member in instalments, 50% after one year and 50% after two years, upon satisfaction of conditions laid out below.

(3) It was stated that:

> "PSCL will take this recommendation into account and any further recommendations it may receive from time to time) when exercising its discretion over reallocations of the [Special Capital]. For the avoidance of doubt, please note that PSCL is not bound by any such recommendation, that PSCL retains absolute discretion over reallocation of the [Special Capital] and that you may not receive a reallocation.
>
> Conditions of allocation:
>
> Under this arrangement, you should note that any recommended reallocations will not be made in your favour where you are not a member of [Odey] at the relevant reallocation date, other than at the absolute discretion of PSCL. For example, in the event of your death or permanent incapacity, PSCL may deem it fit to make a reallocation to you (or your successors) with due consideration of the relevant terms of the Agreement.
>
> Furthermore it is unlikely that a reallocation of the [Special Capital] will be made unless [Odey] retains sufficient Regulatory Capital, or in the event of the insolvency of [Odey], as the [Special Capital] will be available to satisfy any outstanding liabilities of [Odey].
>
> The first reallocation date will be 1 March 2013, with the second anniversary falling on 1 March 2014."

The letter also set out details of the Share Awards on the basis that they would be allocated over three years in three instalments of one third with the third anniversary falling on 1 March 2015."

115. In relation to the reallocation of the first tranche of the Awards for 2011/12:

(1) On 13 March 2013:

(a) Mr Fletcher (acting on behalf of Odey) wrote to PSCL to confirm that the relevant Members of Odey had remained as such and would remain so for the foreseeable future, and that Odey had "sufficient regulatory capital for the foreseeable future".

(b) A board meeting of PSCL took place at which, as recorded in the minutes, it was noted that "certain awards under the Performance Plan vested as of 1 March 2013 and in accordance with the Remuneration Policy of [Odey]" and that a vesting schedule was tabled to the meeting. While not express in the minutes, it appears that PSCL agreed to reallocate amounts of Special Capital in accordance with the vesting schedule.

(2) On 1 June 2013, PSCL wrote to the relevant Members to notify them that (among other things), in accordance with the Remuneration Policy, and in light of their continued membership of Odey, PSCL had reallocated a portion of its Special Capital to them on the first anniversary of the 2012 allocation.

116. In relation to the reallocation of the second tranche of the Awards for 2011/12, on 5 March 2014, the same process was followed as in relation to the first tranche. In the minutes of the board meeting of PSCL, it is recorded in this case that the board members agreed to reallocate the relevant Special Capital to Members. The bundles also contained the following also dated 5 March 2014:

(1) A note from RemCom to ExCo in which RemCom noted that, in accordance with the Remuneration Policy, Odey had confirmed the Members' status as at 1 March 2014 to PSCL and Odey had transferred Special Capital from PSCL's account to the relevant Members' account and this could now be withdrawn on the Members request with a list of the relevant Special Capital.

(2) Letters from Members to Odey giving notice that they wished to withdraw the relevant Special Capital.

117. In relation to the reallocation of the third tranche of the 2011/12 Awards, on 10 March 2015 the same procedure was followed as in relation to the earlier reallocations (although on this occasion Mr Pearey sent the relevant letter to PSCL on behalf of Odey).

118. It was put to Mr Pearey that in the minutes of the meeting of PSCL's directors held on 13 March 2013 it is recorded that the vesting schedule was tabled to the meeting but not that the schedule was actually approved. He said he did not remember the discussion that day. He assumed from what then subsequently happened (namely, that the relevant reallocations of Special Capital were made), that PSCL approved the schedule. It was put to him that, given that the directors of PSCL had already resolved to carry out the Remuneration Policy and to agree to the potential reallocations as recommended to them over a year in advance (in the meetings on 3 February and 16 April 2012), in fact, they had already resolved to make these payments out on the dates shown in the vesting schedule. Mr Pearey did not agree. He thought the failure to record approval of the "vesting schedule" was just poor minute taking.

119. When the same question was put to Mr Odey, he said simply: "They [the relevant Members] have fulfilled the criteria". When it was put to him that, therefore, there did not need to be a second decision taken by PSCL on 13 March 2013 as regards the reallocation of Special Capital, he said: "Our point has always been to say if they are still there and a partner, then they would receive - they would receive the money that had been deferred before".

Awards for 2012/13

120. For 2012/13 only Cash Awards were made in respect of which £4,647,716 of Odey's profits was paid to PSCL.

(1) On 9 January 2013, on behalf of Odey, Mr Fletcher wrote to the Members to notify them of their profit allocation in respect of the calendar year ending on 31 December 2012. The letters were all in the same form. For example, the letter to Mr Pearey stated that:

> "In addition to your monthly drawings, *you have been allocated a share of the Partnership income for the period to 31 December 2012 of £825,000.*
>
> In accordance with the deferral arrangements in the Remuneration Policy, the aggregate of: 20% of the sum between £500k and £1m will be invested, net of Corporation Tax (24%), in OAM Funds by [PSCL]. This is equal to £49,400 worth of shares in the Funds. *PSCL will transfer this investment to you in two annual instalments* at "no gain no loss" for tax purposes, thus the only further tax liability will be Capital gains tax upon sale of the shares by you, based on any uplift in value over the original base cost (ie PSCL's purchase price). *These deferral arrangements are subject to PSCL's policies and discretion, and PSCL will confirm the details to you in March.*
>
> The remaining sum of £760,000 will be paid to you directly and is gross of any taxes for which you will be responsible." (Emphasis added.)

(2) On 15 January 2013:

(a) As recorded in the minutes, at a RemCom meeting attended by Mr Fletcher and Mr Odey, RemCom agreed to a profit allocation to PSCL of £4,647,716 comprising "proposed cash deferred amounts" as set out in a schedule with a "further recommendation that the deferred cash (net of Corporation Tax) should be invested" in the Funds set out by each Member's name. It was noted that PSCL would receive a copy of the minutes detailing the proposed split amongst the Members and that the "potential reallocation by PSCL to these Members" was "at the sole discretion of the Directors of PSCL and upon satisfaction of conditions as outlined in the Remuneration Policy".

(b) RemCom produced a note to ExCo advising of the outcome of the RemCom meeting including that £4,647,716 was allocated to PSCL and that the "deferred cash will be reinvested (net of Corporation Tax) by [PSCL] into Funds Managed by the Odey Group. A further profit allocation to [OAMG] is expected by the year end".

(c) On 24 January 2013:

(i) On behalf of Odey, Mr Fletcher wrote to PSCL to advise of Mr Stewart's resignation as a member of Odey and of the allocation of profits to PSCL and "for the consideration of PSCL" provided RemCom's proposed "breakdown of this allocation and subsequent

investment (net of Corporation Tax) which, in accordance with the Remuneration Policy, could be re-allocated to partners upon satisfaction of certain conditions".

(ii) The directors of PSCL made written resolutions essentially in the same form as those described in relation to the 2011/12 year.

(iii) In a separate written resolution the directors of PSCL noted that (A) Mr Stewart had resigned as a partner in Odey, (B) "in accordance with the remuneration policy agreed with the LLP", a proportion of the award held as assets in the company's Special Capital account with Odey, "for the future benefit of" Mr Stewart, "would lapse", shares and units relating to the relevant Special Capital had been sold and the proceeds received would be held for future awards and they resolved to approve the sale of the shares and units and to authorise the company secretary to sign any documents to give effect to the sale.

(3) On 4 April 2013 RemCom sent a note to ExCo confirming it had allocated a profit share totalling £4,571,533 to Members.

(4) On 1 June 2013, PSCL wrote to the relevant Members to notify them of (among other things) the potential amounts they could receive pursuant to the allocation of profits to PSCL. Essentially this contained the same wording as set out above.

(5) The funds were reallocated in two tranches as determined on 5 March 2014 and 10 March 2015 under the same procedure as described in relation to the earlier year set out above.

121. It was put to Mr Pearey that in the letters Odey sent to Members in 2013 each Member was told he was allocated a share of the partnership income for the period to 31 December 2012 which appeared to include the individual share. He said that:

> "in order for [Members] to understand what is being accounted for within the Remuneration Policy, we felt it was necessary to set out a total figure and then an amount which would be allocated to PSCL, and then therefore that was the amount which was potentially available to partners at a future date".

122. When a similar question was put to Mr Stewart he said:

> "The answer is that at [RemCom], there was a bonus allocation. Then, by definition, because we had a formula, an amount would have been calculated which would have been aggregated between all the different Members - but in this case we are just talking about one Member - towards PSCL. That is how that formula would have worked."

123. In re-examination, when asked what he understood the final words of the letters from PSCL to Members to mean, Mr Pearey said that "in extremis… if I were no longer a member of Odey at the time of the various anniversaries when they fell due, then I would not receive any reallocation of capital". He thought that the circumstances in which a Member might not get a re-allocation also included if the business were in need of regulatory capital or if there were any other form of liability which may have hit the business at the time. When he was then asked if he understood that PSCL might just say "I'm not going to give it [the reallocation of Special Capital] to you" he replied that "there was that possibility, certainly". I note that, in effect Mr Pearey was prompted into this last response and so I give no weight to it.

124. When looking at these letters, it was put to Mr Odey that they meant that if the specified date came around and there was no regulatory capital problem and the Member was still a member of Odey, the Member would get the award. He said "he

gets the reallocation". It was put to him that the letters also said that even if the individual was not a Member and there was not enough regulatory capital, PSCL had discretion to make a reallocation but in practice, that never happened. He said:

> "Yes. I mean, what was interesting again…..of all the people who left - and several partners did leave and they left, seemingly, money on the table, there is not one single letter from them saying that they ever thought that they had any rights to any of this; ie those letters made sense to them and they made sense to us".

125. It was put to him that in the letters from PSCL notifying Members of reallocations of Special Capital it was stated that: "In accordance with the Remuneration Policy and in light of your continued membership, the reallocation has been made" and that was why the reallocation was made. He agreed that was the case and that no other conditions were put forward.

126. It was put to Mr Pearey that the letters notifying Members of their Cash Awards were sent to them on 9 January 2013 but, according to the minutes, the meeting at which the profit allocations were decided upon took place only later on 15 January 2013. Mr Pearey said that he suspected the minutes were incorrectly dated or that, at the meeting, RemCom ratified a decision which was made over a long period of time in the run-up to the January final profit allocation. He noted that the conversation on profit allocation would probably have started in October but "things are very fluid because of course much of the revenue is dependent on a calendar year end and the fund is live right up until 31 December, so even into early January we are slightly unsure of the figures". He added that the letters could not have been sent to Members without RemCom agreeing on the figures.

2013/14 awards

127. In 2013/14 £35,262,639 of profits were allocated to PSCL comprising (i) £22,167,608 in Cash Awards and (ii) £13,095,031 in Share Awards.

128. In relation to the Cash Awards:

(1) On 8 January 2014, on behalf of Odey, Mr Fletcher wrote to the Members to notify them of the Cash Awards. The letters were differently worded to those for 2012/13. For example, the letter to Mr Pearey contained the following:

> "…you have been allocated a share of the Partnership profit of "1,450,000. This will be paid to you directly and is gross of any taxes for which you will be responsible.
>
> <u>Long Term Incentives</u>
>
> In accordance with the Remuneration Policy, a further £300,000 will be invested (net of Corporation Tax) in OAM Funds by [PSCL] and, subject to your continuing membership of the Partnership, PSCL will transfer this investment to you in two annual instalments. These arrangements are subject to PSCL's policies and discretions, and PSCL will confirm the details to you in March. This is calculated on the basis of the level of the notional gross allocation as follows: 20% of the sum between £500k and £1m and 25% of £1-1.5m and 30% of £1.502m."

(2) On 14 January 2014:

(a) A RemCom meeting took place at which the profit allocation to PSCL in respect of the Cash Awards was agreed. The minutes are recorded on substantially the same terms as those described above. It was also during this meeting that the revised Remuneration Policy was approved.

(b) RemCom produced a Note to ExCo advising of the outcome of the RemCom meeting including the allocation of profits to PSCL in respect of the Cash Awards.

(3) On 23 January 2014, on behalf of Odey, Mr Fletcher wrote to PSCL to advise of (i) the revised Remuneration Policy, and (ii) the outcome of the RemCom meeting, including the allocation of profits to PSCL in respect of the Cash Awards. This note was in the same form as that described above.

(4) On 24 January 2014, the directors of PSCL passed written resolutions in substantially the same form as those set out above.

(5) On 5 March 2014, PSCL wrote to the relevant Members of Odey to notify them of (among other things) the potential cash amounts they could receive pursuant to the Cash Awards.

129. In relation to the Share Awards:

(1) On or around 18 March 2014:

(a) A RemCom meeting took place during which a profit allocation of £13,095,031 to PSCL in relation to Share Awards was agreed as well as a further recommendation to invest that sum in bonus shares on the basis of a proposed split and potential reallocation to specified Members.

(b) RemCom sent a note to ExCo advising them of the outcome of the RemCom meeting.

(c) Mr David Fletcher (on behalf of Odey) wrote to PSCL to advise of the outcome of the RemCom meeting in respect of the Share Awards.

(2) On 19 March 2014, the directors of PSCL passed written resolutions in substantially the same form as those set out above.

(3) On 1 April 2014, PSCL notified the relevant Members of the potential shares they could receive pursuant to the Share Awards.

130. The reallocations were made in three tranches as determined on 10 March 2015, 18 March 2016 and 7 March 2017 using the same procedure as set out above.

131. Mr Pearey thought that the Members were notified of the Cash Awards before the relevant meetings of RemCom were held approving the awards for the same reasons as set out above (see [126]).

132. Mr Pearey was asked why the letters to Members in this year were differently worded to those for the previous year in that, in each case, the profit share which was actually paid to the Member and the individual share were separately identified. He said that when revisiting the Remuneration Policy each year the wording is slightly tweaked to ensure the policy is clear. Sometimes feedback from Members also helps:

> "The nomenclature in the letters does not reflect any change in how the plan operated….. in effect, they say nothing different. One is simply stating a total amount up front and explaining how an aspect of that may be allocated to an individual at a later date, and a final figure for which they are directly responsible for, for taxes. And I see the same aspect within the second letter in 2014."

133. It was put to him that in 2013, in response to enquiries HMRC raised into Mr Stewart's tax return for the 2011/12 tax year, Mr Stewart said that: "No amount of profit allocated to me by the LLP was deferred in any year" and that this statement fits much better with the letters Odey sent to Members in 2013/14 than the differently worded letters of 2012/13. Mr Pearey did not agree that any of the letters suggested that an individual share was actually allocated to a Member but deferred or that the change in wording in the letters was made in response to HMRC's enquiries:

> "I think this is in and around how you classify what is profit allocation, or what is a potential deferral or a potential re-allocation of capital. I think in 2013 that probably is not terribly clear, but I think it gets clearer in 2014. And indeed I suspect this is what David Stewart's letter is trying to also highlight, is the fact that this was about reallocation or potential reallocation of capital."

134. He added that any form of letters to employees or members of staff, "are not templates set in stone which are simply updated year in year out for numbers or names"; rather they were reviewed every year and Odey frequently made changes to how any letter is presented".

135. It was put to Mr Pearey that there was no mention of any business update in the minutes of PSCL's meetings set out above (and some of those relating to other years). He said that PSCL was certainly kept abreast of Odey's performance. For example, it received management accounts and updates as to fund performance and other information, in particular, as Mr Odey was on RemCom as well. It was put to him that when the directors of PSCL decided whether or not to reallocate Special Capital there could not have been much to discuss given they had before them only (a) the "vesting schedule" which set out when reallocations fell due on the basis of the earlier recommendations of RemCom, and (b) confirmation of who was still a Member. He said that "certainly there were meetings where there was more information, but:

> "the truth is if there were any exceptions to the recommendations, Crispin Odey was in a very good place to suggest that a potential re-allocation should not occur. So, I think perhaps one should see these on an exceptions-only basis, rather than another detailed three-month discussion period as to what potential reallocation should occur."

136. It was put to Mr Pearey that in the relevant minutes it was recorded that PSCL had received the deferred share from Odey "for value" and essentially that this must mean that PSCL had then agreed, in effect, to use the funds received in accordance with the Remuneration Policy and that was also demonstrated by the vesting schedule showing what was due to vest on the basis of PSCL carrying out that policy. He accepted that when PSCL accepted money on those terms, it held that money for the future benefit of the group. He did not, however, accept that PSCL held the money for the benefit of particular individuals (see [156] below].

137. It was put to him that in a later year (2016) the meeting of the board of PSCL in relation to awards took place on 21 March but the letters to Members were dated 18 March. Mr Pearey said that he suspected that given how busy Crispin Odey's diary is:

> "in order to get him to sign letters or resolutions, often it is a case of finding a 10-minute slot and sitting him down with a bunch of papers to get signed, sometimes in advance. And then hence why it is dated the 18th to reflect the original intended meeting date, which obviously then had to be put back. But I see it as no more than efficiency, perhaps, on probably Crispin's PA's part, I presume, in terms of getting these letters signed, thus ready, but requires a resolution or requires the PSCL board meeting to take place, presumably."

Treatment of members who left before reallocation

138. A number of Members ceased to be members of Odey during the operation of the Remuneration Policy and after RemCom had decided that they were eligible for one or more Awards. The table below sets out those Members, the dates on which they ceased to be members and the instalments of any Awards that were not received by them following their departure:

Member	Date of departure	Instalments not received
Ben Lambert	3 April 2012	Second and third instalments of the Share Award notified to him by PSCL on 6 April 2011 First and second instalments of the Cash Award notified to him by PSCL on 3 April 2012
David Stewart	31 December 2012	Second and third instalments of Share Award notified to him by PSCL on 6 April 2011 First and second instalments of Cash Award notified to him by PSCL on 13 April 2012
Jamie Wood	11 June 2015	Second instalment of Cash Award notified to him by PSCL on 5 March 2014
Andrew Sandler	22 October 2015	Second instalment of Cash Award notified to him by PSCL on 5 March 2014

139. Mr Pearey said that Odey took a strict approach to applying the Remuneration Policy when Members left Odey; the policy was applied regardless of whether the individual left the business entirely or retained some link to Odey (for example, as Mr Stewart did). He noted that if such Members are to be taxed on the full individual shares in the year of allocation, as HMRC now suggest, they would suffer a tax charge on amounts they never actually received.

140. Mr Odey also said that there was no suggestion of special treatment for any of the leavers; when they left, any Special Capital that had been recommended for reallocation but not already reallocated to them was instead retained for PSCL's and Odey's future use, which could include future awards to other Members who had really built up the value of the business.

141. The most senior leaver was Mr Stewart. On 19 December 2012, Mr Pearey wrote to Mr Stewart on behalf of Odey to confirm (amongst other matters) that any potential reallocation of 211,636 bonus shares and of cash in the sum of £74,000 would lapse entirely in accordance with the Remuneration Policy and that the bonus shares that he had had already received were to be repurchased. This was subsequently confirmed by written resolutions of the directors of PSCL on 24 January 2013. PSCL resolved to sell the units representing the cash amounts and the bonus shares and to pay the proceeds into PSCL's bank account to be "held for future awards". Mr Odey and Mr Stewart confirmed that this is what took place. Mr Stewart noted that this was:

> "exactly what I expected to happen, and I would not have thought of challenging this. I always knew that, if I left, I would not receive further payments from the Plan and I saw that as part of the deal - I knew the Policy,

> and we had already taken this approach while I was CEO with Ben Lambert, who resigned in April 2012 and did not receive any amounts that had not been reallocated by the time of his resignation".

142. Mr Stewart explained that he continued to work with Odey in a non-executive director capacity and to provide certain consultancy services, particularly in relation to overseeing Odey's compliance function, and was separately paid a market rate for these services as negotiated with Mr Fletcher. In addition, he agreed to act as one of the directors of PSCL, along with Mr Odey and Mr Norman. Mr Pearey confirmed that at no point did Odey make any payment to Mr Stewart that was intended to compensate him for Special Capital which he did not receive under the Plan due to his departure from Odey.

143. Both Mr Odey and Mr Pearey gave details of the departure of Mr Jamie Wood as the Member who had been provisionally recommended to receive the highest individual share under the Remuneration Policy. Mr Odey set out that Mr Wood was a research analyst who had performed particularly strongly during 2013. On 5 March 2014 he was notified that he could potentially be reallocated cash of around £2.3 million for his performance in financial year 2013 in two tranches. The second tranche which had not been reallocated to Mr Wood at the point of his departure was worth approximately £1 million. Mr Wood resigned from Odey when Mr Odey refused his request to be made Head of Research with autonomy to manage the team's personnel, citing lack of career progression. Mr Odey said that at the time:

> "while we were disappointed to lose Jamie as he was a talented analyst, he left on good terms with our best wishes for his future career. Despite being a "good leaver", when he left, it was clear that he no longer satisfied the conditions to be eligible to be reallocated the second tranche of this amount, as he would no longer be a member in March 2016. As a result, Jamie was not reallocated the second tranche, and he never received this amount (or anything equivalent to it)."

144. To Mr Odey's mind, this demonstrates that RemCom's recommendations did not create any obligation on PSCL to pay the relevant amounts to Members - if a Member left before the reallocation date, they would receive no reallocation of Special Capital and he was not aware of any Member ever suggesting that he was entitled to the amounts that had been allocated to PSCL.

145. Mr Pearey noted that, while Mr Wood had some very good years at Odey (at his best, he would describe him as a brilliant analyst) several of his positions have, since his departure, performed poorly. He considered this demonstrates the volatility of Odey's business and the variability of the performance of its key Members.

146. In his witness statement, Mr Pearey said that the above are "examples where PSCL declined to follow RemCom's initial recommendation". At the hearing it was put to him that actually the fact that such Members did not receive any reallocation was in accordance with the recommendations that Odey made to PSCL. He agreed and said that perhaps he should have said in his witness statement that PSCL "declined to follow the initial cash recommendation", or words to that effect. It was put to him that the documents referred to leavers as "forfeiting" their allocations and that a person cannot forfeit something unless they were entitled to it. He said that this was perhaps not the best word; the documents should have said that "there are no terms for non-reallocation".

End of PSCL's involvement

147. During the first half of 2015, PSCL ceased to be involved in the arrangements but the Remuneration Policy remained in place. Mr Pearey explained that this was a

result of legislative changes introduced with effect from 5 April 2014. When these changes were announced, ExCo decided that Odey would allocate the deferred share to a "notional partner" instead of to PSCL and, on 10 March 2015, the board of PSCL agreed that it would no longer participate in the Plan. Under the new rules, amounts allocated to a notional partner were subject to income tax. However, the basic principles for the Plan have remained part of the remuneration arrangements for Odey going forward and the Remuneration Policy did not need to undergo any material changes.

148. In Mr Pearey's view, the continued use of the Remuneration Policy reflects the positive impact that the Plan has had on the business of Odey as a whole. The decision to change the arrangements was solely attributable to the legislative changes described above, rather than any concerns about the merits of the Plan. Put simply:

> "the new rules (including those introduced in relation to notional partners of LLPs) required us to adopt a different mechanism but enabled us to retain the same principled approach to deferral, and the Remuneration Policy remains in place with the core principles unchanged. In my view, the Plan achieved all of the commercial objectives….. I completely reject any suggestion that the arrangements were artificial in any way. It is no exaggeration to say that, if I could turn back the clock to 2010/2011, then I would not change what happened."

149. Mr Odey said that as he understood it, the various legislative changes both rendered it unnecessary to have PSCL involved and, on a more personal level, risked creating an extremely unfair tax result because he could potentially be subject to income tax on any allocation of profits to PSCL despite not being subject to the Plan. He also noted that the Remuneration Policy, and in particular the use of a deferral mechanism akin to the Plan, have remained a part of the remuneration arrangements for Odey and said that it is now industry standard for these sorts of arrangements to be in place. He said:

> "The Plan itself proved to be far more effective and beneficial for the business than I expected. In relation to PSCL, its importance as a "font of capital" that is available to the business has only grown as the amounts it holds have grown progressively larger owing to Odey's increased profitability and more members having departed without being reallocated any amounts their provisional deferral award."

Further evidence on discretion of RemCom, ExCo and PSCL

150. Mr Pearey said that RemCom, as a sub-committee of ExCo, had considerable discretion and flexibility as to the Awards and the recommendations it made and, once RemCom had allocated amounts to PSCL, PSCL had "absolute discretion to deal with the funds as it liked". He clarified that he accepted that, under the terms of the 2011 LLP Agreement, once PSCL contributed the deferred share to Odey as Special Capital, ExCo had discretion as to how the funds should be invested.

151. Mr Pearey said that Members were asked to confirm to Odey which Fund(s) they would prefer their individual shares to be invested in. While the vast majority of Members nominated their own Funds voluntarily, if a Member did not, ExCo spoke to him to discuss the importance of investing in his own fund. Even though the Members' views were not binding and they could simply be ignored, it was felt that to override a Member's preference would have risked disincentivising him. The preference was always to resolve any issue by discussion between a member of ExCo and the relevant Member. In practice, this was rarely an issue.

152. He described the Remuneration Policy as the agreed policy which "we followed" and agreed in general terms that it was important that the Remuneration

Policy was adhered to. It was put to him that it was important that both Odey and PSCL acted in accordance with the Remuneration Policy. He said:

> "Yes. I mean, ultimately, PSCL is there for the furtherment of the group, as determined by the business purpose trust which structured it. In keeping with that, Crispin Odey was… a director of PSCL and obviously was a part of [ExCo], so the alignment of interest is obvious."

153. Mr Pearey was asked if it was fair to say that PSCL would make reallocations of Special Capital in accordance with the Remuneration Policy, subject to the hurdle of capital adequacy and the relevant Members still being members of Odey. He said that it turned out PSCL did so during the years the Plan was in place but ultimately the directors of PSCL "always had the discretion" as to whether to reallocate Special Capital taking into account the express conditions set out in the Remuneration Policy. Members had no right to ask PSCL to do so. He noted that it was clear in the letters sent to Members that any reallocation by PSCL was "subject to PSCL's policies and discretion". He noted that PSCL received the Remuneration Policy for its own review. He could not think of an example where PSCL did not follow the recommendations of RemCom.

154. Mr Pearey agreed that the board of PSCL determined the reallocation of Special Capital in accordance with their duties and the Remuneration Policy upon satisfaction of certain commercial hurdles although he thought it was perhaps more accurate to say "with acknowledgement of the Remuneration Policy". He was not worried that his Awards could just be given to someone else such as Mr Odey. He thought that, given he had been involved in the inception and drafting of the Remuneration Policy, he was perhaps more comfortable with it than other Members to whom it was simply presented. It was perhaps just through a lack of familiarity that people may have had such concerns.

155. When asked if it is fair to describe the Plan as a "deferred remuneration arrangement", he said: "No, I prefer to call it a "retention and incentivisation plan". He accepted the Plan is connected to remuneration and that its objective is the incentivisation and the retention of Members. He would not describe it as "deferred", however, because the sums allocated to PSCL were not really the Members' funds, rather, in effect, it was a "potential re-allocation of capital, rather than a deferral of profit allocations".

156. Mr Pearey did not accept fully that for the Plan to operate as a retention and incentivisation arrangement, whenever PSCL received the deferred share it held the monies relating to the particular individual shares for the future benefit of somebody in particular. He said that the monies were held for the benefit of the group but noted that any Award was predicated on Odey still having enough regulatory capital and being profitable, the Member still being a member of Odey and any other surrounding circumstances. When the question was put to him again, he said that subject to satisfaction of the applicable conditions, "an individual should have transparency as to what their potential re-allocation could be, predicated on them remaining a partner in the business. We have quite a high turnover of members in our firm. It is a very pressurised business, a very performance driven business, so remaining a Member is of itself part of your ongoing performance in the firm".

157. Mr Pearey agreed that it was important that if Members left, they did not get the relevant monies and that they expected to get the monies if they did not leave. He said that any form of incentivisation planning should be clear as to what the potential benefits could be for an individual to stay on:

> "particularly in our industry, you could have a very good year, and there could be a significant payout, but one wants to ensure that individuals are incentivised to think about the longer term, not just in terms of the investments in their own funds, but by aligning their own potential allocation with those funds and they are thinking longer term".

158. In re-examination he clarified that he thought the Remuneration Policy made it clear that the Plan was not legally binding in the sense that Members had "no right to any potential award which they may receive".

159. In cross-examination Mr Odey initially appeared to confirm that, in his view, the only conditions or criteria for a Member to receive reallocations of Special Capital were that (a) they remained Members on the relevant date, and (b) Odey did not need the relevant funds to strengthen its capital position. However, he then added that "it [the reallocation of Special Capital] was at the discretion, always, of PSCL actually". He confirmed that no one who remained a Member for the requisite period did not get a reallocation of Special Capital. He noted that Odey did not make losses in the relevant period so that there was no reason "to call in any of the contingent alternatives". He said that Odey was:

> "going from a position whereby partners/employees got the whole of their bonuses in one year to something that was, basically, being deferred, and therefore there was a need for transparency for the partners/employees, so they knew what they might get, but we, basically, put ourselves under no obligation."

160. He agreed that in referring to "transparency" he meant that Odey had set out some conditions as to the circumstances in which Members would lose what had been deferred. He said those circumstances included if a Member in any way misbehaved in some way. He confirmed that, as set out in the Remuneration Policy, in practice, RemCom was the final arbiter in deciding "the deferral terms" including "how deferred funds are invested".

161. Mr Odey accepted that the individual shares were based on the Members' performance in the relevant year which they earned through their work for Odey in that year as rewards for that work. He pointed out that Members would not know how much they could get under the Award as it depended on the performance of the Fund. It was put to him that there were not two separate questions for RemCom (how much should a Member get and how much should be deferred?) but rather that the amount deferred follows from the amount the Member was to get. He said: "Exactly". The only reason he could think of for a Member not to receive a potential reallocation of Special Capital, in addition to the reasons set out in the letters to them, was "if Odey was in trouble and needed a rights issue". He thought that, barring those circumstances, it would be unfair if Members did not get the Awards.

162. He agreed that, in practice, Members always got the Award unless they left Odey before the relevant date. As noted above, he remarked there is not one single letter from any of those who left during the relevant period saying that they ever thought that they had any rights to any reallocation of Special Capital.

163. He agreed that PSCL would not simply make a reallocation of Special Capital which was intended for another (as set out in RemCom's recommendations) but:

> "PSCL, I think, had the ability to do anything. It had full discretion. I think the issue was that if you did start sort of messing around like that, you just wouldn't have a partnership for very long, so it was circumscribed as much by the natural sense of, if I had told somebody that was going to happen, it was going to happen."

164. He agreed that PSCL was also circumscribed by the Remuneration Policy and said that PSCL would "naturally" comply with that policy. It was put to him that to comply with the policy, at the stage reallocations of Special Capital were due to be made according to the vesting schedule, PSCL had to accept RemCom's recommendations. He said:

> "I sat on RemCom and that I also sat on PSCL, so you had somebody who was coming through with essentially, all of the information and knowledge of what the RemCom had decided on, and basically, it could help Philip and myself to decide the implementation of that through PSCL. That's how it worked. This was not a large firm."

165. He said that at the meetings of PSCL's directors:

> "the crucial thing was: how is [Odey] doing; is it okay; are the partners still there; what re-allocations are naturally being made; and also what allocations had been determined by the previous RemCom meeting we just had. That was the format."

166. He thought that the minutes of the relevant meetings did not show any discussion about how Odey was doing because, in practice, it was not necessary to discuss that at the time, as Odey was doing well. However, in his view, that does not detract from the fact that a big consideration for PSCL was whether in fact Odey had sufficient money or whether it needed the monies. He noted that PSCL was "a capital buffer company" for Odey for the first time. He said that the firm could incur significant liabilities if it had underwritten the performance of the funds; in other words, if it had promised an investor that it would get its money back. That was something Odey had done.

167. It was put to him that in the 2015/16 year, the performance fees had dropped a lot compared to the previous year and he was asked whether that was a bad year or still a good year. He said it was not as good as previous years and PSCL was looking at the capital demands of Odey. It was put to him that what PSCL considered was only if Odey was in need of additional capital. He said: "Yes, how close was it. How in danger were we…. to demanding capital, obviously that was the big issue for PSCL."

168. Mr Odey agreed that:

(1) The funds PSCL held as Special Capital were all hypothecated to the future benefit of somebody or, as it was put in the documents, "earmarked" for their benefit.

(2) At the reallocation of Special Capital stage, the only thing that was before PSCL for consideration was whether the relevant individuals were still Members and whether there was any problem with the regulatory capital required by Odey: "Our point has always been to say if they are still there and a partner, then they would receive….the money that had been deferred before".

(3) He had duties to PSCL as a director of it and had a fiduciary role. He could not just give PSCL's money away to anybody he felt like; it was not his to play with.

(4) PSCL adopted the Remuneration Policy and made awards of Special Capital in accordance with that policy and not otherwise.

(5) As the Plan was a way of retaining key individuals, if a Member left Odey he would not get the money but if he stayed he would.

(6) When he was acting as a director of PSCL in reallocating Special Capital, he was not making presents to the relevant Members which would come as a surprise to them like Christmas gifts.

169. He added:

> "And in a way, because we were moving from something in which people were paid immediately to something which was staggered payment, we needed a system which was as transparent as possible, so that they, basically as partners, had some kind of confidence that they might get this if they stayed……"

170. When it was put to him again that in acting as a director of PSCL, he was not making presents to Members, he agreed but noted that if they left, "they never anticipated – they never even believed they had any rights….They didn't get the money…Remember, we had that discretion; we just never exercised it".

171. Mr Odey agreed that it was fair to say the arrangement was a deferral arrangement as well as being an incentive scheme but said "remember that the FSA was very keen on the whole idea that bonuses should be staggered over a longer period". He agreed that (a) if PSCL just gave Special Capital to somebody other than the intended recipient that would not be a deferral arrangement or incentive and said it would probably fall foul of the FSA, (b) for the plan to work and be in accordance with the FSA's Code, PSCL had to act consistently with the Remuneration Policy and that was why it was owned by a purpose trust and that he was a director of PSCL so people could be confident that PSCL would not act in an unexpected way. He accepted that "the expected manner" was that what PSCL received, unless there was a call on capital, would be paid out in the staggered form or lapse if the Member had left and in fact PSCL did always act in accordance with that intention.

172. Mr Stewart agreed that once the Remuneration Policy was approved by Odey, his understanding was that the firm had to comply with it and that the conditions for the receipt of Special Capital were that a Member remained a partner and Odey did not need to increase its capital. When it was put to him that the documents make the deferral element of the Remuneration Policy look generally quite predictable he said, in setting the policy up:

> "The most important thing for me, as the CEO, was continuity of the business, and therefore the people. The people are the most important bit of a fund management company. So, if I could retain them and incentivise them to be retained, that was what we were really thinking about at the time. So, I don't think it is as predictable because if someone then left, you would then have that money available to further, potentially, recruit another person into the business using that money….
>
> ……[how to use lapsed awards] would have been entirely due to PSCL…
>
> ….. as an individual, rather than with my CEO hat on, and certainly the way it was described by me to others at the time, it certainly wasn't our money and it could go - ie, it wouldn't be something I would put in my little book, and say, "This belongs to me"; it belonged to the company, to Odey. It was part of Odey's capital."

173. He said, in effect, that the Members knew from the Remuneration policy, that:

> "if they had stayed in the company for two or three years on this rolling basis and we hadn't had an internal capital issue, and they had behaved, there was a pretty good chance it was going to come back to them, because we were trying to run a mature organisation in terms of being fair to people, but it was certainly not guaranteed."

174. He could not recall anyone losing an Award due to their behaviour.

175. It was put to Mr Stewart that under clause 10.12A of the LLP Agreement, it was ExCo which had power over which fund the investment was to be made, rather than PSCL. He said:

> "when we [RemCom] were doing the allocations, we would certainly consult with members and encourage them. In my case, I would encourage them where they were actually a fund manager, to invest in their own fund……once we got the incentive programme organised, that's what we wanted people to do. We wanted them to be in the correct funds because that was one of the issues we had when I arrived and we lost the Japanese fund. The individual did not have enough in that fund."

176. When the question was put to him again he said that PSCL had the rights to change anything it wanted to.

177. Mr Stewart explained that Mr Norman was an external independent director who contributed discipline and order and made sure the rules were followed. As regards his own role, he said:

> "I then came on to this committee once I had resigned, that at least the partners would have known that there was someone there who understood the system, as well as Crispin, to make sure there was balance in the decision-making process….
>
> Just so the debate could go on as to what was going on in the partnership, whether there was a need for capital. There was another pair of eyes that really understood the business, whereas Philip Norman, I think, you would describe as a "technocrat"."

178. He described the Special Capital as "an aggregate sum that belonged to the partnership" and "effectively partnership assets" which "certainly…once it had been allocated, did not belong…to the individuals". Rather:

> "It was an aggregate amount that, in the event of something happening, could be used by the partnership on its balance sheet, which as the CEO of course, I was delighted with because we had gone through the financial crisis and I wanted to strengthen the balance sheet…. [although it was always invested in particular funds] the money could be liquidated if the partnership was in trouble. It didn't belong to the individuals."

179. Mr Stewart agreed, however, that the money was held for the future benefit of particular individuals if all the relevant conditions were met and, if that was the case and there had been no need to use it, the individual would get the money in due course as per the Plan. He later suggested that Members would not receive an allocation of Special Capital if there had been other needs for the Partnership or if the individual had behaved badly.

180. Mr Stewart noted that he left Odey two years after the Plan was put in place but he thought that "it was a thing moving in the right direction, in terms of making Odey a more secure business, and that was the objective". He agreed that in every case PSCL agreed the recommended allocation proportion. When he was asked if PSCL could instead have added one Member's intended allocation to another he said that "they could do anything, but - in the sense, they had discretion to do that, but I think it would be unusual, in terms of your incentivisation programme, unless something had happened to [the Member]….again, I think I was probably on the board at that point to see fair play was being implemented".

181. It was put to Mr Stewart that his role was also to see that the Remuneration Policy was complied with. He said:

> "Yes. But remember, we also had Crispin, who was part of that as a director as well…..So, if he felt strongly that there needed to be a change to that

policy, there was technically nothing to stop him making a recommendation to PSCL to do so. So, your example is correct, it could happen, but I, certainly as a director, would want to know why it was going to happen."

182. It was put to him that he had fiduciary obligations and that the directors could not just do whatever they felt like with PSCL's assets and that as PSCL has resolved to adopt the Remuneration Policy, it would do things that accorded with, rather than breached, that policy. He thought that was right but added:

> "I do come back to this idea of bad behaviour. There could have been a situation by which the allocation had happened, then in fact Crispin had taken a different view on someone and it would be us to look to Crispin - Phil and I would look to Crispin. We are not in the business anymore. I am only an adviser. If Crispin said, "I'm not going to pay that person, something has gone wrong here", I think we would be duty bound to listen to him.
>
> He was the owner, a dominant person in the company, as you know, so it is not beyond the realms of possibility that that could have happened. It didn't, but it could have happened."

183. It was put to Mr Stewart that Mr Odey would need to have a good reason to make that kind of suggestion. He said: "I would want it minuted and, as a director, I would want to make sure due process was followed". When it was put to him that he could not "go around allocating different people than are expected just because you feel like it", he replied:

> "No, I come back to the earlier point. This was meant to be - certainly as I set it up originally when I was CEO - was to incentivise people. So, if one abused it -- someone made the point earlier today – you wouldn't keep your staff for very long."

184. It was put to him that leaving aside someone behaving very badly or the firm needing to call in the money; the other part of the deal is: "if you stay, you will get what is coming to you?". He agreed and said that is what a remuneration policy and an incentive scheme should be.

185. He thought that the Members would have been shown the draft versions of the Remuneration Policy although he could not remember. He agreed that the Members would have known that they would not have received anything if they left and subject to the other points he made above as regards behaviour and needing capital, they would have expected to receive it if they stayed.

186. In re-examination, Mr Stewart was asked what he understood as the meaning of the wording in the Remuneration Policy that it was not intended that the award process including deferral arrangements should be "contractual". He said that it meant that the "money was never yours until you received it".

187. Lord Roborough was asked whether the reallocations of Special Capital he received came as a surprise to him at the time. He said it was not a surprise: "Based on what I understood about the Plan and how it operated, there was no reason at that point not to be reallocated those amounts from PSCL" but if he had left the firm then he "certainly" would not have expected to receive the proceeds and he:

> "was aware of the financial state of the company and therefore knew that we didn't need any extra capital…..we understood that this wasn't our money. Other things could happen, but there was no reason why there should have been anything else happening…Potentially. It is hard to imagine what those other things could be."

188. He said that whilst he remained a Member at the relevant time he would expect to get the reallocation, but that was "subject to the health of the company. Yes, it wasn't my money and therefore there were risks to receiving that money….and as the

date approached, you know, one's expectation of receiving it might increase". He added that "it was always our understanding that this was a separate entity who owned that capital, and what they did with it was up to them, subject to remuneration policy, et cetera".

189. Lord Roborough confirmed that when the Plan was introduced Mr Pearey explained that Members could lose the ability to obtain potential Awards if they left the firm, became insolvent or committed serious misconduct. He thought that also in the event of his death his estate would have forfeited the award or that if things had happened to the capital of the company, even if the company was solvent, some of that capital may have been required to fill the gap. Otherwise, he would hope to receive the award on the expected date if none of these things had happened. He said the monies were at risk because of these factors and also noted that "our business is inherently very risky" and it was quite conceivable that Odey could become insolvent: "Businesses like ours don't necessarily last forever. There are plenty that have shut down and plenty that have got into trouble".

Tax avoidance purpose

190. I fully accept the evidence set out above as regards the commercial reasons for the introduction and operation of the Plan (and there is nothing in the evidence set out below which affects my view on that). However, that should not be taken to mean that I accept that there was no tax motivation or objective involved in introducing and operating the Plan or that any such motivation or objective was incidental only to the other undoubted commercial objectives. I note that in the Spring of 2009, as HMRC pointed out, it was announced that a highest rate of income tax of 50% was to be introduced for high earners. The other evidence on this issue is set out here and there is commentary on it in Part D.

191. The bundles contained only one note from Ernst & Young in relation to the Plan. It is undated and headed "Retention and incentive scheme". The note set out brief details of the Plan and contained a list of "Pros" and "Cons". In the "Pros" section it was stated that (a) "Effective rate of 28% ie Corporation tax (reducing to 24% over the next 4 years) versus 51%", (b) "Greater focus on remuneration and deferral policies give the scheme greater commercial credence", and (c) "Tax efficient way of reinvesting in Funds". In the "Cons" section it was stated that (a) "Scheme open to challenge anytime by HMRC", (b) "Transfer of capital from NewCo to individual member at a no gain/no loss is based on HMRC statement of practice rather than unequivocal tax legislation", and (c) "Deferral should be for at least 1 year".

192. In his witness statement Mr Pearey said that:

> "To the extent that tax was a factor at all, it had more to do with the unfairness of Odey being pressured to put in place deferral arrangements that complied with the regulatory framework and that, as a result, would leave members facing an upfront tax charge on amounts that they might never receive".

193. In his witness statement, Mr Stewart agreed with Mr Pearey's description of the wider commercial benefits of the proposed plan. He said that it was obviously a bonus to have a tax benefit but it was no more than an incidental benefit. He was aware that the arrangements had a potential tax benefit and it was a positive aspect of the Plan, but:

> "when we were discussing why we needed such arrangements and what they needed to achieve, tax was not the reason. I did, however, understand that this structure would ensure that no unfair tax charge would arise to individual members on the initial allocation, even though they might not be reallocated

any amounts in the future. We were aware that such a tax could arise because that had been the case with respect to Alex Griffiths."

194. In his witness statement, Mr Odey said that he was aware that the Plan avoided an unfair tax charge such as the one that arose in relation to Mr Griffiths and that there were also tax savings as a consequence of the Plan being implemented. He said that:

> "Although the Plan was necessary, it was clear that many of the members were reluctant to accept a mechanism which put amounts they might otherwise receive at risk. They were clearly getting a worse deal under the Plan and I am sure that the tax benefit helped to "sweeten" the position. The tax benefit was, however, incidental to creating a remuneration structure and policy that was consistent with the regulatory environment and the Remuneration Code, enabled deferral in a way that met Odey's commercial requirements, and avoided an unfair tax charge."

195. Mr Pearey was taken to Ernst &Young's note. He thought it dated from around 2010 to 2011 and was an amalgam of a diagram produced by Ernst & Young and wording produced by Odey. It was put to him that one of the selling points of the proposal is that there is no upfront tax charge on the deferred share. He agreed that was one aspect of it and that there would be no charge on sums when paid in later years. It was put to him that none of the commercial objectives he set out as reasons for adopting the Plan are listed in the "Pros" in the note and in fact the deferral is listed as one of the "Cons". He said:

> "I think at the time there was great reluctance, really, across the board by many members as to any form of deferral. And this was also, really, at a time with the regulatory climate changing dramatically post the financial crisis……And so there was certainly resistance within the partnership amongst members against any form of deferral. So, I think in some ways the presentation of this to Members was in a sort of a warts-and-all format. One was just wanting to be very clear with them, so perhaps the - so for some to say the pro is "You are deferred for two years or one year or more", would be rather disingenuous, perhaps, to a member who was opposed to any form of deferral mechanism.
>
> This is laying it out, as it were, in a way to a pretty reluctant audience, but just to make sure that they were aware of the structure and how it may work in practice."

196. It was put to him that the other two cons are both about whether HMRC would challenge the arrangement and that it was stated in the note that greater focus on remuneration and deferral policies give the scheme greater commercial credence. He said:

> "I think…. a "con" is a tough word, but I think we wanted to make sure that Members were aware that any mechanism which one puts in place will be, ultimately, one presumes, investigated by HMRC…..
>
> Well, the commercial credence and credibility also ties to the wider aspects of the firm wanting to act in accordance with the regulatory and the political zeitgeist at the time; the commercial nature of having flexible capital within the business, which PSCL afforded us; but also for our investors, who were demanding to see - within this regulatory environment demanding to see a greater alignment of interest between the risk takers and…... So, that all, to my mind, ties into this commercial credibility of what we were trying to achieve……I think one could say that the commercial nature of it, ie the fact that the deferral was over a meaningful period of time; that there was genuine risk involved in it; that the founder, Crispin Odey, who would be very hard to incentivise and retain, did not partake in this, all of that gives this mechanism

> greater commercial credibility in terms of being a genuine mechanism for incentive and retention."

197. Mr Pearey agreed that the note "has more of a tax angle to it". It was put to him that Odey had not put forward any other documents that were given to explain the scheme to the Members. He said that "the Remuneration Policy itself is the key document in terms of giving the wider context to them of the need for the remuneration policy" and this note:

> "is more the practical aspects of what happens in this sort of mechanism….because clearly a lot of people would have asked….in terms of the mechanics of how this works, what are some of the pros and cons to it all? So, one would have presented it to the members as we saw it. I mean, there is no denying, potentially, the consequence of this, but it was not the objective."

198. It was put to Mr Pearey that given the pro is the effective tax rate of 28% listed as the first advantage, saving tax is at least an objective. He said: "It is not an objective; it is a consequence". It was put to him that when the note refers to "commercial credence", this is about the scheme's credibility when looked at by HMRC; the suggestion was that it would look a bit less like a tax scheme because it was tied into remuneration and incentive arrangements. He said that he did not necessarily agree with that:

> "I think any mechanism you put in, the objectives of it, I think, should be in and around a commercial environment in which you are operating. By that, I include the regulator and, most critically, our investor base, who - and still to this day and hence why the remuneration policy has remained completely unchanged albeit the mechanism has changed in the advent of the mixed partnership rules, but the remuneration policy and the tiering effect of how we incentivise and retain people has remained entirely unchanged."

199. It was put to Mr Pearey that a major reason for adopting the Remuneration Policy was to reduce the risk of the 50% tax rate. He disagreed:

> "when one looks back, a lot of the directive was coming out from Europe, who were looking to apply the same terms as has been applied to the investment banking industry, so a cap on salaries and then a cap, subsequently, on any bonus, which would have been a percentage of salary, and over a defined period of time.
>
> This was very much heading into the investment management sector, and there were numerous consultation papers, principally being driven by Brussels, which at one stage looked very much like this was indeed going to be the case, but a last-minute vote in Parliament deflected the more prescriptive nature of it.
>
> However, the FCA still expected, and indeed by now our investors expected us, to have some form of remuneration policy, some form of remuneration plan in place for what they would call the "code staff" or the "key risk-takers". So, whilst some technical aspects of whether a partnership drawing is in fact a remuneration may have not fitted into the very prescriptive nature, it was clear this is what the regulator expected. Indeed, subsequent to that, almost in every year since there has been various iterations of European directives continually pushing for very prescriptive remuneration policies and deferrals. So, either way, I felt we had no choice but to implement some form of remuneration policy."

200. Mr Odey said that the tax saving was "incidental to the whole thing…The importance was fulfilling the FSA changes and what was going on. It didn't save a lot of tax in the scheme of things". He added:

> "basically the original thinking was we asked EY and everybody else, you know, what is the best structure, we're thinking of a remuneration and incentive scheme, and they came back with one which was very tax driven, et cetera. And we said, actually, that's not what we are looking for. We are looking for something which basically does what we want, which is to -- I'm very happy to pay the tax but let's have a retention scheme that really does work…..
>
> …..you know, it was a big sum of money in absolute terms, but it was in relative terms quite a small sum of money
>
> ….. The problem was that we were going from a place where basically we paid out their bonuses to deferring their bonuses.
>
> As soon as I saw something like this I thought this is not what we are looking for. I mean, what we came up with in the end, EY would not be proud of it as a tax-saving device, I have to tell you. When you say, when you looked at this, this document is about the actual scheme? It is thinking about how we retain and incentivise people, yes."

201. Mr Odey could not point to any document setting out what he referred to above as Ernst & Young's first "very tax driven" proposal. He said, in effect that the scale of the tax saving had to be viewed in context given that he did not participate in the Plan and there was a whole lot of non-partner employees. He accepted that in the context of the unpopular new highest rate of income tax of 50%, some individuals were at the time leaving the UK and that reducing tax was an attractive feature of the Plan for those who Odey did not want to leave.

202. Mr Stewart could not remember the particular Ernst & Young document in the bundles but he recalled seeing a presentation from them showing how the Plan worked. He said that the tax saving certainly made the conversation with Members easier because "most people prefer cash in the hand now rather than waiting". When it was put to him that the tax saving was more than an incidental benefit, he said: "I don't agree with the implication that that's why the Plan was embarked upon". When it was put to him that it was, at least in part, one of the advantages sought using the Plan, he said: "No, I don't think - I think it was a by-product of it. I come back to me, as CEO, wanting an incentivisation and remuneration plan in place".

203. When Lord Roborough was asked if the tax advantage was explained to him at the time, he said: "We understood that this turned - that the allocation to PSCL and the re-allocation out would mean that there was corporation tax within the initial transfer". He thought this benefit helped to sell the plan to the Members. He did not agree that paying a reduced amount of tax make taking the risk of receiving the sums worth taking. He said: "it was discussed as a way of trying to persuade us not to protest against the scheme too much". He thought the Members had no choice but to accept the scheme but the fact that there was some tax benefit softened the blow.

Part B – Year of allocation issue

Legal framework

204. All references in this Part B of this decision to sections, parts and chapters of legislation are to sections, parts and chapters of ITTOIA unless there is an express statement to the contrary. An LLP is a body corporate under the Limited Liability Partnerships Act 2000 (see s 1(2)). However, an LLP which carries on a trade or business with a view to profit is, for tax purposes, treated as though it were an ordinary partnership under s 863 and s 1273 CTA 2009. Section 863 provides as follows:

"For income tax purposes, if a limited liability partnership carries on a trade, profession or business with a view to profit –

(a) all the activities of the limited liability partnership are treated as carried on in partnership by its members (and not by the limited liability partnership as such),

(b) anything done by, to or in relation to the limited liability partnership for the purposes of, or in connection with, any of its activities is treated as done by, to or in relation to the members as partners, and

(c) the property of the limited liability partnership is treated as held by the members as partnership property.

References in this subsection to the activities of the limited liability partnership are to anything that it does, whether or not in the course of carrying on a trade, profession or business with a view to profit.

(2) For all purposes, except as otherwise provided, in the Income Tax Acts –

(a) references to a firm or partnership include a limited liability partnership in relation to which subsection (1) applies,

(b) references to members or partners of a firm or partnership include members of such a limited liability partnership,

(c) references to a company do not include such a limited liability partnership, and

(d) references to members of a company do not include members of such a limited liability partnership."

205. It was common ground that Odey carries on business or trade as a Fund manager with a view to profit so that its Members are subject to tax on its profits under the rules relating to partnerships. It was also common ground that under those rules, for each tax year, each member of such an LLP is subject to tax on a proportion of the profits of the LLP attributable to that tax year on the basis that (a) the overall profits or losses of each period of account are first calculated as though the LLP were a single person (as regards the tax liability of a UK resident individual member) or single entity (as regards the tax liability of a UK resident corporate member) (under s 849 and s 1259 CTA 2009), and (b) the member's share of those profits is determined under s 850 and s 1262 CTA 2009.

206. The relevant rules applicable to individual members of an LLP such as Odey are set out in ITTOIA as follows (and, as noted equivalent rules apply to corporate members):

"847 **General provisions**

(1) In this Act persons carrying on a trade in partnership are referred to collectively as a "firm".

(2) The provisions of this Part which are expressed to apply to trades also apply, unless otherwise indicated (whether expressly or by implication)-

(a) to professions, …

…

848 **Assessment of partnerships**

Unless otherwise indicated (whether expressly or by implication), a firm is not to be regarded for income tax purposes as an entity separate and distinct from the partners.

849 **Calculation of firm's profits or losses**

(1) If –

(a) a firm carries on a trade, and

> (b) any partner in the firm is chargeable to income tax,
>
> the profits or losses of the trade are calculated on the basis set out in subsection (2) or (3), as the case may require.
>
> (2) For any period of account in which the partner is a UK resident individual, the profits or losses of the trade are calculated as if the firm were a UK resident individual.
>
> (3) For any period of account in which the partner is non-UK resident, the profits or losses of the trade are calculated as if the firm were a non-UK resident individual.
>
> …
>
> 850 **Allocation of firm's profits or losses between partners**
>
> (1) For any period of account a partner's share of a profit or loss of a trade carried on by a firm is determined for income tax purposes in accordance with the firm's profit-sharing arrangements during that period.
>
> (2) In this section…"profit sharing arrangements" means the rights of the partners to share in the profits of the trade…"

207. Usually, for each tax year, the representative member of an LLP such as Odey is required to submit a partnership tax return to HMRC which has to include a statement of the amount of each member's share of the LLP's income for the relevant period (under s 12AB(1)(b) TMA). Each individual member must include that share in his personal self-assessment tax return for the relevant tax year (under s 8(1B) TMA).

208. HMRC referred to *MacKinlay v Arthur Young McClelland Moores & Co* [1986] 1 WLR 1468 at 1474 ("*MacKinlay*") where the court described the process under the rules then in place for computing and dividing the profits of a business taxed as a partnership among the partners as involving the following three stages:

> "There are, in effect, three stages. *First, the profits of the firm for an appropriate basis period must be ascertained. What has to be ascertained is the profits of the firm and not of the individual partners.* That is not, I think, stated anywhere in the Income Tax Acts, but it follows necessarily from the fact that there is only one business and not a number of different businesses carried on by each of the partners. *The income of the firm for the year is then treated as divided between the partners who were partners during the year to which the claim relates – the year of assessment – in one of the many senses of that word*: see the proviso to s 26 of the Taxes Act 1970. That is the second stage. The tax payable is then calculated according to the circumstances of each partner – that is, after taking into account on the one hand any personal allowances, reliefs or deductions to which he is entitled and any higher rate of tax for which he is liable. The Acts do not provide for the way in which personal allowances, reliefs and deductions are to be apportioned between the partnership income and other income. I understand that in practice they are deducted from the share of the partnership income if that was the partner's main source of income. When the tax exigible in respect of each share of the partnership income has been ascertained the total tax payable is calculated. Section 152 (formerly Rule 10 of the Rules applicable to Cases I and II of Schedule D) provides that the total sum so calculated is to be treated as "one sum … separate and distinct from any other tax chargeable on those persons … and a joint assessment shall be made in the partnership name." That is the third stage." (Emphasis added.)

209. In *Vaines v HMRC* [2018] EWCA Civ 45 ("*Vaines*") the Court of Appeal explained, in effect, that current rules operate according to the first two stages identified in *MacKinlay* but that, following the introduction of the self-assessment system, the third stage set out in that case is no longer applicable. Lord Justice

Henderson explained the operation of the current statutory regime in the context of the taxation of Mr Vaines as a partner in a partnership as follows:

(1) He said, at [17], that it follows from ss 849 (1) and (2) ITTOIA that "the profits of the (deemed) partnership trade are to be calculated as if the firm were a UK resident individual", the "firm" for this purpose being "a collective description of Mr Vaines and his fellow partners in the (deemed) partnership" in question and that the trade in question is "the actual trade of the partnership, which section 863 (1) treats as carried on in partnership by its members" and "not a separate trade carried on by Mr Vaines alone, but the trade of [the partnership] carried on collectively by himself and his fellow partners".

(2) He continued, at [18], that once the profits of that collective trade have been ascertained, s 850 ITTOIA then provides that Mr Vaines' share of the profit for the relevant period of account is to be determined "in accordance with the firm's profit-sharing arrangements during that period". He noted that under s 5 ITTOIA, Mr Vaines is charged to income tax on his share of the profits and under s 7, the tax is charged on the full amount of the profits of the tax year, which means the profits of the "basis" period for the tax year as that period is determined under chapter 15 of part 2 ITTOIA. As he set out, the normal rules operate by reference to the date in the tax year by reference to which 12 month accounts are drawn up, with specific rules to cover the situation in which a person has started or ceased (or is treated as starting or ceasing) to carry on a trade.

(3) At [19], he explained that there is a further complication but that it only relates to the basis period rules in chapter 15 of part 2 ITTOIA. The complication is that s 852 (1) states that: "For each tax year in which a firm carries on a trade (the "actual trade"), each partner's share of the firm's trading profits or losses is treated, for the purposes of Chapter 15 of Part 2 (basis periods), as profits or losses of a trade carried on by the partner alone (the "notional trade")."

(4) He said, at [20], that the important point as regards this provision (and related detailed provisions on basis periods) is that:

> "it is only for these limited purposes that a partner is deemed to carry on a notional trade of his own, separate from the actual trade of the partnership which he carries on together with his fellow partners. Furthermore, these provisions only come into play at the final stage of assessing partnership profits to tax on the individual partners, after the profits of the trade have been ascertained and after each partner's share of those profits has been allocated to him."

(5) He set out, at [21], the passage from *MacKinlay* set out above. As regards the third stage set out in *MacKinlay*, he said, at [22], that after the introduction of self-assessment it was no longer possible to require a joint assessment to be made in the partnership name after calculating the amounts of tax payable by each of the individual partners separately. Further, as the UT correctly observed at [25] of their decision:

> "….. Following the introduction of self-assessment, however, each partner is assessed to tax on their share of the profits by reference to the basis period determined according to their notional trade. It is, however, as the language of [*ITTOIA*] recognises, a notional trade only for the purposes of assessment. The actual trade remains that of the partners collectively and it is the profits of that collective trade that must be computed before being *allocated or shared among partners to*

provide each partner's share of the profit that is the profit of their notional trades for the purposes of their self-assessment." (Emphasis added.)

210. It was common ground, therefore, that, for each relevant tax year, the individual Members are subject to tax on their share of the profits of Odey attributable to that tax year on the basis that (a) Odey's overall profits or losses of Odey's trade for each period of account are calculated as though it were a single person, and (b) each individual Member's share of those profits is determined according to that Member's "rights to share" in the profits of the trade during that period.

211. HMRC noted that, as also did not appear to be disputed:

(1) Under the 2011 LLP Agreement, the Members had a *right* to share in the profits of Odey as allocated to them by Odey in exercise of its discretion.

(2) The Members are taxable on profits of a period of account which they had a right to share in the relevant period whether or not they are free to withdraw the monies from Odey. HMRC added that, similarly, if an LLP such as Odey or a partnership incurs non-deductible expenses, those sums are added back into the profits for tax purposes and allocated to the members, even though there is in fact no money to distribute (see *Reed v Young* [1986] STC 285 at 289 to 290).

212. The dispute was whether, on a purposive approach to the legislation, for each relevant tax year, each relevant Member is taxable not only on his share of the profits of Odey's trade for the relevant period which he actually received but also the individual share which was "awarded" to him in that period. Essentially, this turns on how s 850 is to be applied:

(1) HMRC's primary argument was that, on the correct purposive construction, viewing s 850 in the scheme of the overall rules on the taxation of LLPs and partnerships and taking a realistic view of the facts, the relevant Members had the "rights to" the individual shares as a share of the profits of Odey in the year of allocation on the basis that those shares were in fact allocated to or, are to be regarded as allocated to, the relevant Members in that period as a "deferred profit share":

(a) Mr Chacko emphasised that the charge to income tax under s 850 is not a receipts-based charge. The question is not what a member or partner has a right "to get out of" the partnership/LLP. The "rights" referred to under s 850 are not "rights" to be paid money, but "rights" to share in the profits. He said: "What this is getting at is: how are the profits divided? What is the allocation in the year?"

(b) He thought that the fact that s 850 is about "division" or "allocation" is apparent from *Vaines* where Henderson LJ, in effect, endorsed the passage from *MacKinlay* where the court referred to the "division" of profits (see [21]) and the comments of the UT in *Vaines* as regards the allocation or sharing of profits (see [22]).

(2) The appellants said that the purpose of s 850 is plainly to tax partners and members of LLPs only on profits to which they had *rights* in the relevant period, in the sense of an entitlement in a legal sense which, in principle, they could turn to account or obtain value from. The purpose is not, as the appellants consider is the effect of HMRC's approach, to impose tax on profits that a partner/member might have a right to in future periods or on his expectation of receiving profits (see *Franklin v IRC* [1930] 15 TC 464). In their view, on a realistic view of the facts, under the contractual arrangements between the Members, only PSCL had the "right" to the individual shares in the year of

allocation in the required sense. The Members had no such "right", during that period, either as regards the individual share or a reallocation of Special Capital in respect of that share.

213. As set out in further detail below, my view is that the appellants' view of the purpose of s 850 is correct. Before turning to the parties' more detailed submissions on this, I have set out the caselaw on how tax legislation is to be interpreted.

Law - Purposive approach to construction

214. Following the seminal decision in *WT Ramsay Ltd v Inland Revenue Commissioners* [1981] UKHL 1 ("*Ramsay*"), it is well established that, in line with how other legislation is interpreted, the courts and tribunals must apply a purposive approach in interpreting tax legislation. The essence of the modern approach to statutory construction in a tax context is encapsulated in the Hong Kong case of *Collector of Stamp Revenue v Arrowtown Assets Ltd* [2003] HKCFA 46 (2004) 6 ITLR 454 ("*Arrowtown*") where, at [35], Ribeiro PJ summarised the "driving principle" in the *Ramsay* line of cases as involving:

> "a general rule of statutory construction and an unblinkered approach to the analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically."

Ramsay

215. In *Ramsay*, as noted, the House of Lords was concerned with a tax avoidance scheme under which the taxpayer sought to offset a capital gain by creating an allowable loss for capital gains purposes without incurring an economic loss. As Lord Wilberforce explained, at page 179, under the scheme "two assets appear, like particles in a gas chamber with opposite charges, one of which is used to create the loss, the other of which gives rise to an equivalent gain which prevents the taxpayer from supporting any real loss, and which gain is intended not to be taxable". The relevant assets were loans which he said "like the particles" had a very short life:

> "Having served their purpose they cancel each other out and disappear. At the end of the series of operations, the taxpayer's financial position was precisely as it was at the beginning, except that he paid a fee, and certain expenses, to the promoter of the scheme."

216. He also noted that it was the clear and stated intention that once started the scheme would proceed through the various steps to the end and that "the taxpayer does not have to put his hands in his pocket" given the monies required were provided by a finance house and were automatically repaid at the end of the operation.

217. Lord Wilberforce continued that their Lordships were invited to treat the transactions as a fiscal nullity not producing either a gain or a loss and that counsel described that approach as "revolutionary". Lord Wilberforce concluded, however, that far from being revolutionary, this approach resulted from the application of ordinary principles of statutory construction.

218. At pages 179 and 180, Lord Wilberforce set out what he considered to be well established principles:

(1) The courts are not confined to literal interpretation of statutory provisions but should consider "the context and scheme of the relevant Act as a whole, and its purpose may, indeed should, be regarded…..".

(2) A person "is entitled to arrange his affairs so as to reduce his liability to tax. The fact that the motive for a transaction may be to avoid tax does

not invalidate it unless a particular enactment so provides. It must be considered according to its legal effect".

(3) It is for the fact-finding commissioners to find whether a document, or a transaction, is genuine or a sham in the sense that "while professing to be one thing, it is in fact something different. To say that a document or transaction is genuine, means that, in law, it is what it professes to be, and it does not mean anything more than that."

(4) "Given that a document or transaction is genuine, the court cannot go behind it to some supposed underlying substance. This is the well-known principle of *Inland Revenue Commissioners v Duke of Westminster* [1936] AC 1, 19."

219. He continued, at page 180, that whilst the principle set out in the *Duke of Westminster* is "a cardinal principle" it "must not be overstated or overextended" to require a blinkered approach:

> "While obliging the court to accept documents or transactions, found to be genuine, as such, it does not compel the court to look at a document or a transaction in blinkers, isolated from any context to which it properly belongs."

220. In the same passage, he continued to set out what I term "the composite approach":

> "If it can be seen that a document or transaction was intended to have effect as part of a nexus or series of transactions, or as an ingredient of a wider transaction intended as a whole, there is nothing in the doctrine to prevent it being so regarded: to do so is not to prefer form to substance, or substance to form. It is the task of the court to ascertain the legal nature of any transaction to which it is sought to attach a tax or a tax consequence and if that emerges from a series or combination of transactions, intended to operate as such, it is that series or combination which may be regarded…."

(I note that I use the term "composite approach" by way of shorthand. I do not suggest that Lord Wilberforce was laying down a composite approach as some sort of free-standing principle; he was clear that was not the case.)

221. He concluded that whether under the principle set out in *Westminster* or under any other authority:

> "the courts are not bound to consider individually each separate step in a composite transaction intended to be carried through as a whole".

222. Lord Wilberforce went on to state that the composite approach is particularly in point where "it is proved that there was an accepted obligation once a scheme is set in motion, to carry it through its successive steps" and where (as in *Ramsay* itself) "there is an expectation that it will be so carried through, and no likelihood in practice that it will not". In such cases "(which may vary in emphasis) the commissioners should find the facts and then decide as a matter (reviewable) of law whether what is in issue is a composite transaction, or a number of independent transactions".

223. He went on to state explicitly, at page 181, that the approach he set out did not introduce a new principle. Rather it involved applying to "new and sophisticated legal devices the undoubted power and duty of the courts to determine their nature in law and to relate them to existing legislation" in recognition that while "the techniques of tax avoidance progress and are technically improved, the courts are not obliged to stand still". He said, at page 182, that:

> "To force the courts to adopt, in relation to closely integrated situations, a step by step, dissecting, approach which the parties themselves may have

> negated, would be a denial rather than an affirmation of the true judicial process. In each case the facts must be established, and a legal analysis made: legislation cannot be required or even be desirable to enable the courts to arrive at a conclusion which corresponds with the parties' own intentions."

224. As Lord Reed later put it in *UBS v HMRC* [2016] STC 934 ("*UBS*"), it is plain that Lord Wilberforce was saying not only that the purposive approach to statutory construction, which was orthodox in other areas, extended to tax law but also "equally significantly….that the analysis of the facts depended on that purposive construction of the statute".

225. Having noted, at page 182, that capital gains tax was "created to operate in the real world, not that of make-belief" Lord Wilberforce referred to his own comments in *Aberdeen Construction Group Ltd.* v. *I.R.C.* [1978] AC 885 that:

> "it is a tax on gains (or I might have added gains less losses), it is not a tax on arithmetical differences. To say that a loss (or gain) which appears to arise at one stage in an indivisible process, and which is intended to be and is cancelled out by a later stage, so that at the end of what was bought as, and planned as, a single continuous operation, is not such a loss (or gain) as the legislation is dealing with, is in my opinion well and indeed essentially within the judicial function."

226. He summarised the relevant facts, at page 183: (a) the scheme had no commercial justification as the taxpayer was bound to make a loss, (b) "every transaction would be genuinely carried through and in fact be exactly what it purported to be", (c) it was "reasonable to assume that all steps would, in practice, be carried out, but there was no binding arrangement that they should. The nature of the scheme was such that once set in motion it would proceed through all its stages to completion", (d) the transactions "regarded together, and as intended, were from the outset designed to produce neither gain nor loss…they were self cancelling", (e) the scheme "was not designed as a whole to produce any result for Ramsay or anyone else, except the payment of certain fees for the scheme,…" and (f) the monies were advanced by a financier "on terms which ensured that it was used for the purposes of the scheme and would be returned on completion, having moved in a circle".

227. He concluded, at page 383, that:

> "it would be quite wrong, and a faulty analysis, to pick out, and stop at, the one step in the combination which produced the loss, that being entirely dependent upon, and merely a reflection of the gain. The true view, regarding the scheme as a whole, is to find that there was neither gain nor *loss*, and I so conclude."

Furniss

228. Notwithstanding the plain meaning of Lord Wilberforce's judgment, as Lord Nicholls recognised in *Barclays Mercantile Business Finance Ltd v HM Inspector of Taxes* [2004] UKHL 51 ("*BMBF*"), for some time there was a tendency for taxpayers and HMRC to view *Ramsay* as establishing "a new jurisprudence governed by special rules of its own". That view was based, in particular, on comments made in the cases which followed in the wake of *Ramsay*, such as *Inland Revenue* v *Burmah Oil Co Ltd* 1982 SC (HL) 114 ("*Burmah Oil*"), *Furniss* v *Dawson* [1984] AC 474 ("*Furniss*") and *Carreras Group Ltd* v *Stamp Commissioner* [2004] STC 1377 ("*Carreras*"). Parties interpreted the decisions in these cases as meaning that, on a composite approach, *whatever the taxing statute*, elements inserted into a pre-ordained composite scheme without any commercial or business purpose should be treated as having no significance to the tax analysis. In particular, the well-known comments of

Lord Brightman in *Furniss* at page 527 (as based on the earlier formulation by Lord Diplock in *Burmah Oil*) suffered from this view.

229. In *Furniss* the taxpayers transferred shares which they wished to sell to a third party to a newly formed offshore company, IoM, in exchange for shares and that company then immediately sold the shares on to the third party for cash. The taxpayers' purpose in inserting this step prior to the sale was to avoid any immediate charge to tax on capital gains on the sale on the basis that IoM was outside the UK tax net. It was critical to the success of the scheme, therefore, that the initial transfer of the shares to IoM took place as a tax neutral reorganisation for capital gains tax purposes. The House of Lords took a composite approach in deciding that the taxpayers were to be treated as though they had disposed of the shares direct to the third party on the basis that, with their concurrence, the sale price was paid to IoM.

230. In the relevant passage Lord Brightman said that the correct expression of the limitations of the *Ramsay* principle is as follows, at page 527:

> "First, there must be a pre-ordained series of transactions; or, if one likes, one single composite transaction. This composite transaction may or may not include the achievement of a legitimate commercial (ie business) end. The composite transaction does, in the instant case….It did not in *Ramsay*. Secondly, there must be steps inserted which have no commercial (business) *purpose* apart from the avoidance of a liability to tax - not 'no business *effect*'. If those two ingredients exist, the inserted steps are to be disregarded for fiscal purposes. The court must then look at the end result. Precisely how the end result will be taxed will depend on the terms of the taxing statute sought to be applied.
>
> In the instant case the inserted step was the introduction of [IoM] as a buyer from the [taxpayers] and as a seller to [the third party]. That inserted step had no business purpose apart from the deferment of tax, although it had a business effect…."

231. However, as set out in detail below, the House of Lords and the Supreme Court have been at pains to clarify that the view that the composite approach embodies a new jurisprudence governed by special rules of its own is a misconception. They have set out clearly that (a) *Ramsay* itself does not set out any such special principle, and (b) in *Furniss* and the other relevant cases, the courts were not laying down any such special principle or interpreting *Ramsay* as doing so.

MacNiven and BMBF

232. In *MacNiven* v *Westmoreland Investments Ltd* [2003] 1 AC 311 ("*MacNiven*"), the House of Lords held that a debtor made a payment of interest within the meaning of the relevant statute which entitled him to a deduction or repayment of tax notwithstanding that it was funded by monies borrowed for that purpose from the creditor himself and was made solely to reduce the debtor's liability to tax. The House of Lords said that the purpose of requiring interest to be "paid" is to produce symmetry; it gives a right to a deduction in respect of any payment which gives rise to a corresponding tax liability for the recipient (or which would do so if the recipient is a taxable entity.) As the payment was accepted to have had this effect, it answered the statutory description.

233. In reviewing the *Ramsay* line of cases, Lord Nicholls emphasised that in *Ramsay* "the House did not enunciate any new legal principle" but rather highlighted that, "confronted with new and sophisticated tax avoidance devices, the courts' duty is to determine the legal nature of the transactions in question and then relate them to the fiscal legislation…." (at [1]). He noted, at [2] to [5] that *Ramsay* brought out the following three points, in particular:

(1) When seeking to attach a tax consequence to a transaction, the court may have regard to the overall effect of a series or combination of transactions intended to operate as such and:

> "..Courts are entitled to look at a pre-arranged tax avoidance scheme as a whole. It matters not whether the parties' intention to proceed with a scheme through all its stages takes the form of a contractual obligation or is expressed only as an expectation without contractual force".

(2) That does not mean that transactions or relevant steps are to be treated as "shams" nor does it require going "behind a transaction for some supposed underlying substance". Rather it enables the court "to look at a document or transaction in the context to which it properly belongs".

(3) Having identified the legal nature of the transaction, the courts must then relate this to the language of the statute:

> "For instance, if the scheme has the apparently magical result of creating a loss without the taxpayer suffering any financial detriment, is this artificial loss a loss *within the meaning of the relevant statutory provision*?"

234. Lord Nicholls, therefore, specifically endorsed the composite approach. He then referred with approval, at [6], to the comments of Lord Steyn and Lord Cooke of Thorndon in *Inland Revenue Commissioners v McGuckian* [1997] 1 WLR 991 ("*McGuckian*") at 1000 and 1005 respectively. He noted that they said that this approach (as Lord Nicholls had described it, including the composite approach) "is an exemplification of the established purposive approach to the interpretation of statutes" and "an application to taxing Acts of the general approach to statutory interpretation whereby, in determining the natural meaning of particular expressions in their context, weight is given to the purpose and spirit of the legislation".

235. At [7], he cautioned that the observations on the *Ramsay* approach in some later decisions should be read in the context of the particular statutory provisions and sets of facts under consideration and that they:

> "cannot be understood as laying down factual pre-requisites which must exist before the court may apply the purposive, *Ramsay* approach to the interpretation of a taxing statute. That would be to misunderstand the nature of the decision in *Ramsay*."

236. Whilst he "readily accepted", at [8], that the factual situation described by Lord Brightman in *Furniss* is one where, typically, the *Ramsay* approach will be "a valuable aid" which may well often have the effect he set out, it really is just an aid and:

> "This is not an area for absolutes. The paramount question always is one of interpretation of the particular statutory provision and its application to the facts of the case. Further, as I have sought to explain, *Ramsay* did not introduce a new legal principle. It would be wrong, therefore, to set bounds to the circumstances in which the *Ramsay* approach may be appropriate and helpful. *The need to consider a document or transaction in its proper context, and the need to adopt a purposive approach when construing taxation legislation, are principles of general application. Where this leads depends upon the particular set of facts and the particular statute…..*" (Emphasis added.)

237. It is clear, therefore, that Lord Nicholls did not consider that *Furniss* was wrongly decided or that the description Lord Brightman gave of how the composite approach may apply was wrong, as applied in the context of the particular provision in issue in Furniss and the facts of that case. He considered that those comments

provide useful guidance but are not to be viewed as providing a set of universally applicable conditions which must be satisfied for a *Ramsay* composite approach to apply; it is always a question of interpretation of the relevant provision and its application to the specific facts.

238. Lord Hoffmann was also clear that, on a *Ramsay* approach, the ultimate question is one of statutory interpretation. However, he sought to provide guidance on precisely when a composite approach is appropriate. In summary, he drew a distinction between cases where a statutory concept is intended to be given (a) a commercial meaning, in which case steps with no commercial purpose artificially inserted into a composite transaction for tax purposes will not affect the answer to the statutory question, and (b) a legal meaning, in which case the juristic interpretation of the provision is to be respected.

239. At [28], Lord Hoffmann said that "everyone agreed that *Ramsay* is a principle of statutory construction". However, in his view it involved an "innovation" in that its effect "was to give the statutory concepts of "disposal" and "loss" a commercial meaning" in recognition that "the statutory language was intended to refer to commercial concepts", so that "the court was required to take a view of the facts which transcended the juristic individuality of the various parts of a pre-planned series of transactions".

240. At [40], he considered what the court meant in *Ramsay* in referring to the "real" nature of the transaction and to what happens in "the real world". He said that: "The point to hold onto is that something may be real for one purpose but not for another". He said that accordingly:

> (1) The acceptance that the transactions in *Ramsay* were not shams was an acceptance of "the juristic categorisation of the transactions as individual and discrete" and that "each of them involved no pretence. They were intended to do precisely what they purported to do. They had a legal reality".
>
> (2) On the other hand, the view that the transactions did not give rise to a "real" disposal giving rise to a "real" loss was a rejection of "the juristic categorisation as not being necessarily determinative" for the purposes of those statutory concepts as properly interpreted. He thought that the "contrast here is with a commercial meaning of these concepts" and that reference to the income tax legislation as operating "in the real world", is a reference to "the commercial context which should influence the construction of the concepts used by Parliament".

241. He said, at [48], that in the famous passage in *Furniss* Lord Brightman provided "a careful and accurate summary of the effect which the *Ramsay* construction of a statutory concept has upon the way the courts will decide whether a transaction falls within that concept". He expanded on this as follows:

> "If the statutory language is construed as referring to a commercial concept, then it follows that steps which have no commercial purpose but which have been artificially inserted for tax purposes into a composite transaction will not affect the answer to the statutory question. When Lord Brightman said that the inserted steps are to be "disregarded for fiscal purposes", I think that he meant that they should be disregarded for the purpose of applying the relevant fiscal concept."

242. He emphasised at [49] that this formulation "is not a principle of construction" but is "rather a "statement of the consequences of giving a *commercial construction* to a fiscal concept" (emphasis added). He advised that before applying Lord Brightman's words:

> "it is first necessary to construe the statutory language and decide that it refers to a concept which Parliament intended to be given a commercial meaning capable of transcending the juristic individuality of its component parts. But there are many terms in tax legislation which cannot be construed in this way. They refer to purely legal concepts which have no broader commercial meaning. In such cases, the *Ramsay* principle can have no application. It is necessary to make this point because, in the first flush of victory after the *Ramsay*, *Burmah* and *Furniss* cases, there was a tendency on the part of the Inland Revenue to treat Lord Brightman's words as if they were a broad spectrum antibiotic which killed off all tax avoidance schemes, whatever the tax and whatever the relevant statutory provisions."

243. He noted, at [50], that the distinction between commercial and legal concepts has also been drawn in other areas of legislation and noted "by way of caution that although a word may have a "recognised legal meaning", the legislative context may show that it is in fact being used to refer to a broader commercial concept".

244. He also approved the comments in the *McGuckian* case which Lord Nicholls referred to and suggested, at [56], that particular attention should be paid to the way Lord Cooke of Thorndon dealt with the criteria stated by Lord Brightman in *Furniss.* He said that:

> "if the ultimate question is always the true bearing of a particular taxing provision on a particular set of facts, the limitations [in *Furniss*] cannot be universals. *Always one must go back to the discernible intent of the taxing Act*" and that he suspected that "the advisers of those bent on tax avoidance...do not always pay sufficient heed to the theme in the speeches in the *Furniss* case...to the effect that the journey's end may not yet have been found". (Emphasis added.)

245. Lord Hoffmann concluded, at [58] and [59], by again referring to the distinction between legal and commercial concepts:

> "The limitations of the *Ramsay* principle therefore arise out of the paramount necessity of giving effect to the statutory language. One cannot elide the first and fundamental step in the process of construction, namely to identify the concept to which the statute refers. I readily accept that many expressions used in tax legislation (and not only in tax legislation) can be construed as referring to commercial concepts and that the courts are today readier to give them such a construction than they were before the *Ramsay* case. But that is not always the case. Taxing statutes often refer to purely legal concepts…If a transaction falls within the legal description, it makes no difference that it has no business purpose. Having a business purpose is not part of the relevant concept…
>
> Even if a statutory expression refers to a business or economic concept, one cannot disregard a transaction which comes within the statutory language, construed in the correct commercial sense, simply on the ground that it was entered into solely for tax reasons. Business concepts have their boundaries on this topic."

246. In the later cases, such as *BMBF*, the House of Lords clarified that Lord Hoffmann's words are not to be interpreted as meaning that there is an a priori assumption that statutory concepts should be classified into legal or commercial ones before a *Ramsay* approach can be applied. As set out below, in *BMBF* Lord Nicholls referred to Ribeiro PJ's comments in *Arrowtown*, at [37] and [39]. Ribeiro PJ said that he did not think that Lord Hoffmann "actually intended to lay down a mechanistic test based on a "commercial"/"legal" dichotomy for pre-determining whether a particular provision is or is not susceptible to a *Ramsay* approach" and that:

> "the "valuable insights" that Lord Hoffmann was acknowledging [as regards Lord Brightman's comment in *Furniss*] were all centred on the proposition that the *Ramsay* doctrine has at its core the purposive interpretation of statutes applied to facts viewed realistically and untrammelled by "limitations" which might be thought to arise out of Lord Brightman's formulation. Such an approach strikes me as the antithesis of a mechanistic use of the "commercial"/"legal" dichotomy as a straitjacket limiting construction of the relevant statute…" [as Ribeiro PJ thought was reinforced by Lord Hoffmann's comments at [50]].

BMBF

247. If any further clarification were needed on the effect of the decision in *Ramsay* Lord Nicholls provided this in giving the unanimous judgment of the House of Lords *BMBF* in what is now widely regarded as the definitive word on this topic.

248. *BMBF* concerned whether a Barclays group company, BF, could claim capital allowances under the Capital Allowances Act 1990 ("**CAA**") which it asserted it was entitled to under a finance leasing transaction. In summary, as set out in detail at [3] to [17] of the decision in *BMBF*:

(1) BF was a UK market leader in providing asset-based finance whereby typically it provided capital for the purchase of an asset for use by its customer in return for a series of periodic payments secured upon the assets:

(a) BF purchased a gas pipeline from an Irish entity, BGE, for £91 million and leased it back to BGE. BF borrowed the funds for the purchase price from Barclays Bank at a fixed commercial rate.

(b) BGE had constructed the pipeline largely with finance provided by a consortium of banks. The price of £91 million corresponded to that borrowing.

(c) BGE sub-leased the pipeline to, and made arrangements with, a newly formed UK subsidiary, BGE UK, for its operation.

(d) The lease to BGE was for a period of over 30 years for rents with an escalating profile and on terms typical of a finance lease, including that the rents were subject to adjustment if certain assumptions were to prove incorrect. The assumptions were based around the premise that BF would obtain allowances on the expected basis on £91 million and thereby achieve a particular level of tax saving. The sublease was on similar terms to the lease but the rents were not subject to this adjustment mechanism. BGE UK assumed direct liability to pay the rent to BF but with adjustments to the payment arrangements where the rental adjustment mechanism was triggered.

(2) There was no dispute that BF would ordinarily be entitled to allowances on the basis it incurred the purchase price on acquiring the asset for the purposes of its finance leasing trade. Nor was it disputed or perceived to be unacceptable tax avoidance that the basic premise of a finance leasing transaction, as it was put by one of BF's witnesses is that "lessors pass on the value of the capital allowances available to them in respect of the asset being financed to the customer. The customer gets the use of the asset concerned and pays rent at a rate which reflects the margin required by the Bank and the reduced funding cost to the Bank of providing lease finance as a result of the tax deferral benefit available." The House of Lords stated that if the above steps were the only ones involved in the transaction, HMRC would accept that BF was entitled to the allowances (see [13]).

(3) The unusual feature, which caused both the Special Commissioners and the High Court (Park J) concern was that BGE did not have immediate access to the funds raised of £91 million. This was because:

(a) BF required BGE UK to procure a guarantee in respect of the rental obligations.

(b) This guarantee was provided by Barclays Bank itself, which required BGE UK to provide a charge over the £91 million as counter security for its potential liability under the guarantee.

(c) For this purpose, BGE provided the sales proceeds to Barclays Bank via a complicated set of arrangements whereby it deposited them with a Jersey company and they reached the bank via an Isle of Man Barclays company.

(d) The Jersey company undertook complicated obligations to make a range of periodical payments to BGE and BGE UK over the duration of the lease which totalled much more than £91 million. One set of payments was used to funds the rents and the rest, of some £8.1 million in net terms, were retained by BGE. The House of Lords noted (at [17]) that the benefit obtained by BGE was entirely attributable to BF being able to pass on the benefit of its capital allowances.

249. Lord Nicholls first re-capped on the applicable principles of statutory construction. At [28], he noted that, as Lord Steyn explained in *McGuckian* at 999 the modern approach to statutory construction is:

> "to have regard to the purpose of a particular provision and interpret its language, so far as possible, in a way which best gives effect to that purpose".

250. He noted that until *Ramsay*, however, revenue statutes were "remarkably resistant to the new non-formalist methods of interpretation". The "particular vice" of formalism in this area was "the insistence of the courts on treating every transaction which had an individual legal identity ….as having its own separate tax consequences, whatever might be the terms of the statute". He continued that as Lord Steyn said, it was:

> "those two features - literal interpretation of tax statutes and the formalistic insistence on examining steps in a composite scheme separately - [which] allowed tax avoidance schemes to flourish."

251. He described *Ramsay*, at [29], as having "liberated the construction of revenue statutes from being both literal and blinkered". At [32] he summarised the essence of this liberated approach, noting specifically that it may include the composite approach:

> "to give the statutory provision a purposive construction in order to determine the nature of the transaction to which it was intended to apply and then to decide whether the actual transaction *(which might involve considering the overall effect of a number of elements intended to operate together)* answered to the statutory description…however one approaches the matter, the question is always whether the relevant provision of statute, upon its true construction, applies to the facts as found. As Lord Nicholls of Birkenhead said in [*MacNiven*], para 8:
>
> > "The paramount question always is one of interpretation of the particular statutory provision and its application to the facts of the case."" (Emphasis added.)

252. He continued to emphasise, as he had done in *MacNiven*, that *Ramsay* did not introduce a new doctrine operating within the special field of revenue statutes. On the contrary, as Lord Steyn observed in *McGuckian* at 999 "it rescued law from being "some island of literal interpretation" and brought it within generally applicable principles". He said that the unfortunate tendency "to regard *Ramsay* as establishing a new jurisprudence governed by special rules of its own" was "encouraged by two features characteristic of tax law, although by no means exclusively so" (at [34]):

(1) The first is that:

> "tax is generally imposed by reference to economic activities or transactions which exist, as Lord Wilberforce said, "in the real world"."

(2) The second is that:

> "a good deal of intellectual effort is devoted to structuring transactions in a form which will have the same or nearly the same economic effect as a taxable transaction but which it is hoped will fall outside the terms of the taxing statute. It is characteristic of these composite transactions that they will include elements which have been inserted without any business or commercial purpose but are intended to have the effect of removing the transaction from the scope of the charge."

253. He continued to caution, at [35], as he had also done in *MacNiven*, that comments made in the cases such as *Burmah Oil*, *Furniss* and *Carreras* are not to be taken out of context, in effect, as justifying a broad-brush approach. In doing so, he did not suggest, however, that those cases were wrongly decided or that the wrong approach was taken. He said that in those cases, in looking at the overall effect of the composite transactions in question, "*on the true construction of the relevant provisions of the statute*, the court treated the elements inserted into the transactions without any commercial purpose as having no significance" (emphasis added). However, the view based on these cases that, in the application of "*any* taxing statute, transactions or elements of transactions which had no commercial purpose were to be disregarded" is "going too far" in that:

> "It elides the two steps which are necessary in the application of any statutory provision: first, to decide, on a purposive construction, exactly what transaction will answer to the statutory description and secondly, to decide whether the transaction in question does so.
>
> As Ribeiro PJ said in [*Arrowtown* at [35]]…" (as set out at [214] above).

254. He said, at [37] and [38], that the need to avoid sweeping generalisations about disregarding transactions undertaken for the purpose of tax avoidance was shown by *MacNiven* which, in his view, shows:

> "the need to focus carefully upon the particular statutory provision and to identify its requirements before one can decide whether circular payments or elements inserted for the purpose of tax avoidance should be disregarded or treated as irrelevant for the purposes of the statute."

255. In the same passage, he commented on Lord Hoffmann's approach in *MacNiven* as not "an unreasonable generalisation" but said:

> "we do not think that it was intended to provide a substitute for a close analysis of what the statute means. It certainly does not justify the assumption that an answer can be obtained by classifying all concepts *a priori* as either "commercial" or "legal". That would be the very negation of purposive construction: see Ribeiro PJ in *Arrowtown* at paras 37 and 39…."
> [see [246] above]

256. In turning to applying these principles to the facts of *BMBF*, Lord Nicholls said, at [39], that *BMBF*, like *MacNiven*, illustrates the need for a close analysis of what, on a purposive construction, the statute actually requires. In that context, he considered that the "object of granting the allowance is to provide a tax equivalent to the normal accounting deduction from profits for the depreciation of machinery and plant used for the purposes of the trade". He said that:

> "Consistently with this purpose, the relevant provision requires that a trader should have incurred capital expenditure on the provision of machinery or plant for the purposes of his trade. When the trade is finance leasing, this means that the capital expenditure should have been incurred to acquire the machinery or plant for the purpose of leasing it in the course of the trade. In such a case, it is the lessor as owner who suffers the depreciation in the value of the plant and is therefore entitled to an allowance against the profits of his trade."

257. At [40] he held that the statutory requirements he had described are "in the case of a finance lease concerned entirely with the acts and purposes of the lessor". In his view the CAA:

> "says nothing about what the lessee should do with the purchase price, how he should find the money to pay the rent or how he should use the plant. As Carnwath LJ said in the Court of Appeal [2003] STC 66, 89, para 54:
>
> > "There is nothing in the statute to suggest that 'up-front finance' for the lessee is an essential feature of the right to allowances. The test is based on the purpose of the lessor's expenditure, not the benefit of the finance to the lessee.""

258. He held, at [41], that so far as the lessor was concerned, all the requirements to qualify for allowances were satisfied noting that a director of BF, "gave unchallenged evidence that from its point of view the purchase and lease back was part of its ordinary trade of finance leasing" and that "if one examines the acts and purposes of [BF], it would be very difficult to come to any other conclusion". He thought that the finding of the Special Commissioners that the transaction "had no commercial reality" depended entirely upon an examination of what happened to the purchase price after BF paid it to BGE. However, in his view "these matters do not affect the reality of the expenditure by [BF] and its acquisition of the pipeline for the purposes of its finance leasing trade".

259. At [42] he concluded that, in light of the purpose of s 24 CAA, on the facts of this case, the fact that there were pre-ordained arrangements and a circular movement of funds was simply not relevant to the analysis:

> "if the lessee chooses to make arrangements, even as a preordained part of the transaction for the sale and lease back, which result in the bulk of the purchase price being irrevocably committed to paying the rent, that is no concern of the lessor. From his point of view, the transaction is exactly the same. No one disputes that [BF] had acquired ownership of the pipeline or that it generated income for [BF] in the course of its trade in the form of rent chargeable to corporation tax. In return it paid £91m. The circularity of payments which so impressed Park J and the special commissioners arose because [BF], in the ordinary course its business, borrowed the money to buy the pipeline from Barclays Bank and Barclays happened to be the bank which provided the cash collateralised guarantee to [BF] for the payment of the rent. But these were happenstances. None of these transactions, whether circular or not, were necessary elements in creating the entitlement to the capital allowances."

260. *BMBF* sets out very clearly the effect of the decision in *Ramsay* (including as regards the composite approach) and the correct approach to be adopted in construing tax legislation. This has been recognised in many subsequent decisions including the latest decisions on this topic in *UBS* and *Rangers*.

Scottish Provident

261. The decision in *Scottish Provident Institution v Inland Revenue Commissioners* [2004] UKHL TC 76 538 ("*Scottish Provident*") was released on the same day as that in *BMBF* by the same panel as in *BMBF*. The case concerned a scheme designed to take advantage of a change in the law governing the taxation of gains and losses made by mutual life offices on the grant or disposal of options to buy or sell gilts. Under the scheme:

> (1) The life office, SPI, granted Citibank the option to buy a quantity of gilts from it at a "strike price" of 70, well below their anticipated market value at the time the option was exercised, in return for a premium. Under the law then in force, the premium was exempt from tax.
>
> (2) After the law had changed, Citibank exercised the option, requiring SPI to sell the gilts to it at a loss. Under the law then in force, the loss was allowable for tax purposes. In order to ensure that no real loss could be suffered by either party, the scheme also provided for Citibank to grant an option to SPI, entitling it to buy a matching quantity of gilts from the bank at a strike price of 90, calculated so that the overall movements of money between the parties were equivalent.
>
> (3) It was anticipated that both options would be exercised, but there was a possibility that they might not be. In the event, both options were exercised, and neither gilts nor money changed hands.

262. Lord Nicholls set out, at [18], that whether SPI was entitled to treat the loss suffered on the exercise of the option granted to the bank as an income loss essentially depended on whether the option gave the bank an "entitlement" to gilts within the meaning of the relevant statute. At [19], he noted that if attention was confined to that option, it "certainly gave [the bank] an entitlement, by exercise of the option, to the delivery of gilts" but "if the option formed part of a larger scheme by which [the bank's] right to the gilts was bound to be cancelled by SPI's right to the same gilts, then it could be said that in a practical sense [the bank] had no entitlement to gilts". He then endorsed the view that a purposive approach to the construction of tax legislation allows and indeed may require a composite approach:

> "Since the decision of this House in [Ramsay] it has been accepted that the language of a taxing statute will often have to be given a wide practical meaning of this sort which allows (and indeed requires) the Court to have regard to the whole of a series of transactions which were intended to have a commercial unity. Indeed, it is conceded by SPI that the Court is not confined to looking at the Citibank option in isolation. If the scheme amounted in practice to a single transaction, the Court should look at the scheme as a whole. [Counsel] for SPI, accepted before the Special Commissioners that if there was "no genuine commercial possibility" of the two options not being exercised together, then the scheme must fail."

263. Lord Nicholls continued, at [20] and [21], to note that the taxpayer's counsel submitted that "even if the parties intended that both options should be exercised together…the Court could treat them as a single transaction only if there was "no practical likelihood" that this would not happen". In that context, the Special

Commissioners, in adopting (at [24]) the analogy of horserace betting, had accepted this. They said that:

> "If the chance of the price movement occurring was similar to an outsider winning a horse race we consider that this, while it is small, is not so small that there is no reasonable or practical likelihood of its occurring; outsiders do sometimes win horse races."

264. Lord Nicholls noted, at [21], that the test of "no practical likelihood" derived from the speech of Lord Oliver of Aylmerton in *Craven* v *White* [1989] A C 398, at page 514. However, he thought there was a distinction between that case and *Scottish Provident*. In *Craven v White* "important parts of what was claimed by the Revenue to be a single composite scheme did not exist at the relevant date" (see Lord Oliver (at page 498)); there was an uncertainty about "whether the alleged composite transaction would proceed to completion which arose, not from the terms of the alleged composite transaction itself, but from the fact that, at the relevant date, no composite transaction had yet been put together" ([22]). On the other hand, in *Scottish Provident*:

> "…the uncertainty arises from the fact that the parties have carefully chosen to fix the strike price for the [option granted to SPI] at a level which gives rise to an outside chance that the option will not be exercised. There was no commercial reason for choosing a strike price of 90. From the point of view of the money passing (or rather, not passing), the scheme could just as well have fixed it at 80 and achieved the same tax saving by reducing the Citibank strike price to 60. It would all have come out in the wash. Thus the contingency upon which SPI rely for saying that there was no composite transaction was a part of that composite transaction; chosen not for any commercial reason but solely to enable SPI to claim that there was no composite transaction. It is true that it created a real commercial risk, but the odds were favourable enough to make it a risk which the parties were willing to accept in the interests of the scheme."

265. At [23], Lord Nicholls held that it would "destroy the value of the *Ramsay* principle of construing provisions" such as those in issue as referring to the effect of composite transactions:

> "if their composite effect had to be disregarded simply because the parties had deliberately included a commercially irrelevant contingency, creating an acceptable risk that the scheme might not work as planned. We would be back in the world of artificial tax schemes, now equipped with anti-*Ramsay* devices. The composite effect of such a scheme should be considered as it was intended to operate and without regard to the possibility that, contrary to the intention and expectations of the parties, it might not work as planned."

266. At [24], he concluded, therefore, that the Special Commissioners erred in law in finding that "there was a realistic possibility of the options not being exercised simultaneously meant, without more, that the scheme could not be regarded as a single composite transaction".

UBS and Rangers

267. In the more recent cases of *UBS* and *Rangers FC (2012) plc v HMRC* [2017] 1 WLR 2767 ("*Rangers*"), the Supreme Court has endorsed fully the explanation of the modern approach to statutory construction in *BMBF* and the approach in *Scottish Provident*.

268. In *UBS* Lord Reed (with whom the other Lords agreed), at [61], referred to *BMBF* and noted that until *Ramsay* "the interpretation of fiscal legislation was based predominantly on a linguistic analysis" and that:

> "the courts treated every element of a composite transaction which had an individual legal identity (such as a payment of money, transfer of property, or creation of a debt) as having its own separate tax consequences, whatever might be the terms of the statute" (citing Lord Steyn in *McGuickan* at p 999)."

269. He continued, at [62], that the significance of the *Ramsay* case was "to do away with both those features". In his explanation of *Ramsay*, he very plainly accepted that it was established by that case that the composite approach is a feature of applying a purposive approach to the interpretation of tax legislation:

> "First, it extended to tax cases the purposive approach to statutory construction which was orthodox in other areas of the law. *Secondly, and equally significantly, it established that the analysis of the facts depended on that purposive construction of the statute.* Thus, in *Ramsay* itself, the terms "loss" and "gain", as used in capital gains tax legislation, were purposively construed as referring to losses and gains having a commercial reality. Since the facts concerned a composite transaction forming a commercial unity, with the consequence that the commercial significance of what had occurred could only be determined by considering the transaction as a whole, the statute was construed as referring to the effect of that composite transaction….." (Emphasis added.)

270. He continued at [63] to refer to *BMBF* (at [32] to [34] and [64]) and said that this approach has proved to be particularly important in relation to tax avoidance schemes as a result of two factors identified in *BMBF* at [34]. In that context he also referred to the comments of Carnwath LJ in the Court of Appeal in *BMBF* [2003] STC 66, at [66] that, taxing statutes generally "draw their life-blood from real world transactions with real world economic effects". He said that:

> "Where an enactment is of that character, and a transaction, or an element of a composite transaction, has no purpose other than tax avoidance, it can usually be said, as Carnwath LJ stated, that "to allow tax treatment to be governed by transactions which have no real world purpose of any kind is inconsistent with that fundamental characteristic." Accordingly, as Ribeiro PJ said in [*Arrowtown* at [35]], where schemes involve intermediate transactions inserted for the sole purpose of tax avoidance, it is quite likely that a purposive interpretation will result in such steps being disregarded for fiscal purposes. But not always."

271. He then made a similar observation, at [65], as that made by Lord Nicholls in *BMBF* that in cases such as *Furniss*, *Carreras*, *Burmah Oil* and he added later cases including *Scottish Provident*:

> "*the court considered the overall effect of the composite transaction, and concluded that, on the true construction of the relevant statute, the elements which had been inserted without any purpose other than tax avoidance were of no significance. But it all depends on the construction of the provision in question.* Some enactments, properly construed, confer relief from taxation even where the transaction in question forms part of a wider arrangement undertaken solely for the purpose of obtaining the relief. The point is illustrated by the decisions in [*MacNiven*] and [*BMBF*] itself." (Emphasis added.)

272. He said, at [66] that the position was summarised by Ribeiro PJ in *Arrowtown* at [35] (as set out at [214] above). He cautioned, at [67], that "references to "reality" should not, however, be misunderstood" and said, at [67] and [68]:

> "In the first place, the approach described in [*BMBF*] and the earlier cases in this line of authority has nothing to do with the concept of a sham, as explained in *Snook.* On the contrary, as Lord Steyn observed in *McGuckian*

at p 1001, tax avoidance is the spur to executing genuine documents and entering into genuine arrangements.

> Secondly, it might be said that transactions must always be viewed realistically, if the alternative is to view them unrealistically. *The point is that the facts must be analysed in the light of the statutory provision being applied. If a fact is of no relevance to the application of the statute, then it can be disregarded for that purpose. If, as in Ramsay, the relevant fact is the overall economic outcome of a series of commercially linked transactions, then that is the fact upon which it is necessary to focus. If, on the other hand, the legislation requires the court to focus on a specific transaction, as in MacNiven and [BMBF], then other transactions, although related, are unlikely to have any bearing on its application*." (Emphasis added.)

273. At [69] and [70], he then referred at some length to the *Scottish Provident* case and proceeded to apply the approach set out in that case in concluding that a contingency which created a minor risk, but one which the parties were willing to accept in the interests of the scheme could in effect be ignored (see [88]).

274. HMRC based some of their arguments on the year of allocation issue specifically on the decision in *Rangers*. In that case, the taxpayer company (RFC) was a member of group of companies which set up a trust arrangement for the remuneration of employees. When it wished to benefit an employee, it made a payment to a trust, asked the trustee to resettle the sum on to a sub-trust and requested that the sub-trust income and capital should be applied in accordance with the employee's wishes. The trustee had a discretion whether to comply with those requests, but, in practice, the trustee without exception created the requested sub-trust. The employee was appointed as protector of the sub-trust with the power to change its beneficiaries.

275. HMRC assessed RFC to tax on the basis that under the PAYE system it should have accounted for income tax and national insurance contributions (NICs) on amounts paid into the main trust on the basis they comprised payments of emoluments/earnings from an employment. The Supreme Court unanimously decided in favour of HMRC. Lord Hodge gave the judgment with which the other Lords agreed.

276. In considering the correct approach to the employment tax provisions under consideration, Lord Hodge similarly described the speech which Lord Nicholls made in *BMBF* as explaining "the true principle established in *Ramsay*" and the cases which followed it. He referred, at [13], to Lord Nicholls' comments at [34] and [36] and to the same comments of Carnwath LJ in the Court of Appeal as Lord Reed had referred to in *UBS*. At [14], he endorsed what he described as Lord Reed's helpful summary of the significance of the new approach, which *Ramsay*, as explained in *BMBF*, has brought about citing from [62] of his decision in *UBS*. He concluded, at [16], that accordingly the proper approach was, first, to interpret the relevant statutory provisions purposively and, secondly, to analyse the facts in the light of those statutory provisions so construed.

277. He said, at [36], that the central issue was "whether it is necessary that the employee himself or herself should receive, or at least be entitled to receive, the remuneration for his or her work in order for that reward to amount to taxable emoluments". In his view, at [37] and [38], a careful and detailed examination of the provisions of the primary legislation revealed no such requirement. Moreover, at [39] and [40], he saw "nothing in the wider purpose of the legislation" which excluded from the charge or the PAYE regime, remuneration which the employee is entitled to have paid to a third party and thought that the relevant subordinate legislation points

in the same direction. He concluded, at [41], that as a general rule, therefore, the charge to tax on employment income:

> "*extends to money that the employee is entitled to have paid as his or her remuneration whether it is paid to the employee or a third party*. The legislation does not require that the employee receive the money; a third party, including a trustee, may receive it." (Emphasis added.)

278. He continued in the same passage that while that is a general rule, not every payment by an employer to a third party falls within the tax charge and it is necessary to consider other circumstances revealed in case law and in statutory provisions which fall outside the general rule. In considering this, he said, in effect, that where there is "an arrangement by which the employer's payment does not give the intended recipient an immediate vested beneficial interest" but "on a proper analysis of the facts there is only a contingent right", then "the taxable earnings or emoluments are not paid by the employer as remuneration until the occurrence of the contingency" and he cited examples of cases where rights were asserted to be contingent only at [47] and [48].

279. He noted, at [49], that those cases (and others on which RFC relied) were not concerned with the identity of the recipient of the benefit; the focus was on the source or the nature of the right which the employee received and, accordingly, they were not of assistance. Rather, as he continued at [50], the advice of the Privy Council in *Hadlee v Commissioners of Inland Revenue* [1993] AC 524 ("*Hadlee*") was in point. That case concerned legislation in New Zealand which provided that income tax was payable by every person on income derived by him during the year for which tax was payable. A partner in an accountancy firm assigned a proportion of his share in the partnership to a trust under which the primary beneficiaries were his wife and child. The New Zealand courts rejected his argument that he was not liable to income tax on that proportion of his annual partnership income. The Privy Council upheld their decision, holding that income tax was a tax on income which was the product of the taxpayer's personal exertion and that the taxpayer could not escape liability to pay that tax by assigning a part of his share in the partnership. Lord Hodge noted that:

> "While the relevant provision of the New Zealand statute was worded differently from the United Kingdom legislation, the latter, by its emphasis on emoluments arising from a taxpayer's employment, adopts a similar concept of the tax charge. It supports the view which I have reached that a charge to income tax on employment income can arise when an arrangement gives a third party part or all of the employee's remuneration."

280. He said, at [51], that it was also necessary to decide whether under the PAYE provisions there had been a "payment" of emoluments/earnings from which deductions were required. In that context he considered that misplaced reliance on "judicial glosses" in earlier cases on the meaning of the term "payment". Whilst the judicial gloss put upon that term gave a sensible result in *Garforth v Newsmith Stainless Ltd* [1979] 1 WLR 409, that gloss was misapplied in *Aberdeen Asset Management plc v Revenue and Customs Comrs* 2014 SC 271 and *Sempra Metals Ltd v Revenue and Customs Comrs* [2008] STC (SCD) 1062) (see [52] to [57]).

281. He concluded, at [58] and [59], that:

> "In summary, (i) income tax on emoluments or earnings is due on money paid as a reward or remuneration for the exertions of the employee; (ii) focusing on the statutory wording, [none of the relevant provisions]…. (except section 62(2)(b)), provide that the employee himself or herself must receive the remuneration; (iii) in this context the references to making a relevant payment "to an employee" or "other payee" in the PAYE

> Regulations fall to be construed as payment either to the employee or to the person to whom the payment is made with the agreement or acquiescence of the employee or as arranged by the employee, for example by assignation or assignment; (iv) the specific statutory rule governing gratuities, profits and incidental benefits in section 62(2)(b) of ITEPA applies only to such benefits; (v) the cases, to which I have referred above, other than *Hadlee*, do not address the question of the taxability of remuneration paid to a third party; (vi) *Hadlee* supports the view which I have reached; and (vii) the special commissioners in *Sempra Metals* (and in *Dextra*) were presented with arguments that misapplied the gloss in *Garforth* and erred in adopting the gloss as a principle so as to exclude the payment of emoluments to a third party.
>
> Parliament in enacting legislation for the taxation of emoluments or earnings from employment has sought to tax remuneration paid in money or money's worth. No persuasive rationale has been advanced for excluding from the scope of this tax charge remuneration in the form of money which the employee agrees should be paid to a third party, or where he arranges or acquiesces in a transaction to that effect….."

282. Applying the legislation to the facts Lord Hodge held, at [64], that the relevant provisions for the taxation of emoluments/earnings were and are "drafted in deliberately wide terms to bring within the tax charge money paid as a reward for an employee's work". The scheme was designed to give each footballer access without delay to the money paid into the trust, if he so wished, and to provide that the money, if then extant, would ultimately pass to the member or members of his family whom he nominated. He concluded, therefore, that "having regard to the purpose of the relevant provisions….the sums paid to the trustee of the main trust for a footballer constituted the footballer's emoluments or earnings".

283. At [65], he said that the fact that there was a chance that the trust company as trustee of the main trust might not agree to set up a sub-trust and that as trustee of a sub-trust it might not give a loan of the funds of the sub-trust to the footballer, did not alter the nature of the payments to the main trust. That was on the basis that, in applying a purposive interpretation of a taxing provision in the context of a tax avoidance scheme it is legitimate to look to the composite effect of the scheme as it was intended to operate (by reference to *Scottish Provident* at [23]). The footballers, when accepting the offer of higher net remuneration through the trust scheme which the side letters envisaged, were prepared to take the risk that the scheme might not operate as planned. The fact that the risk existed did not alter the nature of the payment to the trustee of the principal trust. Accordingly, he held, at [67], that payment to the trust should have been subject to deduction of income tax under the PAYE Regulations.

Submissions

HMRC's submissions

284. Mr Chacko did not make any comments in addition to those made above on the purpose of s 850. He made the following submissions in the alternative:

(1) First, he said the terms of s 850 were engaged on the basis that the documents demonstrate that RemCom actually "allocated" the individual shares to the Members upfront when they notified the Members of them albeit that they only received the benefit of the individual shares in stages over a period of time. The factual matters on which HMRC relied included that (a) the Awards are described as *deferred* profit allocations and arrangements in the documentation, and (b) the wording of the RemCom minutes of 15 January 2013 and the letters

Odey sent to members in 2013 notifying them of the allocation of profits. Whilst the form of the letters changed in January 2014, it appears that nothing of substance changed in how the Plan operated.

(2) Second, HMRC suggested that something less than what they described as an actual "allocation" of the individual shares suffices for the Members to be taxable in the year of allocation. They said that on a realistic view of the facts, "in substance and reality", the individual shares should be "regarded as "allocated" to the relevant Members in the year of allocation on the basis that PSCL effectively held the individual shares for their benefit throughout and it was inevitable that they would receive the reallocation of Special Capital. Mr Chacko made the following main points:

(a) The allocation of the individual shares to the Members logically and temporally was the initial step, as each individual share was calculated by reference to the gross sum before the deduction of corporation tax which PSCL had to pay on the relevant sums.

(b) When the deferred share was transferred to PSCL, individual shares were, in effect, "earmarked" for each relevant Member, so that an amount of money or number of shares could always be attributed to the Member who was to receive a reallocation of Special Capital (unless he forfeited it by leaving Odey). Each individual share was invested in Funds according to the wishes of the relevant Member for whom it was "earmarked" thereby fulfilling the objective of the Plan that Members had "skin in the game"; they had money at risk given the relevant monies were held in the Funds for them.

(c) When the deferred share was transferred to PSCL, RemCom informed PSCL of the Members for whom each individual share was to be held and of the intended "reallocation" of Special Capital. Whilst PSCL had a formal discretion under the 2011 LLP Agreement whether or not to endorse this recommendation, in practice, PSCL always did so and there was no realistic possibility that it would not do so.

(d) In fact, it was a foregone conclusion that the Members would receive the reallocations of Special Capital which RemCom recommended, subject to the risk, accepted by the Members, that they would "forfeit" them if they left Odey or if Odey suffered a shortfall of regulatory capital:

(i) When Members were notified of their individual shares they were told that "PSCL *will transfer* this investment to you in two annual instalments…" (emphasis added), although that was subject to PSCL's "policies and discretion" and as PSCL would confirm to the Member.

(ii) When PSCL gave confirmation to Members of the Awards, it made clear that the circumstances in which it would exercise its discretion not to make the promised reallocations were only if (A) the Member left Odey, or (B) Odey needed to call on the funds for its capital requirements.

(iii) Once PSCL had agreed to the initial recommendations made in respect of individual shares and invested the sums as Special Capital, PSCL had no real freedom in respect of those sums. As noted, it was for ExCo to decide how the monies were to be invested and PSCL could not withdraw the sums without ExCo's consent and could only

reallocate the Special Capital to another Member following a recommendation from ExCo.

(iv) This limited discretion PSCL had to make a reallocation of Special Capital was subject to an implied contractual term that it must be exercised in good faith and rationally, in accordance with the Remuneration Policy as further explained below.

(e) Throughout the documents there are references to the "forfeiture" and "lapsing" of awards. Such language is used when a person has already been made an award which he then loses.

(3) HMRC argued that, even if, on a realistic view of the facts, the relevant profits were allocated to PSCL: (a) The individual shares were in reality rewards for the Members' work and can truly be described as remuneration (see *Hosking v Marathon Asset Managemen*t *LLP* [2017] Ch 157 at [43(ii)]) and, therefore, constitute income resulting from personal activities (as in *Hadlee*), and (b) on that basis, on the authority of *Rangers*, the Members are taxable in respect of them, whether or not they are paid to them, as they acquiesced or consented to the redirection of the relevant sums to PSCL:

(a) As set out above, in *Hadlee* the Privy Council held that a New Zealand partner who had assigned his partnership share to a trust for his family was still taxable on the share. The court said, at 296, that: "No taxpayer can, by way of assignment, escape assessment of tax on income resulting from his personal activities…". It was held at 298 that there is no basis to distinguish wage earners from professionals who are rewarded (as partners) for their personal exertion. Accordingly, in *Rangers* the Supreme Court applied the decision in *Hadlee* to employment income (see [50]) and held, in effect, that the principle set out in that case applied not only where someone explicitly assigned their income, but also where they acquiesced in its redirection (see [59]).

(b) The Members accepted some degree of risk that they would not receive as much profit share as they would have if they had been paid the profits to which the Awards related immediately. However, for the reasons already set out, the possibility of PSCL exercising its discretion in any more unpredictable sense was illusory. In any event, as the Supreme Court held in *Rangers* at [65], (by reference to Lord Nicholls' comments in *Scottish Provident* at [23]), "the composite effect" of the scheme "should be considered as it was intended to operate and without regard to the possibility that, contrary to the intention and expectation of the parties, it might not work as planned…", including that a discretion conferred on a third party might be exercised against the taxpayer.

(c) In *Rangers*, Lord Hodge was clear that the principle he adopted did not mean a taxpayer would be taxed on a contingent award before the contingency fell away (see [41]). However, in this case, the immediate allocation of the individual shares is not contingent; the contingency relates only to the possibility of eventual receipt.

(4) The deferred share "allocated" to PSCL represents an unallocated reserve (out of which Awards were to be made) rather than a "right" for PSCL to share in the profits of Odey. It is clear that PSCL was not absolutely entitled to deal with the sums transferred to it as it chose. It was wholly owned by a purpose trust the object of which was to seek to ensure that the money so received was contributed as Special Capital which PSCL was not entitled to withdraw without

Odey's consent. The sums must be divided, therefore, among the Members who in reality enjoyed the profits of Odey, in the same proportions as those Members otherwise received their profit shares for that year.

Appellants' submissions

285. Mr Goldberg made the following main points:

(1) The scope of the statutory enquiry mandated by s 850 is limited by the words (i) "during that period" at the end of s 850(1) and (ii) "rights" in the definition of the "profit sharing arrangements" in s 850(2), by reference to which each partner's taxable share of profits is to be determined.

(2) The word "right" may have a broad meaning, but there cannot be a right without some form of entitlement. It is difficult to find authority about the word "right", but in *Melville* it was held, at [15], that the words "right" and "interest" connote "any form of proprietary right or interest which is of value to its holder and which may be turned to account":

(a) a person who thinks that something will happen in the future does not have a right to what he thinks will happen: he merely has a thought, a hope or an expectation falling far short of anything which can be described as a right; and

(b) what may happen in subsequent years cannot affect the profit-sharing arrangements in the year of allocation.

(3) Under the relevant case law, taking a realistic view of the facts in applying a purposive approach to the construction of s 850, requires ascertaining what facts are relevant to their application (see *Arrowtown* at [35] and *BMBF*). For the reasons already given, the fact of relevance to the application of s 850 is *the right* of the Members to share in profits *in the relevant period*, as determined under the 2011 LLP Agreement. The statute is not concerned, therefore, with what might happen in future years and does not allow that to be taken into account. Similarly, in asking specifically about *rights* to share profits, the statute is expressly not asking about what the ultimate economic outcome might be (see the contrast in *MacNiven* and *UBS* (see [66]).

286. Mr Goldberg said that the position may be different if:

(1) The allocation of Special Capital by PSCL to a Member was, as a matter of fact, a foregone conclusion, so that the intermediate steps could be ignored on the basis that they were inserted into the transaction without any business or commercial purpose. However, that is plainly not the case. Moreover, facts may only be ignored where a correct construction of the relevant statutory provision, requires them to be ignored but, for the reasons already given, the Member's right to profits in the relevant year is the very focus of s 850.

(2) On the correct factual analysis, a Member had a right to the individual share in the year of allocation which was subject to defeasance in a subsequent year. However, an analysis of that kind is neither permitted by the statute (which looks at the legal concept of "rights") nor would it accord with a realistic view of the facts relevant to the question posed by s 850.

287. Mr Goldberg continued that, viewing the facts realistically, the Members (a) did not get or have rights to get the individual share in the year of allocation, or (b) have any right to get a reallocation of Special Capital in subsequent years:

(1) It is entirely clear from the applicable terms of the 2011 LLP Agreement, the Remuneration Policy and the letters of January and March sent to Members that Members had no contractual right to the individual shares.

(2) It is also clear from the terms of the 2011 LLP Agreement that PSCL had absolute discretion over whether to contribute the relevant sums to Odey as Special Capital or to make any reallocation of Special Capital to Members (if recommended to do so by ExCo). That accords with one of the purposes of the Remuneration Policy, namely, that the relevant funds were to belong to PSCL in order to achieve the relevant regulatory and commercial aims. Accordingly, a Member had nothing in respect of an Award which he could have turned to account before there was an allocation of Special Capital to him.

(3) Moreover, it was made plain to the Members that "PSCL retains absolute discretion over reallocation … you may not receive a reallocation" and some Members who RemCom recommended should receive an allocation of Special Capital did not in fact receive one. While no doubt everybody "had an expectation that their ship was going to come in eventually, they all knew that that ship could be sunk by stormy financial markets or the choice of PSCL". As Lord Roborough said; "the fact that the amount was not yours and you may never receive it was made clear to us from the outset".

(4) Accordingly, a Member had nothing in respect of an Award which he could have turned to account before there was an allocation of Special Capital to him.

(5) The points made above are reinforced by the fact that, as is clear from clauses 8 and 9 of the 2011 LLP Agreement, the relevant Members did not have any say on the allocation of profits to them and did not have any control over the business of Odey. They had certain limited rights of veto, but they had no positive control.

(6) Overall, the evidence demonstrates that it cannot be claimed that the Remuneration Policy produces a predetermined economic outcome which means that each Award was intended inevitably to end up with Members.

288. Mr Goldberg said that, on the basis that the correct interpretation of the provisions is as he set out, the remainder of HMRC's arguments are untenable. He noted, in particular, that the decisions in *Hadlee* and *Rangers* do not apply given that, for all the reasons he had already set out, the Members had no right to the individual shares or any reallocation of Special Capital which they could assign or redirect or acquiesce in the redirection of and there was no contractual redirection of any funds. The Members of Odey do not have a share of Odey's profits unless and until there has been both calculation and allocation of a relevant sum. He added that, in any event the decision in *Rangers* deals solely with the tax position of employees according to the correct purposive construction of the relevant provisions. It says nothing about the meaning of s 850.

Submissions on correct approach to contractual interpretation

289. In support of his analysis of the contractual position, Mr Goldberg referred to the case law on how the construction of contracts is to be approached. He relied, in particular, on the following comments of Lord Clarke in *Rainy Sky SA & Orsd v Kookmin Bank* [2011] UKSC 50 at [21]:

> "language used by parties will often have more than one potential meaning. I would accept the submission made on behalf of the appellants, that the exercise of construction is, essentially, one unitary exercise in which the court must consider the language used and ascertain what a reasonable person, that is a person who has all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract, would have understood the parties to have

> meant. In doing so, the court must have regard to all the relevant surrounding circumstances. If there are two possible constructions, the court is entitled to prefer the construction which is consistent with business common sense and to reject the other."

290. Mr Goldberg submitted that the approach in the *Rainy Sky* case has been approved by the Supreme Court in *Wood v Capita Insurance Services Ltd* [2017] UKSC 24. I note that prior to the decision in that case, there was some debate about the respective importance of what Lord Hodge (who gave the leading judgment in *Wood v Capita*) referred to as "textualism" and "contextualism" in interpretation. Lord Hodge said that both approaches have a role and it is not a case of one approach or the other. He set out, at [10], that the court's task is to ascertain "the objective meaning of the language which the parties have chosen to express their agreement" and noted that it has:

> "long been accepted that this is not a literalist exercise focused solely on a parsing of the wording of the particular clause but that the court must consider the contract as a whole and, depending on the nature, formality and quality of drafting of the contract, give more or less weight to elements of the wider context in reaching its view as to that objective meaning…"

291. He continued that it is affirmed in the cases that "the factual background known to the parties at or before the date of the contract, excluding evidence of the prior negotiations" is of relevance. He noted, however, that when in *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896 Lord Hoffmann (at pages 912-913) reformulated the principles of contractual interpretation, "some saw his second principle, which allowed consideration of the whole relevant factual background available to the parties at the time of the contract, as signalling a break with the past". But Lord Bingham in an extra-judicial writing (*A new thing under the sun? The interpretation of contracts and the ICS decision* Edin LR Vol 12, 374-390) "persuasively demonstrated that the idea of the court putting itself in the shoes of the contracting parties had a long pedigree".

292. In the passage in the *Investors* case to which Lord Hodge referred, Lord Hofmann gave the following guidance on the relevance of background information:

> "(1) Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.
>
> (2) …Subject to the requirement that it should have been reasonably available to the parties and to the exception to be mentioned next, [the background] includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.
>
> (3) The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent. They are admissible only in an action for rectification…."

293. At [11], Lord Hodge said the following as regards interpretation as "a unitary exercise":

> "where there are rival meanings, the court can give weight to the implications of rival constructions by reaching a view as to which construction is more consistent with business common sense. But, in striking a balance between the indications given by the language and the implications of the competing constructions the court must consider the quality of drafting of the clause….and it must also be alive to the possibility that one side may have agreed to something which with hindsight did not serve his interest… Similarly, the court must not lose sight of the possibility that a provision may

> be a negotiated compromise or that the negotiators were not able to agree more precise terms."

294. He said, at [12], that this unitary exercise involves "an iterative process by which each suggested interpretation is checked against the provisions of the contract and its commercial consequences are investigated" and to his mind:

> "once one has read the language in dispute and the relevant parts of the contract that provide its context, it does not matter whether the more detailed analysis commences with the factual background and the implications of rival constructions or a close examination of the relevant language in the contract, so long as the court balances the indications given by each".

295. He concluded, at [13], that "textualism" and "contextualism" are not "conflicting paradigms in a battle for exclusive occupation of the field of contractual interpretation". Rather when interpreting any contract, they can be used "as tools to ascertain the objective meaning of the language which the parties have chosen to express their agreement". He noted that the extent to which each "tool" will assist the court will vary according to the particular circumstances:

> "Some agreements may be successfully interpreted principally by textual analysis, for example because of their sophistication and complexity and because they have been negotiated and prepared with the assistance of skilled professionals. The correct interpretation of other contracts may be achieved by a greater emphasis on the factual matrix, for example because of their informality, brevity or the absence of skilled professional assistance......The iterative process, of which Lord Mance spoke in *Sigma Finance Corpn* (above), assists the lawyer or judge to ascertain the objective meaning of disputed provisions."

296. Mr Goldberg said that, applying this approach to the construction of the relevant documents, it is highly relevant that the evidence establishes that the Members knew that the individual shares belonged to PSCL and to nobody else. As a matter of business common sense, as is consistent with clause 12.2 of the 2011 LLP Agreement, the Members were told that the individual shares were given to PSCL and not to them, and that while held by PSCL as Special Capital they were subject to PSCL's absolute and sole discretion.

297. Mr Chacko did not dispute the relevance of the caselaw set out above. He said that it must be borne in mind that it is clear from that caselaw that, in construing contractual provisions, it is not permissible to have regard to the parties' subjective views on the meaning of those provisions, especially when expressed many years after the conclusion of the relevant contractual arrangements.

298. As noted, Mr Chacko emphasised that, in HMRC's view, PSCL was not free to use the deferred share it received as it wished and, in effect, had only a "theoretical discretion" for the reasons he had already set out. He submitted that the limited discretion it had under the 2011 LLP Agreement was subject to the orthodox and well-established principle of contract law that, where a contract confers a discretion on one of the contracting parties which may adversely affect the interests of the other party, as set out in Lewison on the Interpretation of Contracts, 6th edn, ch.14 at 11:

> "it will usually be implicit that the discretion must be exercised honestly and rationally and for the purpose for which it was conferred…. Accordingly, if a contract confers an apparently unfettered discretion, that discretion must not be exercised capriciously or unreasonably."

299. Mr Chacko noted that the principle has been explained most recently by the Supreme Court in *Braganza v BP Shipping* [2015] 1 WLR 1661 ("*Braganza*") in considering a term in an employment contract that provided the chief engineer on

board a vessel with a death in service benefit save where his death had resulted from his own wilful act. In holding that a term of good faith should be implied into the relevant term in the employment contract, Baroness Hale of Richmond said the following, at [18]:

> "Contractual terms in which one party to the contract is given the power to exercise a discretion, or to form an opinion as to relevant facts, are extremely common.
>
> It is not for the courts to rewrite the parties' bargain for them, still less to substitute themselves for the contractually agreed decision-maker. Nevertheless, the party who is charged with making decisions which affect the rights of both parties to the contract has a clear conflict of interest. That conflict is heightened where there is a significant imbalance of power between the contracting parties as there often will be in an employment contract. The courts have therefore sought to ensure that such contractual powers are not abused. They have done so by implying a term as to the manner in which such powers may be exercised, a term which may vary according to the terms of the contract and the context in which the decision-making power is given."

300. At [19], Baroness Hale continued to indicate that the standard of review generally adopted by the courts to the decisions of a contracting party should be no more demanding than the standard of review adopted in the judicial review of administrative action. Rather the question is whether it should be any less demanding. In that context she considered, at [20] to [31], whether an implied term should include both limbs of the "Wednesbury reasonableness" test referring to *Associated Provincial Picture Houses Ltd v Wednesbury Corporation* [1948] 1 KB 223 (see [306] for a description of the two limbs of that test). Having set out a detailed review of the cases at [20] to [31], she said that she thought both limbs were applicable but it was not necessary to form a definitive view "given that the question may arise in so many different contractual contexts, it may well be that no precise answer can be given". Lord Hodge thought that, whilst the courts had not yet spoken with one voice, in reviewing at least some contractual discretionary decisions, the court should address both limbs of the test. Although Lord Neuberger formed a different overall conclusion, he essentially agreed that the approach set out by Baroness Hale was the correct one.

301. Mr Chacko submitted, as Mr Goldberg did not appear to dispute, that this principle can apply to decision-making in an LLP (see Whittaker & Machell on the Law of Limited Liability Partnerships ("**Whittaker**") 4th edn (2016), ch.17 at 26 to 37) and that it applies to powers to award discretionary bonuses to a member of an LLP on the basis of the decision in *Reinhard v Ondra LLP* [2015] EWHC 26 (Ch) [2015] EWHC 1869 (Ch), [2016] 2 BCLC 571 (at [412] and [445]).

302. As set out at [411] of *Reinhard v Ondra LLP*, that case concerned (among other issues) a claim by a member of an LLP that the LLP had acted in breach of an implied term to act in good faith as regards the exercise of its discretion to pay the member a bonus which provided that:

> "You will also be eligible to receive a discretionary bonus. The partnership will take into account various factors in exercising its discretion, such as the performance of Ondra as a whole and your individual contribution to the partnership."

303. At [412] the court described the "well settled" principles governing the exercise of such a discretion as follows:

> "It must be exercised in good faith and rationally and not perversely: see *Clark v Nomura International plc* [2000] IRLR 766 (**"*Nomura*"**) as approved in *Horkaluk v Cantor Fitzgerald International* [2005] ICR 402. In *Nomura*, Burton J rejected the tests of capriciousness on the one hand, and absence of reasonable or sufficient grounds on the other. He considered that the correct test was one of irrationality or perversity (of which capriciousness would be a good example), adding that this meant "that no reasonable employer would have exercised his discretion in this way". He regarded this as the same test as that applied in what is now the Administrative Court. Another authority is *Keen v Commerzbank AG* [2006] EWCA Civ 1536 ("Keen"), [2007] ICR 623 in which Moses LJ made some observations about the provision of information in relation to the award of bonuses: see at [111]:
>
>> "…An employee must establish, at least, a *prima facie* case of irrationality, before an employer is required to justify his decision. For example, an employee would be able to rely upon a refusal to pay an award, despite the success of his department, or a significantly lower award than one awarded to comparable fellow employees. It is likely that such cases can only be met by a sustainable explanation from the employer. The need to provide reasons arises, not to give the right to challenge content, but because, without any explanation, the employee is likely to succeed. In short, in cases which do not rely upon a breach of the implied duty of trust and confidence, the absence of reasons is only of evidential significance. The absence of reasons is not dispositive of the issue of rationality.""

304. At [445], the High Court concluded that the partnership did not exercise its discretion properly. Having failed to give proper weight to what he had achieved and having improperly taken into account that which he did not achieve, the partnership was in breach of contract. In the language of the cases, the decision was irrational or perverse. At [447] and [448], the High Court explained that Mr Reinhard's remedy was for damages for breach of contract (as was the way in which the matter was approached in *Clark v Nomura*) and that in carrying out that exercise, the court has the same unfettered discretion as the partnership which must be exercised reasonably.

305. Mr Chacko continued that the implication of such a term is "extremely difficult to exclude". He submitted that, in effect, it can be excluded only where there is already a tight set of controls on the relevant discretion on the basis of the comments of Jackson LJ at [83] to [92] of *Mid Essex Hospital Services NHS Trust v Compass Group UK and Ireland Ltd* [2013] EWCA Civ 200). He also noted that in Whittaker the authors suggest that such an implied term may not apply to require the application of the second limb of the *Wednesbury* test, where the relevant discretion is stated to be "absolute". He pointed out, however, that this version of Whittaker was written in 2016, and since then it has been held, that a term of that nature may be implied even where the parties have stressed the discretionary nature of the power such as by describing the discretion as being "absolute" in *Faieta v ICAP Management Services Ltd* [2017] EWHC 2995 (QB), [2018] IRLR 227 ("*Faieta*").

306. In *Faieta* the issue was the correct interpretation of a garden leave clause which provided that "the company may in its absolute discretion require [Mr Faieta]…not to perform any of his duties…provided always that throughout the period [his] salary and contractual benefits shall continue to accrue or be paid". In July 2014 Mr Faieta was put on garden leave and was dismissed in November 2015. The company admitted that he was wrongfully dismissed. Mr Faieta sought damages for alleged breach of contract in placing him on garden leave on the basis that the company was in breach of an implied term of rationality and/or of trust and confidence in doing so.

The High Court held, at [28], that on the authorities reviewed, which included *Braganza*, there was an implied duty on the company of that kind. The court said that, on the basis of the decision in *Braganza*:

> "the question for the court is not whether the outcome for the claimant is objectively reasonable but whether the decision-making process is lawful and rational in the public law sense, that the decision is made rationally (as well as in good faith) and consistently with the contractual purpose. Further it seems to me following *Braganza* that the court needs to consider the two limbs of the test: whether the right matters have been taken into account in reaching the decision and secondly even though the right things have been taken into account, the result is so outrageous that no reasonable decision maker could have reached it."

307. Mr Chacko submitted that:

(1) In all the circumstances, the implication of a term that PSCL would exercise its discretion to make reallocations of Special Capital in good faith and rationally, by taking account of ExCo's recommendation and of the Remuneration Policy, is necessary for the commercial efficacy of the relevant provision in the 2011 LLP Agreement. There was plainly an imbalance of power between the individual Members and PSCL and, for that matter, ExCo who had to make a recommendation for PSCL to make reallocations of Special Capital before PSCL could exercise its discretion to do so. On the appellants' own case, in deciding whether to follow a reallocation recommendation by RemCom and, if so, how much to re-allocate, PSCL faced a conflict of interest between it and the Members because the alternative was for it to retain that capital itself.

(2) Without such an implied term, the Members would have had no means of redress if, for example, PSCL had: (a) in bad faith reallocated all its Special Capital to one Member; (b) arbitrarily reallocated its Special Capital by drawing lots; or (c) irrationally ignored RemCom's recommendations, for example, by reallocating Special Capital only to researchers and not to fund managers. However, in the light of the evidence, for it to act in that way would be commercially absurd. It is quite clear that Mr Odey and Mr Stewart, thought they had to exercise their role as directors of PSCL responsibly.

(3) On that basis, if PSCL had failed to exercise its discretion in accordance with this principle, it would have been in breach of the 2011 LLP Agreement and the relevant Member would have been entitled to sue for damages.

(4) It is not correct that the Remuneration Policy had no contractual effect noting the following:

(a) Under the 2011 LLP Agreement the members delegated the general management of Odey to ExCo and ExCo had the power to adopt and vary the Remuneration Policy.

(b) The appellants' witnesses appeared to consider that the Remuneration Policy had binding effect and considered it to be important because it was of interest to potential clients.

(c) The Remuneration Policy governed employee bonuses which were presumably provided for under a contract of employment (albeit the awards were discretionary).

(d) The phrase in the Remuneration Policy that: "It is not intended this award process including deferral arrangement should be contractual" is simply an acknowledgement that ExCo/RemCom had enormous

discretion over the Awards; Members had no entitlement to any particular amount but once ExCo/RemCom had exercised their discretion to make an Award the terms of the Remuneration Policy were intended to govern that Award. Moreover, whether the Remuneration Policy had binding effect or not is not to be determined solely by such a statement; it is to be decided in all the circumstances.

308. Mr Chacko said that, in any event, the Remuneration Policy was not something Odey could simply ignore. He considered that is readily apparent from the statement in it that: "The above represents the default position. Any substantial variation will need justification or agreement between the partner concerned and RemCom."

309. Finally, Mr Chacko added that:

(1) It is not HMRC's case that the Members would inevitably *receive* reallocations of Special Capital. HMRC accept that they would not do so if the relevant conditions were not satisfied and that the witnesses believe that that there was a possibility that Odey could call on the Special Capital or that it could be lost due to insolvency. (He said that it is not clear from the terms of the 2011 LLP Agreement that their belief is correct but, in his view, their belief shows that the witnesses thought Odey rather than PSCL was in control of the Special Capital).

(2) The fact that it was possible Members may not *receive* a reallocation subject only to the specified conditions does not detract from HMRC's analysis that the individual shares were *allocated* to the Members in full in the first place (or the other points made above). The important point is that there was no general discretion for PSCL to refuse to make reallocations of Special Capital if all the indicated conditions were satisfied. It was a central feature of the Remuneration Policy and the documents and process under which Awards were made that the only conditions for a reallocation to be made were that the relevant Member remained as such at the relevant time and Odey had sufficient capital for regulatory purposes. Mr Pearey, Mr Odey and Mr Stewart accepted that these were the only conditions for an Award to be fulfilled and that Members understood that to be the case. There was no suggestion that the Members were told that they might receive nothing, even if those conditions were satisfied. Mr Stewart said that PSCL could not have refused to make a reallocation of Special Capital unless it had a good reason to do so. In fact, the scheme operated as Mr Odey described it and, as all those involved expected, as a transparent system of staggered payment. Whenever any sum went to PSCL, it was promptly used to acquire Special Capital in Odey and then reallocated to the relevant Member according to the proposed timetable/vesting schedule, unless, as was also in line with the Remuneration Policy, the Member had left Odey.

(3) In any event, the current state of the *Ramsay* case law enables the tribunal to assess the tax consequences of these arrangements on the basis of an intended series of steps, even if there is no contractual requirement that means each step will occur. In other words, an expectation that a series of steps are going to be taken, can suffice for those steps to be viewed as a preordained series of transactions (see *Trustees of the Morrison 2002 Maintenance Trust v HMRC* [2019] STC 400 (at [53])). In this case, the allocation of the deferred share to PSCL, contribution of the deferred share by PSCL to Odey as Special Capital and the reallocation of Special Capital by PSCL to the relevant Members are all "supposed to follow on from each other, even if there is no right forcing PSCL

to play its role". Moreover, on the authority of *Scottish Provident*, the risk that PSCL could remove a Member's Award, even if they were a member of Odey at the relevant time and there was no risk to Odey's capital, can be ignored because everybody acted on the basis that they would take that risk.

310. Mr Goldberg made the following main points on HMRC's stance on the *Braganza* principle and the effect of the Remuneration Policy:

(1) It is accepted that there are cases where the law implies a term that a discretion must be exercised honestly and rationally but there are limits to the principle as is clear from the comments in *Braganza* at [18]:

(a) The provision in question, under which PSCL had the right, in its sole and absolute discretion to reallocate Special Capital, is simply not a contractual term of the kind described in *Braganza*. When read in the context of the letters which PSCL sent to Members notifying them of their Awards, that provision simply recognises PSCL's absolute ownership of the monies given to it by Odey. It does not render PSCL (or anyone else) subject to any duty as regards the Members in terms of what it decides to do with the monies represented by the Special Capital. Indeed, it is plain that the discretion of PSCL to make an allocation of Special Capital to another member is "no different from a statement by my Uncle Jim…… that he has a discretion to give his money away. It is a statement of the obvious. It has no consequence whatever, so far as the law is concerned. It does not create or destroy rights, liabilities, privileges or obligations; it does not impose a duty to consider making a payment".

(b) As it is put in Lewison, such an implication can be made only where the exercise of the discretion may adversely affect the interests of the other party. In this case, in fact, the interests of Members could only be advantageously affected by an exercise of PSCL's discretion. PSCL did not have discretion to take anything away from Members; it only had discretion to give them something by way of a reallocation of Share Capital. None of the Members could be adversely affected by an exercise of such a discretion. Any disadvantage would fall on PSCL but obviously it would not make any complaint given it was its decision to make any reallocation. The fact is that once the individual shares were allocated to PSCL, PSCL was the only party with a right to those profits. No Member had any right or ability to make PSCL pay him (or anyone else) a certain amount and PSCL was not under any obligation in that regard.

(c) In any event, even if PSCL's discretion to allocate Special Capital is subject to an implied term of the type set out in *Braganza*, that does not mean that in the year of allocation the relevant Members had a "right" to Special Capital of the kind falling within s 850. Such an implied term does not create an immediate entitlement to Special Capital but only imposes a control on how PSCL must exercise its discretion in considering whether to reallocate Special Capital.

(2) The fact that the Remuneration Policy changed does not provide any support for HMRC's argument. If the Policy had created a contractually binding commitment it could not have been changed except with the consent of all the members of Odey but it was simply changed by RemCom.

Conclusions

311. For all the reasons set out below, I have concluded that the appellants are not subject to income tax in the year of allocation on the individual shares or in respect of any sums received in later years on any reallocation of Special Capital.

Summary of correct purposive approach

312. To recap, the decision in *Ramsay* was a key turning point in bringing the approach to interpreting tax legislation into line with the purposive approach adopted in other areas. In what is widely recognised as a succinct and accurate summary, in *Arrowtown* Ribeiro PJ said that the driving principle of the *Ramsay* line of cases is to apply in tax cases "a general rule of statutory construction and an unblinkered approach to the analysis of the facts"; in other words, the "ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically".

313. Most recently in *UBS* Lord Reed emphasised (as cited with approval by Lord Hodge in *Rangers*), that *Ramsay* established not only that a purposive approach must be taken to the construction of tax statutes but also and "equally significantly" that "the analysis of the facts depended on that purposive construction". In other words, "the facts must be analysed in the light of the statutory provision" and "if a fact is of no relevance to the application of the statute", it can be disregarded for that purpose. Lord Wilberforce's composite approach, therefore, provides an illustration of the effect of taking an "unblinkered" and "realistic" view of the facts where, in light of its purpose and context, the statutory provision in question is concerned with the characterisation of the entirety of a transaction which has a commercial unity rather than with the individual steps into which it may be divided.

314. As Lord Nicholls put it in *MacNiven* the "paramount question always is one of interpretation of the particular statutory provision and its application to the facts of the case" in the light of "the need to consider a document or transaction in its proper context, and the need to adopt a purposive approach". As he later said in *BMBF*, the court or tribunal must "determine what transactions the relevant provision is intended to apply to and whether the actual transaction (which might involve considering the overall effect of a number of elements intended to operate together) answers to the statutory description". Lord Nicholls emphasised, therefore, the need to avoid sweeping generalisations about disregarding transactions undertaken for the purpose of tax avoidance. Rather it is essential "to focus carefully upon the particular statutory provision and to identify its requirements" before it can be decided "whether circular payments or elements inserted for the purpose of tax avoidance should be disregarded or treated as irrelevant for the purposes of the statute". There is simply no substitute for a close analysis of what the particular provision requires.

315. As Lord Reed and Lord Hodge recognised in *UBS* and *Rangers* respectively citing the decision in *Scottish Provident*, in applying this purposive approach it is legitimate to look to the effect of the composite scheme as it was intended to operate without regard to the possibility that, contrary to the intention and expectations of the parties, it might not work as planned.

Purpose of s 850

316. The plain purpose underpinning s 850 is to subject each member/partner of an LLP/partnership to income tax on his "share" of its overall trading profits (as computed in accordance with s 849) as determined in accordance with the "profit sharing arrangements", defined as "*the rights of the partners to share in* the profits" of the trade, which subsist during the relevant period of account. In my view, on its natural meaning viewed in the context of the overall regime for taxing partners and members of LLPs, the term "*rights*… to share in the profits" of the partnership/LLP

connotes rights creating an entitlement in a legal sense to those profits vis a vis the other partners/LLP, which rights, therefore, in principle a person could obtain value from or turn to account, whether when the entitlement arises the profits are physically received or not.

317. HMRC said that the focus of s 850 is, as they put it, on a "division", "allocation" or "sharing" of profits which they seemed to suggest involves a partner or member receiving something falling short of an entitlement to profits in the sense set out above. I note that in *Vaines*, which HMRC relied on in support of their view, Henderson LJ referred to passages in the decisions in *MacKinlay* and of the UT in *Vaines* in which the relevant court or UT referred to the need to share, allocate or divide profits amongst the partners/members and Henderson LJ himself also referred to such an allocation (see [208] and [209] above). However:

(1) In *Mackinlay* and the UT's decision in *Vaines*, the courts were simply recognising, that under the three stage process outlined in *MacKinlay* for assessing partners to income tax on trading profits, having determined the overall trading profits of the partnership (at stage one, as currently provided for in s 849), it is then necessary to work out each partner's share of those overall profits by dividing, allocating or sharing those overall profits between them (at stage two, as currently provided for in s 850). The courts were not commenting on precisely how that division, allocation or share is to be effected and determined.

(2) In the Court of Appeal's decision in *Vaines* Henderson LJ did not refer to the passages cited for any purpose other than illustrating the three-stage process as it applies under the current rules. Henderson LJ also simply acknowledged that once the profits of that collective trade have been ascertained, s 850 then provides that Mr Vaines' share of the profit for the relevant period of account is to be determined "in accordance with the firm's profit-sharing arrangements during that period" (see [18] of *Vaines*).

318. It seems to me, therefore, that these comments simply leave open the question of how the term "rights…to a share in" the profits of a partnership/LLP is to be interpreted. Indeed, interpreting "rights" as constituting merely an allocation, division or sharing of profits to my mind simply begs the question of on what basis any such allocation, division or sharing is to be made. Overall, I can see no reason to interpret the term "rights" otherwise than in accordance with its natural meaning as set out above. It is necessary, therefore, to assess what (if any) entitlement the Members had in the year of allocation to the individual shares and/or to sums they received following a reallocation of Special Capital under the profit-sharing arrangements in place during the relevant periods under the 2011 LLP Agreement, as the contractual document governing the relations between the Members, and under any related contractual arrangements.

Contractual arrangements - Allocation of profits under the 2011 LLP Agreement

319. The relevant terms of the 2011 LLP Agreement are set out at [18] to [23] above. Under clause 12.2 of the 2011 LLP Agreement, ExCo was required to allocate all profits for each financial year, after certain prior allocations, between the Members "in such proportions as [ExCo] may, in its sole discretion, determine". When the Remuneration Policy was introduced, ExCo delegated this function to RemCom. Under this provision, therefore, the Members had only an entitlement to require ExCo/RemCom to allocate the profits to them collectively but no individual Member had the right to an allocation of any particular share.

320. However, on the basis of the decision in *Braganza* and related caselaw, it seems to me that there must be an implicit term that ExCo/RemCom had to exercise their discretion in this respect honestly and rationally, for the purpose for which it was conferred. By way of shorthand, I refer to this as an implied term to act in good faith.

Contractual arrangements - Effect of the Remuneration Policy

321. I do not accept that the Remuneration Policy had no contractual effect or role in the contractual arrangements between the Members:

(1) It seems to me that the Remuneration Policy formed part of the contractual arrangements in place between the Members relating to the allocation of profits given that, having received a full explanation from the management of Odey of the intended operation of the Plan as an incentive and retention mechanism, (a) the Members approved the introduction of the Plan in 2011 and, in doing so it seems specifically approved the Remuneration Policy (Lord Roborough thought he had signed it), and (b) signed up to the 2011 LLP Agreement, as amended from the previous version of the document governing their relations, to contain the necessary provisions and mechanics to give effect to the Plan (see [91] to [97] and [102] above). Looking at the arrangements in the round, therefore, in 2011 (a) the Members agreed that the Plan would be introduced and operated by ExCo/RemCom in the future in accordance with the Remuneration Policy, and (b) in return for ExCo/RemCom agreeing to do so, the Members agreed to remain as such on the revised contractual terms.

(2) In any event, in my view, ExCo/RemCom had to take the Remuneration Policy into account in exercising its discretion to allocate profits under clause 12.2 of the 2011 LLP Agreement under the implied term to act in good faith I consider must be applicable to that provision. I find it very difficult to see that, in light of the way the Remuneration Policy was presented to the Members, ExCo/RemCom could be regarded as having complied with that implied term if it did not take account of the Remuneration Policy in doing so (see [91] to [102] above).

322. In my view, on a textual and contextual approach to the construction of the Remuneration Policy, a reasonable person having all the background knowledge which would reasonably have been available to the parties at the time the Plan was approved including (a) the rationale underpinning the Plan (namely, to incentivise and retain key Members), and (b) the relevant terms of the 2011 LLP Agreement which were introduced to give effect to the Remuneration Policy, would interpret the overall effect of the Remuneration Policy as set out below. I base this on the evidence of the information available when the Plan was introduced and approved (see, in particular, [8] to [24] and [91] to [(102]) and the terms of the Remuneration Policy as set out at [16] above):

(1) Under the main body of the provisions, ExCo/RemCom gave an undertaking to members of Odey that they would:

(a) Have regard to the terms of the Remuneration Policy in exercising their discretion to allocate profits to Members under clause 12.2 of the 2011 LLP Agreement.

(b) Accordingly, determine any individual share "awarded" to a Member, (i) as regards Cash Awards, in carrying out the usual profit allocation exercise in or around January of each relevant year by notionally "allocating" an overall notional share of the profits for the previous calendar year to that Member according to the Member's performance in his role for Odey in that period and by applying the

specified threshold and percentages, and (ii) as regards Share Awards, in or around March of that year, by "allocating" a further notional share of any additional profits identified for the period to the end of Odey's financial year again by reference to the Member's performance.

(c) Follow the procedure set out in the Remuneration Policy as regards dealing with any such individual share by arranging (subject to and in accordance with the terms of the 2011 LLP Agreement) for (i) the cash to be invested in Funds managed by Odey, and (ii) a Member to receive the relevant "deferred" sums or for "deferred" share awards to vest on the specified dates over a two or three year period subject to the conditions that (A) the Member remained a member of Odey at the relevant dates, and (B) as was stated a number of times in slightly different ways, payment of deferred cash/vesting of deferred shares was subject to "the firm's ability to make such payments/vesting without limiting the firm's ability to strengthen its capital base" or as it was put later in the document, in all cases, "deferred amounts will only be payable to the extent the firm has sufficient regulatory capital". In my view, a reasonable person, with the background knowledge set out above, would further interpret this to mean that ExCo/RemCom would make recommendations to PSCL to make contributions of Special Capital and to reallocate Special Capital where that is line with and, accordingly, to give effect to the Remuneration Policy.

(2) Having regard to the overall terms of the Remuneration Policy, the statement in the policy that it was not "intended that this award process, including deferral arrangements, should be contractual" is intended to make it plain that (a) ExCo/RemCom retained full discretion to determine the amount of profits to be allocated and individual shares to be awarded to any particular individual, (b) whether a Member who was "awarded" an individual share would receive any funds under the allocation of Special Capital mechanism was subject to the specified conditions, and (c) that PSCL was ultimately to have discretion over the reallocation of Special Capital.

(3) I make the comments in (2) on the basis that, whilst there was no specific mention of PSCL's role in the Plan in the Remuneration Policy, I consider that the Members (and hence a reasonable person interpreting the policy) are to be taken to have had full knowledge of its intended role when the Remuneration Policy was put in place on the basis of the evidence as to the introduction and approval of the Plan (see [8] to [24] and [91] to [102]). The evidence was that the Members were made aware of PSCL's role when the management of Odey explained the Plan to them and they agreed to the relevant terms of the 2011 LLP Agreement which defined the parameters of PSCL's rights, powers and obligations as regards contributing the deferred share as Special Capital, the reallocation Special Capital to any Member and the withdrawal of any Special Capital.

323. In my view, it supports rather than detracts from the above analysis of the meaning of the Remuneration Policy that it was stated in it that whilst RemCom was the "final arbiter in deciding deferral terms (including how deferred funds are invested)", the position set out in the policy "represents the default position" so that "any substantial variation will need justification, or agreement between the partner concerned and [RemCom]":

(1) In agreeing to the introduction of the Remuneration Policy on this basis, the Members agreed, in effect, that in future RemCom could change the policy without obtaining the agreement of all the Members but only where there was "justification" or by agreement with the particular Member affected.

(2) This demonstrates that the Remuneration Policy was intended to subject ExCo/RemCom to a commitment to operate the Remuneration Policy according to its terms albeit that an entitlement to an Award was wholly conditional on certain matters. Indeed, as a matter of commercial common sense, the Remuneration Policy could hardly be expected to achieve its stated aims of incentivisation and retention of key members (and staff) in the absence of any binding commitment for ExCo/RemCom to act in accordance with it.

Contractual arrangements - role of PSCL

324. As recorded in the minutes of the board meetings of the directors of PSCL when it was set up, PSCL was formed as a special purpose vehicle to act as a Member for the sole purpose of using any deferred share allocated to it to make contributions of Special Capital to Odey and to reallocate that capital "upon consideration of recommendations from Odey's Remuneration Committee, which executes Odey's Remuneration Policy" (see [8] to [11] and [13] to [15] above).

325. In order to fulfil this role it "adopted" the Remuneration Policy and, as a Member, under the 2011 LLP Agreement (as set out in detail at [18] to [23] above) it had certain powers under which:

(1) it could make Special Capital contributions with the agreement of ExCo, and

(2) following receipt of a recommendation from ExCo it "may, in his sole and absolute discretion, decide that all or any part of its interest in any Special Capital should be reallocated" to any other Members (on giving notice to ExCo and provided that it could not reallocate any Special Capital within 12 months of the date upon which it was initially contributed unless ExCo had specifically consented to that in writing). I refer to this provision as "**the reallocation discretion**". I note also that PSCL could withdraw Special Capital only with the agreement of ExCo.

326. I note that under the terms of the 2011 LLP Agreement ExCo had sole and absolute discretion over the investment of funds which PSCL contributed to Odey as Special Capital and any resulting income or losses arising were stated to form part of the profits or losses of Odey which were to be allocated amongst the Members in accordance with clause 12. In my view, under the principle set out in *Braganza* and given the interpretation of the Remuneration Policy set out above, this provision was subject to an implied term that ExCo would act in good faith in exercising its discretion to invest the monies contributed as Special Capital which required ExCo, in effect, to take account of the Remuneration Policy in doing so.

327. PSCL, therefore, had no explicit contractual obligation to Odey or any Member as regards what it was to do with the deferred share and any Special Capital it contributed to Odey. However, it was nevertheless constrained in what it could do with the deferred share in the sense that (a) under the 2011 LLP Agreement, it could only use the funds it received to make a Special Capital contribution with the agreement of ExCo and it could only reallocate any such Special Capital if it received a prior recommendation from ExCo to do so, and (b) given its declared specific purpose and that, to further that purpose, it had "adopted" the Remuneration Policy, it was bound to follow that Policy, in the sense that it owed a duty to its shareholder to do so (the special purpose trust formed to own it).

328. Moreover, in my view, under the principles in *Braganza* the provisions in the 2011 LLP Agreement relating to the exercise of PSCL's discretion to make contributions of Special Capital and to reallocate Special Capital are also to be regarded as subject to an implied term to act in good faith. I do not accept that the reasons put forward by Mr Goldberg mean there can be no such term as regards the allocation discretion. I note the following:

(1) Under the allocation discretion, on receiving a recommendation from Odey that it should make a reallocation of Special Capital to a Member, PSCL was charged with making a decision "in its sole and absolute" discretion as to whether or not to do so which could plainly affect (a) individual Members, who expected to receive such a reallocation according to the terms of the Remuneration Policy, (b) Odey, for whose benefit the reallocation mechanism was put in place to enable it to incentivise and retain key Members whilst ensuring that the relevant funds represented by the Special Capital remained available to it where needed, and (c) PSCL itself, as the party which owned the Special Capital albeit that, according to its declared purpose, it held the Special Capital for the furtherance of Odey's business.

(2) Whilst the position is more complicated, therefore, than, for example, where there is a contractual provision for the payment of a discretionary bonus by an employer to an employee, it seems to me that this is exactly the type of circumstance in which an implied term to act in good faith is necessary to give effect to the underlying purpose of the contractual provisions. PSCL could plainly exercise this power to the detriment of one or more of the other parties to the contractual arrangement if, for example, it decided not to make a reallocation of Special Capital to a Member in accordance with a recommendation from RemCom which was in line with the Remuneration Policy thereby defeating the Member's expectations and those of Odey for whose benefit the Plan was put in place.

(3) I cannot see any basis in the caselaw for the view that, as is the effect of the appellants' argument, a term to act in good faith can be implied into a provision only if it gives the decision maker the power expressly to take something away from another party to the contract as opposed to the power to make an award to another party which it may choose not to make. This must surely be a distinction without a difference in considering whether it is necessary to imply a term to act in good faith into a provision in order to prevent a person abusing the unfettered discretion they would otherwise have. I note that the cases relating to discretionary awards of bonuses concern the employer or LLP deciding whether to give additional monies to the employee/member or rather, in effect, to keep those monies; they were not exercising a discretion to take something away as such.

(4) As set out in *Braganza*, an implied term as to the manner in which an otherwise unfettered discretion may be exercised may vary according to the terms of the contract and the context in which the decision-making power is given. The decision in *Faieta* demonstrates that such a term may be implied even where the discretion in question is expressed to be "sole and absolute".

(5) Applying the principles of contractual construction set out in *Wood v Capita*, it seems to me that a reasonable person, with the background information reasonably available to a Member when the 2011 LLP Agreement was entered into (such as the terms of the Remuneration Policy, the rationale for it and PSCL's role as a special purpose company (see, in particular, [8] to [23]

and [91] to [102] above)) would understand the allocation discretion to mean that, on the receipt of a recommendation from ExCo/RemCom that Special Capital should be allocated to a Member, PSCL was obliged at least to consider that recommendation albeit that, ultimately, it was for PSCL alone to decide whether or not to follow that recommendation. Having regard to the overall context in which the allocation discretion was plainly intended to operate, namely, within the framework of the Plan and the Remuneration Policy, the further term which it is necessary to imply into the allocation discretion to give effect to the intended underlying purpose of these contractual provisions is that PSCL was required to act in good faith, honestly and rationally in considering a recommendation from ExCo/RemCom and, in particular, to take account of the Remuneration Policy.

329. I do not, however, accept that the fact that PSCL's discretion to contribute sums as Special Capital and to reallocate Special Capital was subject to these constraints somehow means, as HMRC seemed to suggest, that PSCL did not really have any discretion and/or that, in reality, PSCL was obliged to act in accordance with ExCo's/RemCom's recommendations:

(1) I can see that, as the witnesses recognised, it is highly unlikely that, in practice, PSCL would have cause to exercise its discretion in a manner which was contrary to the recommendations of ExCo/RemCom. The witnesses accepted that the relevant parties were expected to comply with the Remuneration Policy, that it was important to the operation of the Plan that they did so and that, given the way PSCL was set up, its interests were aligned with those of Odey such that it would usually act in accordance with recommendations Odey made (see [150 to [189]).

(2) However, that does not detract from the fact that under the contractual provisions, PSCL plainly could exercise its discretion not to act in accordance with any recommendation without being in breach of the relevant provision provided that in doing so, acting in good faith, honestly and rationally, it properly considered the recommendation in the context of the Remuneration Policy and acted for a good reason such as if ExCo had not itself made the recommendation in accordance with the Remuneration Policy or if, in line with the spirit of the policy, there was some exceptional event concerning Odey's business which ExCo had not taken into account.

Contractual arrangements - documentation under which Awards were made

330. The procedure for making the Awards followed essentially the same process in each relevant year and the terms set out in the documents in which the Awards were made substantially reflect the contractual arrangement set out above (see [24] and [110] to [136] above). I note that throughout the documents there was reference to (a) the Awards as made on a "deferred" basis, (b) the fact that PSCL had discretion over whether to make reallocations of Special Capital to Members, and (c) the fact that any such reallocation was subject to the satisfaction of the conditions set out in the Remuneration Policy. I note, in particular, that:

(1) In all of the letters in the bundles in which Odey notified the Members of Awards for 2012/13 and 2013/14 (there were no letters in the bundles for 2011/12) it was stated that "these deferral arrangements are subject to PSCL's policies and discretion, and PSCL will confirm the details to you".

(2) All of the letters in the bundles from PSCL to Members for the relevant years contained the same wording that PSCL would take RemCom's recommendation into account when exercising its discretion over reallocations

of the Special Capital but that it was not bound by any such recommendation and retained "absolute discretion" over reallocation of the Special Capital and that any recommended reallocations may not be made where the specified conditions were not met other than at the discretion of PSCL.

Conclusion on effect of the contractual arrangements

331. It is plain from the above comments that I do not accept the appellants' position that, as a matter of contract, both ExCo/RemCom and PSCL had absolute unfettered discretion to allocate profits, contribute individual shares as Special Capital, invest the relevant funds and reallocate Special Capital entirely as they chose on the basis that the Members had no contractual form of redress at all should those parties not adhere to the terms of the Remuneration Policy. However, on the analysis of the arrangements set out above:

(1) at the very most, a Member had the contractual right only (a) to require ExCo/RemCom to act in accordance with the Remuneration Policy in exercising their discretionary powers to allocate profits and make "awards" of individual shares, to decide how to invest Special Capital, and to make recommendations to PSCL to give effect to the policy, and (b) to require PSCL to exercise the discretion it had to make a contribution of Special Capital and reallocate Special Capital in good faith, honestly and rationally as further set out above (or perhaps more accurately, a Member had the ability to sue for damages should that not be the case);

(2) the Remuneration Policy made it plain, as did the documents under which Awards were made, that a Member's entitlement to an individual share/reallocation of Special Capital was conditional on future events, some of which were beyond the control of the individual Members (namely, whether Odey/PSCL could decide that the funds were needed for Odey's capital requirement purposes); and

(3) that right does not, therefore, constitute a legal entitlement to the individual shares or any reallocation of Share Capital vis a vis Odey and the other Members which subsisted in the year of allocation and which, in principle, at that time was of value to the Member and could be turned to account as is required for the Member to be taxable in that period on the individual share/any reallocation of Special Capital under the terms of s 850. In other words, the deferral of the Award was not simply a deferral of the ability to receive the relevant funds but of the very "entitlement" on which any right to receive the funds would need to be based.

332. In my view, HMRC's contrary argument that under the documents the relevant Members had an immediate entitlement to an "allocation" of the individual shares in the year of allocation are not supported by the other factors they point to:

(1) Viewed in the overall context in which they appear, it is not apparent to me that the references in the documents to the Awards as involving a "deferral" can be taken to indicate that the Awards gave an immediate entitlement to the individual shares. On the contrary the equally consistent references to the conditionality of the Awards and the discretion of PSCL in making a reallocation of Share Capital indicate that entitlement was not intended to crystallise until a reallocation was actually made. In other words, read in context, any "deferral" was intended to be of the entitlement itself, such that it did not arise until as and when the relevant conditions were satisfied and PSCL exercised its discretion and not simply of the right physically to receive the relevant sums.

(2) HMRC made much of the fact that in the letters for the 2012/13 tax year, in the initial section, Odey notified Members of a single sum comprising, for the relevant period, both an allocation of the profits for immediate receipt and the Member's individual share. They say that plainly shows that the relevant Members obtained an immediate allocation of the individual shares. However, my view is that this is not of itself sufficient to demonstrate that is the case given that (a) it was also stated in the letters that in fact the Awards were conditional and dependent on the discretion of PSCL, and (b) such statements were consistently made in the other relevant documents including, as regards the conditionality of the Awards, in the Remuneration Policy itself.

(3) I note that HMRC attributed the fact that in the letters for 2013/14 Odey notified Members of a separate allocation of profits for immediate receipt and a separately identified individual share to Odey becoming aware of scrutiny of the Plan by HMRC. I accept Mr Pearey's evidence that was not the case.

333. I note that, as recorded in Part A, the witnesses were questioned at some length about their views on how the Plan operated and, in my view, their responses are largely in kilter with the analysis set out above. I accept that they genuinely held the views they expressed. However, it is clear from the caselaw on the correct approach to contractual interpretation that the parties' subjective views on the effect of contractual terms are not relevant to the required exercise and, accordingly, I have not taken them into account in the above analysis.

Conclusion on HMRC's alternative arguments

334. If, as is my view, it is correct that, on a purposive construction of s 850, the term "rights" is to be given the meaning of "entitlement" in a legal sense, there is simply no scope for an argument to succeed that it suffices for s 850 to apply that the Members could be viewed as having some lesser or different form of interest in the individual shares/reallocation of Special Capital, whether by reference to the overall expected and predictable outcome of the transactions or the overall economic effects of the arrangements or otherwise. On that view, as Mr Goldberg said, in applying the correct purposive approach, the only fact of relevance on which it is necessary to focus, are the "rights" to any share of Odey's profits which the Members had of the required nature. An analysis of the existence or lack of any such "rights" is the beginning and the end of the exercise required; either on a realistic view of the facts, there are such "rights" or there are not.

335. In other words, this is a case where, on the correct purposive approach to the particular provision under consideration, like in *MacNiven* or *BMBF*, there is no scope for applying a composite approach. In effect, HMRC's stance would involve applying such a composite approach as though it constitutes a free-standing principle rather than an illustration of purposive construction as the higher courts have repeatedly said is incorrect. As Lord Nicholls stressed in *BMBF*, it is not permissible to strike down transactions on the basis of general propositions that the arrangements involve an element of tax planning and/or that the arrangements were designed to operate together to achieve a particular outcome; what is required is a close scrutiny of the particular provisions in question.

336. I note that I accept that Odey had commercial reasons for the introduction of the Plan is as set out in the extensive evidence in Part A (albeit that reducing the overall tax charge may have been one of the objects as I have considered below). With that context in mind, in any event, the contingencies on which the crystallisation of the Members' entitlement depended (namely, Members remaining as such and Odey's

business needs) can hardly be viewed as uncommercial, artificial or inserted solely for the purposes of avoiding income tax.

337. In my view, on that basis, the remainder of HMRC's points on this issue essentially fall away. I cannot see that the decision in *Rangers* has any material relevance to these appeals given that (a) that case is concerned with a different set of tax provisions, namely, those relating to the taxation of earnings from employment, and (b) for the reasons already given, on a purposive approach the particular provision under consideration here, s 850, is concerned with a Member's entitlement to a share of profits in a legal sense and that test is not met.

Part C – Does s 687 apply?

Law and submissions

338. HMRC argued that the cash sums which the Members received on the reallocation of Special Capital made in years after the year of allocation were taxable as miscellaneous income under s 687 ITTOIA ("**s 687**"). This provides that:

> "(1) Income tax is charged…on income *from any source* that is not charged to income tax under or as a result of any other provision of this Act or any other Act…
>
> (2) Subsection (1) does not apply to annual payments.
>
> (3) Subsection (1) does not apply to income that would be charged to income tax under or as a result of another provision but for an exemption.
>
> (4) The definition of "income" in section 878(1) does not apply for the purposes of this section…." (Emphasis added.)

339. In *Kerrison v HMRC* [2019] UKUT 8 (TCC), [2019] STC 614, at [66] to [68], the UT explained the history of this provision and the related caselaw as follows:

> (1) Prior to the enactment of ITTOIA (a) the residual charge to income tax arose under Schedule D Case VI on any annual profits or gains not falling under any other Case of Schedule D and not charged under Schedules A, E and F (under s 18(3) ICTA).
>
> (2) The enactment of this residual charge to income tax in s 687(1) was part of the Tax Law Rewrite Project and it was intended that the scope of the re-written taxing provisions should be the same as in the predecessor statute.
>
> (3) It follows that the earlier authorities relating to Schedule D Case VI remain relevant to the interpretation of s 687(1).
>
> (4) Those earlier authorities can be summarised in the following propositions, as the UT set out at [68]:
>
>> "The receipt must:
>>
>> (1) have the nature of "annual profits". That simply means that the receipts must be capable of being "calculated in any one year" (per Rowlatt J in *Ryall v Hoare* TC 521 at 526). It does not mean that the income must recur every year (per Viscount Dunedin in *Jones v Leeming* (HMIT) 15 TC 333 at 359) ("*Leeming*");
>>
>> (2) be of an income nature (*Leeming*, ibid);
>>
>> (3) be analogous to some other head of charge under what was previously Schedule D (*Leeming*, ibid) - this is the eiusdem generis principle;
>>
>> (4) be the recipient's income ([*Spritebeam v HMRC* [2015] STC 1222 ("*Spritebeam"*)] at [54]); and
>>
>> (5) involve a sufficient link between the source and the recipient (*Spritebeam* at [54])."

(5) The UT noted, at [69], that it was argued that it was necessary for the receipt to have a "source" for tax purposes and, at [70], that in *Spritebeam* the UT noted, at [55], that the House of Lords in *National Provident Institution v Brown* (1921) 8 TC 57 left open the question whether it is necessary to identify a source before a Case VI liability can arise. They said, however, that s 687(1) expressly refers to "income from any source" which they thought suggested that in order for income to be taxable under Case VI it requires a source. They commented that moreover, "it is hard to see how a receipt which had no source could be euisdem generis with the other heads of charge in what was formerly Schedule D, all of which require a source for the receipt in question". Nonetheless, although they "would be minded to accept that a receipt taxable" under s 687(1) "must have a source", it was not necessary for them to reach a decision on that point.

340. The parties appeared to be agreed that for s 687(1) to apply it is necessary to identify a "source" for the relevant sums. The dispute relates to what constitutes a "source" for this purpose and a "sufficient link" between the source and the recipient and, in particular, whether it is necessary for the relevant sum to be paid under a contractual obligation for this requirement to be satisfied. This, therefore, raised many of the same points on the effect of the documents relating to the Plan as set out above.

341. In HMRC's view:

(1) The source of the sums received by the Members on the reallocation of Special Capital is their continued service as a member of Odey:

(a) The sums are a reward for services rendered and are, therefore, taxable. There is no requirement that the person who, in effect, pays the relevant income (PSCL) must be contractually obliged to reward those services, as long as the reward and services are provided one for the other.

(b) In any event, (i) PSCL was contractually obliged to make the relevant reallocations of Special Capital, and/or (ii) applying the approach in the *Ramsay* line of cases, the Members should be taxed as if PSCL was so obliged.

(2) Further or alternatively:

(a) PSCL's exercise of its discretion to reallocate Special Capital is a sufficient source by analogy with cases on discretionary trusts.

(b) The Members' rights as members of Odey provide a sufficient link to the source of the sums they received.

342. HMRC made the following main points in support of the above arguments:

(1) It is clear from *Spritebeam* (see [70] to [77]) that a source can be either an activity carried on by the taxpayer or some form of property. Moreover, it has been held that payments received in return for "some service rendered by way of action or permission, or both" are taxable as miscellaneous income if they fall short of trade or employment income (see *Ryall v Hoare* 8 TC 521 per Rowlatt J at 525).

(2) The "source" of the relevant sums received by the Members is their continued activity as a member of Odey and/or the provision of their fund management services. The Members were rewarded for their work at Odey in a particular year, in effect, in two ways: (a) by a direct allocation of profit share to them for the current year, and (b) by the reallocation of Special Capital made by PSCL in later periods but which also related to their work in the earlier year. It

is plain that in order to receive any such reallocation, a Member had to continue as a member of Odey during the specified period as accords with the stated rationale for the Remuneration Policy. The Members plainly provided a service to PSCL of remaining as members of Odey in return for PSCL making payments as a reward for their ongoing performance as such, which benefitted it (as another Member) in terms of ensuring the continued profitability of Odey.

(3) The receipts relating to Special Capital are not (a) actually income of Odey because clause 7.1 of the 2011 LLP Agreement states that: "All property held or created by the Partnership which has been paid for by the Partnership or contributed to the Partnership by any Member or has otherwise accrued to the Partnership is owned by the Partnership absolutely and the Members have not individual right to that property (*save as specifically provided herein in relation to Special Capital*) other than through their entitlement to Capital Shares….." (emphasis added), (b) an actual trading receipt because the Members do not individually carry on a trade, nor (c) income from an employment. However, the receipts of Special Capital are clearly analogous to employment income (in effect, as deferred bonuses), and also to the trading income earned by the Members by virtue of the activities of Odey. (Employment income was historically within Case I of Schedule D (see for example s 122 of the Income Tax Act 1952 as originally enacted)). It is clearly in the nexus of things that would normally be taxable as a reward and so is the type of income that the miscellaneous income charge is for.

(4) Further, when a third party supplements someone's income, that is typically taxable as income, whether they make contributions to a trader (see *Falkirk Ice Rink v IRC* [1975] STC 434), an employee (see *Shilton v Wilmshurst* [1991] 1 AC 684) or the beneficiary of a trust (see *Cunard's Trustee v Inland Revenue Commissioners* 27 TC 122 ("*Cunard's Trustee*")). In this case, the relevant sums are additional receipts derived from the Members' trade, even though they are not brought into the trade directly (as in the *Falkirk Ice Rink* case). It cannot make a difference that in this case one Member of Odey, PSCL, in effect tops up the income of other Members to incentivise them to continue in work for Odey, rather than a third party doing so.

(5) For s 687(1) to apply, there is no requirement for there to be an enforceable contract between the person paying the income and the person receiving it, if the income is paid in return for carrying out an activity the taxation of which is ejusdem generis with other forms of taxable income (see *Manduca v Revenue and Customs Comrs* [2015] STC 2002 ("*Manduca*") at [34] and [36]). This supports the observation of the High Court in *Alloway v Phillips* 53 TC 372 at 381H, that there is "no authority for the proposition that money received and retained under a contract void for public policy escapes taxation…"

(6) There is no difficulty in one activity being the source of different kinds of income. This was the case in the examples cited above, and in *Black Nominees v Nicol* [1975] STC 372 (see 375 and 418). Whilst part of the proceeds of the individual partners' exertions have been paid to PSCL, when they come back from PSCL, they are miscellaneous income.

(7) In any event, the Members' receipts did arise under a binding contract (namely, the 2011 LLP Agreement) or at least, in accordance with binding obligations on both PSCL and Odey, which are sufficient to establish the sums are taxable under s 687(1). The reallocations of Special Capital were in no sense

purely voluntary and in fact there was not just one but many binding contractual obligations capable of constituting the source of the individual Members' Special Capital receipts:

(a) In notifying the Members that the conditions for reallocation of Special Capital were their continued membership of Odey and Odey not needing the Special Capital for its capital requirements, PSCL in effect gave an undertaking as to how it would use its discretion.

(b) Further, PSCL's ability to reallocate Special Capital or withdraw it was under the control of ExCo.

(c) Both ExCo and PSCL were required, as a matter of contract law, to use their discretions reasonably and for their proper purpose, as explained above. Given the terms of the Remuneration Policy, this meant that both ExCo and PSCL were obliged respectively to recommend and make reallocations of Special Capital on the "vesting" dates notified to the relevant Members, unless some sufficiently powerful reason not to do so arose.

(8) In any event, the Plan, as designed and carried out, involved a pre-ordained series of transactions which should be taxed on the basis that that was the arrangement, whether or not there were contractual requirements at each stage that ensured PSCL would act as expected. As held by the Court of Appeal in *Trustees of the Morrison 2002 Maintenance Trust v HMRC* [2019] STC 400 per Newey LJ at [53], there is no requirement even that "arrangements" exist for the final stage in a set of pre-planned steps, before the courts are entitled to look at the whole series when addressing its tax treatment. There is certainly no requirement that each participant be contractually bound to play its part.

(9) The circumstances are analogous to those where it has been held that the right of discretionary beneficiaries for a trustee to consider making awards to them may be a source (see *Spritebeam* at [67]). Here, as noted, PSCL was obliged to consider making reallocations as recommended to it and to exercise its discretion properly.

(10) In *Cunard's Trustee* it was held at 132 that when trustees exercise their discretion to make an award to a beneficiary, the beneficiary becomes entitled to the income at that stage and a new source then comes into existence. Similarly, once PSCL exercised its discretion and complied with its obligation to give notice to Odey, the assets credited to the individual Members' Special Capital accounts were held exclusively for the benefit of those Members and they were entitled to withdraw them on five days' notice.

(11) The totality of a Member's contractual and statutory rights and obligations attaching to his membership constitute property (see chapter 8 of Whittaker at [18] and *Reinhard v Ondra* at 589f-590a at [57]) in respect of which the income from reallocations of Special Capital arises. There is plainly a sufficient connection between the income and these rights within the meaning set out by the UT in *Spritebeam* at [84]. The following membership interests under the 2011 LLP Agreement are especially relevant: (a) eligibility for a discretionary profit allocation under (and for an interim profit allocation); (b) eligibility for a reallocation of Special Capital by PSCL; (c) the obligation on a Member which had decided to reallocate Special Capital to give notice of its decision to ExCo; (d) the right of a Member (other than PSCL) to withdraw Special Capital; and (e) the implied right that powers to remove a Member would be exercised in good faith, not irrationally and for a proper purpose.

343. Mr Goldberg made the following main points in support of the appellants' stance that, contrary to HMRC's view, the sums received by Members on the reallocation of Special Capital had no source with a sufficient connection to the Members for the purposes of s 687 and so are not taxable in their hands:

(1) The caselaw shows that a sum cannot have a "source" for the purposes of s 687 unless the person who provides the sum is under a contractual obligation to do so. HMRC rely, in particular, on *Dickinson v Abel* 45 TC 353 ("*Dickinson v Abel*"), *Spritebeam* at [54], [61] and [68], *Kerrison* at [67] and [70], *Scott v Ricketts* 44 TC 303 ("*Scott v Ricketts*") at 316 and 321, and *Manduca* at [34] to [37]. The concept of source in s 687 is intentionally narrow. A wide concept of source would expose all cases of casual receipts to taxation, contrary to the evident intention of Parliament and to good sense. Some careful discrimen of what creates a taxable receipt is necessary, and the law has fastened on obligation as the relevant hallmark.

(2) It is clear that there was no obligation on PSCL (or anyone else) to allocate any of PSCL's Special Capital to a Member; any such allocation was made at the sole and absolute discretion of PSCL without any obligation of any kind. It follows that the sums received by Members on the reallocations had no source for the purposes of s 687 and so are not taxable in their hands. A gratuitous payment which is not contractually enforceable simply cannot be a reward for services.

(3) Mr Goldberg could not see the relevance of clause 7 of the 2011 LLP Agreement. The sums allocated by PSCL are not an addition to trading profits. The sums constitute an already earned partnership profit, which was moved from one Member (PSCL) to another (an individual Member) and cannot be brought into charge a second time as some species of trading income.

(4) This case is not analogous to the circumstances in *Spritebeam* and *Manduca* but rather to those in *Dickinson v Abel* and *Scott v Ricketts*. These cases provide clear authority that if a payment is not made under a binding contract, there could be no liability under Schedule D Case VI and accordingly under s 687(1). No matter how realistic a view of the facts is taken (in the sense set out in *UBS*), an obligation cannot be created where none exists. The statute asks: "Is there an obligation?" and the answer can only be "yes" or "no". Moreover, to the extent that there is any conflict between decisions in the UT such as *Manduca* and *Spritebeam* those decisions cannot override the decision in *Scott v Ricketts*, as the decision of a superior court.

(5) It is manifestly wrong that the existence of an activity is sufficient for a receipt, which arises after the activity has taken place, to be taxable. That is contrary to all of the case law on this topic but particularly *Dickinson v Abel* and *Scott v Ricketts*. The receipt must be from the service which is performed or the thing which is done and that cannot be the case where it is paid without obligation after, and in recognition of, the relevant service/thing done. Nor is it taxable, as HMRC suggest, because some supposed condition has been satisfied, which, in any event, cannot exist where there is no right or entitlement to the relevant sum.

(6) In so far as HMRC claim that the source of the relevant sums is a trading activity, it is self-evident from the terms of s 687 that no charge can be imposed under it on receipts from a trade; such receipts are taxable as trading receipts under the relevant tax legislation or not at all.

(7) It is wrong, as HMRC seek to do, to equate an allocation of Special Capital to a Member with a payment which is a supplement to trading income or to employment income. Members are not employees and, as is clear from the decision in *Vaines*, they do not individually carry on a trade the income of which can be supplemented. It is plain that Odey's profits from its trade are not increased if PSCL gives Special Capital to a Member; that does not have any effect on Odey's trade and it does not come from Odey's trade.

(8) There is no similarity between this case and cases where trustees have a duty to consider the exercise of a discretion. For the reasons already set out in relation to the year of allocation position, PSCL was not under any obligation to make or even to consider making a payment or transfer of Special Capital to another member; the case is not akin to cases like *Cunard's Trustee* where the trustee was under a duty to consider making a payment so that, when it was paid, it was paid under an obligation and, in any event, that case is about Schedule D Case III (annual payments) and says nothing about the claim made by HMRC in this case.

(9) It is equally wrong to say that the Members have rights, which are a source for the allocations of Special Capital made by PSCL to them. There is no right to the transfers of Special Capital made by PSCL (and if there were, the receipts from them would clearly be capital not income, on the authority of *Scott v Ricketts*). The correct analysis, as is made absolutely clear by clause 10.12B of the LLP agreement, is that there was no obligation on anyone to allocate any part of PSCL's Special Capital to another Member. The commercial expectation that a payment will be made is not the equivalent of an obligation.

(10) Nor can it make any difference that some Members received more than one allocation of Special Capital (see *Stedeford v Beloe* [1932] AC 388 ("*Stedeford v Beloe*").

Caselaw

Spritebeam and Cunard's Trustee

344. I have started by setting out the decision in *Spritebeam* as the UT considered a number of the relevant older authorities in that case. *Spritebeam* concerned a corporation tax avoidance scheme whereby a company lent money to a group company on terms that no interest was payable while the loan was outstanding, but instead irredeemable preference shares equal in value to a commercial rate of interest were issued to a different group company. The issue of relevance was whether, as HMRC argued, the recipient of the shares was taxable on the interest in the form of shares, or alternatively, on the value of the shares as an amount analogous to interest, under Schedule D Case VI.

345. At [55] the UT noted that they were acting on the assumption that a source had to be identified for schedule D Case VI to apply and, at [54], summarised the appellant's arguments as follows:

> "54. Mr Prosser's primary argument was that it was not enough that a person receives something for tax to be chargeable. That argument, as we see it, breaks down into four elements: (i) the receipt must have the character of income (a word we use as an umbrella term to include the profits or gains to which case VI refers); (ii) *it must be the recipient's income*; (iii) it must have a source; and (iv) *there must be a sufficient link between the source and the recipient*. Mr Ghosh did not dispute those propositions as propositions; the

substance of the disagreement between the parties centres on elements (ii) and (iv) ...” (Emphasis added.)

346. The dispute centred on whether the requirements set out in (ii) and (iv) of this passage were met.

Spritebeam – requirement (ii)

347. In considering whether the requirement set out at [54(ii)] of the decision in *Spritebeam* was fulfilled, the UT referred, at [57] to [59], to two cases where it was held that sums were not taxable under Schedule D Case VI:

(1) In *Watkins v Commissioners of Inland Revenue* [1939] 2 KB 420 it was held that payments which a husband made, under an undertaking to the court, to make up a shortfall in the income of his mentally-ill wife to meet fees of a mental institution in which she resided was not income in her hands. He sought a tax deduction for the payments, conceding in the High Court that they were not voluntary. At [57], the UT cited the following comments of Lawrence J at 424-5:

> “the crucial question ... is: does the payment to be made by the husband in the present case constitute income in the wife’s hands?... the wife, although she has the benefit of the expenditure, is not entitled to the money as such. She does not choose the institution and has no say in the application of the money. These considerations lead me to the conclusion that the sum payable by the husband is an expenditure of his income and does not constitute the income of the wife.”

(2) The UT commented, at [58], that while the wife indirectly benefited from the husband’s expenditure she did not in substance receive the money in such a manner that it could be regarded as her income. They noted that the appellant argued that the recipient of the shares was in a similar position to the wife in that (a) neither had a right to receive the payment/issue of shares, even though there was an obligation on the borrower, or the husband in that case, to pay/issue the shares and (b) neither had a means of enforcing payment/the issue of the shares; they amounted to a gift in the recipient’s hands.

(3) In *Stedeford v Beloe*, it was held that an annual pension paid by the warden and council of Bradfield College, acting under powers conferred on them by the college statutes, to the former headmaster of the college was not taxable income in his hands. The statutes empowered them to apply certain moneys to such purposes as, in their absolute discretion, they may deem to be for the benefit of the college including the payment of any pension to any person who had held the office of headmaster but laid upon them no obligation to do so. At [58] and [59], the UT cited the following comments of Viscount Dunedin (at 390) and Lord Warrington (at 391):

> “Now it must be a real profit under Schedule D, and it has been held again and again that a mere voluntary gift is not such a profit because it is not, in the true sense of the word, income. It is merely a casual payment which depends upon somebody else’s good will….[Viscount Dunedin]
>
> This question can, in my opinion, be answered in only one way. Here each payment is wholly voluntary. The case is only an instance of a succession of voluntary payments, each of which is voluntary and none of which need necessarily be continued.” [Lord Warrington]

348. The UT continued, at [60], to note that they were referred to other cases in which a “purely voluntary and also non-enforceable payment” was still regarded as taxable income, such as *Calvert (Inspector of Taxes) v Wainwright* [1947] KB 526 (as

regards a tip to a taxi driver) and the *Falkirk Ice Rink* case (as regards a voluntary contribution to trading profits to keep the taxpayer's ice rink open for curling). They noted that it was argued these cases were not relevant because the payments under consideration in *Spritebeam* had been made and received in the context of the taxpayer's trade, and the absence of a legal right to enforce them was irrelevant.

349. At [61] to [67] the UT set out details of a number of cases they were referred to involving trustees:

(1) In *Drummond v Collins (Inspector of Taxes)* [1915] AC 1011 ("*Drummond*"), as Lord Loreburn explained, an American gentleman left by his will a large sum of money to trustees upon trusts which "tied up his property with a view to its accumulation for a long time, and created a somewhat complicated series of interests". The will authorised and indeed required the trustees in America to exercise their discretion as to providing money for the maintenance of the testator's grandchildren, who were then minors. In pursuance of this authority the trustees exercised their discretion and remitted to the taxpayer, the mother of these children who resided in England, certain sums of money for their maintenance. The court rejected the argument that they were non-taxable merely voluntary payments and held that they were taxable in the mother's hands.

(2) At [61], the UT noted that, in *Drummond*, the beneficiaries had the right to require the trustees to consider the exercise of the discretion but they did not have the right to require the trustees to exercise that discretion in their favour, nor did they have anything more than a contingent right to a share in the capital of the fund. Yet that limited right was enough of an interest in the trust fund to render the payments the taxable income of the recipient. The UT added, at [62], that it could be argued that when the payment was made to the mother the right arose because at that moment it became non-discretionary (the discretion was exercised in favour of a relevant child) and was impressed with a trust in the children's favour. Thus, at that moment they became legal and enforceable rights.

(3) The UT concluded, at [63], that it did not seem to them that there has to be an enforceable legal right in the recipient to receive a payment before it can form part of his income. They said that whilst it is true that in *Drummond* the beneficiaries did have an enforceable right, the members of the House of Lords did not express themselves in those terms. They noted that Earl Loreburn put it in this way (at p 539):

> "I do not assent to the proposition that a voluntary payment can never be charged, but it is enough to say that these were not voluntary payments in any relevant sense. They were payments made in fulfilment of a testamentary disposition for the benefit of the children in the exercise of a discretion conferred by the will. They were the children's income, in fact."

(4) The UT noted, at [64], that Lord Parker, too, spoke in the language of interests and entitlements rather than enforceable legal rights and:

> "The word entitlement can be limited to the right to receive rather than the right to enforce payment. In Lord Parker's view it did not matter that the mother was not a beneficiary and could not control the property, although control is often the badge of enforceability of a legal right."

(5) The UT did not set this out, but to explain further Lord Parker said, at page 539 to 540, that the monies transmitted from America were "certainly profits and gains arising from property" and the property from which they arose was, "equally clearly, a foreign possession within the meaning of Case VI". Lord Parker understood it was argued that they were not taxable on the basis that Case V applies only to profits or gains from foreign possessions when these possessions belong to the person sought to be assessed, and that this property did not in the present case belong either to the infants or to their mother as their guardian. In his opinion:

> "it is enough for Case 5 to apply that the person to be assessed has such an interest in the property as to entitle him to the profits or gains in question. The infants had in my opinion such an interest. Though they might be incapable, because of their age, of giving a receipt for the money, it is in my opinion none the less clear that the money in question was as soon as the Trustees had exercised their discretionary trust held in trust for these infants as beneficiaries……"

(6) At [65], the UT noted that both *Drummond* and *Stedeford v Beloe* were referred to in *Lindus & Hortin v IRC* (1933) 17 TC 442, where it was contended that payments of capital to a beneficiary under a will (the testator's daughter) were to be regarded as voluntary payments. However, Finlay J appeared to have no difficulty in holding that such a payment was taxable as income in the hands of the daughter.

(7) At [66], they referred to *Cunard's Trustee*. In that case under the terms of a will there was power to supplement income with capital to ensure the comfort and maintenance of the beneficiary (the sister of the deceased). The Court of Appeal held that the payments were income of the recipient which were taxable as annual payments (under schedule D case III). Having carefully considered the terms of the will, Lord Greene MR said the following at 132:

> "The payments, therefore, in my opinion, were properly made and at the moment of payment became income of the recipient…...[*her] title to the income arose when the trustees exercised their discretion in her favour and not before. At that moment a new source of income came into existence*. The payments came to [the recipient] under the express terms of the will…." (Emphasis added.)

(8) At [67] the UT said that at first blush the passage highlighted above supports the argument that the taxpayer must have an enforceable right to the relevant property. They noted, however, that Lord Greene went on to say the following (at pages 133 to 134):

> "It was suggested, however, that the Rule does not extend to mere voluntary payments. But the payments here were of a totally different character. They were not voluntary in any relevant sense, but were made in the exercise of a discretion conferred by the will out of a fund provided for the purpose by the testatrix. It is true, of course, that the trustees had an absolute discretion whether to make a payment or not. But the question whether they should do so is one which they were bound to take into their consideration. They could not refuse to consider whether the income of the estate was sufficient to give [the beneficiary] the required degree of comfort and the fact that, after examining that matter, they might come to the conclusion that it was sufficient, does not, in my opinion, give to a payment, if and when made, the character of a voluntary payment in any relevant sense."

(9) The UT did not cite the remainder of the passage but it continues as follows:

> "The money when received by [the beneficiary, was received by her through the joint operation of the will and the exercise of their discretion by the trustees. This very question was considered …in the case of *Lindus & Hortin*…..There as here the trustees had a discretion to supplement the income of a tenant for life out of capital. This discretion was absolute and it was argued there, as here, that the payments were not income because there was a discretion on the part of the trustees, and there was no right in the beneficiary to claim them. I am in agreement with the decision of Finlay J on this point…."

350. At [68] the conclusion the UT drew from the above authorities was that:

> "*it is immaterial that the recipient cannot enforce payment; what matters is whether there is an obligation on the payer to pay*. Thus in *Stedeford* there was no obligation on the governors to make any payment; they could have refrained at any time from making further payments, and neither the former headmaster nor anyone else could have compelled them to continue. By contrast, in the trustee cases the beneficiaries, individually, could not enforce the payment of any particular sum to themselves; *but the trustees were under an enforceable obligation to exercise their discretion and make a payment to one or more of the beneficiaries as circumstances required*. In *Drummond*, for example, the payments were not voluntary payments in any relevant sense because the payments were made on the basis of the trustees' duties arising under the testamentary trust. In the present case, the right to payment may not have been enforceable by the Share Recipient but it was not voluntary either; the Borrower was under a contractual duty to the Lender to allot and issue shares to the Share Recipient. Thus we conclude, in relation to issue (ii), that the shares were income in the Share Recipient's hands." (Emphasis added.)

Spritebeam – requirement (iv)

351. At [69], the UT moved on to considering the requirement they had set out at [54(iv)] (see [345] above). They noted that there was no argument that the obligation imposed on the borrower to issue the shares did not represent a source. Rather the argument was that there was no, or no sufficient, link between that source and the recipient of the shares. They said that at first sight this seemed to be the argument set out above about the distinction to be drawn between voluntary and non-voluntary payments put in another way, but on closer analysis that was not the case. They explained further, at [70] to [73], that:

(1) It was argued that a source is limited to a kind of property or a kind of activity by reference to:

(a) *CIR Lever Bros & Unilever Limited* [1946] 13 SATC 1 where it was stated, at [16], that:

> "...a source of income is either (a) some personal activity of the taxpayer, or (b) some property over which he has rights, or (c) a combination of both".

(b) The observation of Viscount Haldane in *National Provident Institution v Brown* at p 84:

> "There was imposed under the Schedules no collection of taxes distinct from each other, but simply one tax [income tax] with standards for assessment which varied according to the sources from which the taxable income was derived. [The Income Tax

Act 1853] ... was an Act to impose income tax on annual profits or gains arising from property or from some occupation", and

(c) The schedules themselves.

(2) It was further submitted that the property-activity categorisation determined the necessary connection between the taxpayer and the source. If an activity then the taxpayer must carry it on, and if property, then the taxpayer must have the legal right to enforce it. In *Spritebeam*, the argument was that the source was property in the form of the shares but the recipient of the shares had no right to compel enforcement of an issue of shares (see [73]).

352. The UT noted, at [80], that the rule is merely that the taxpayer cannot be taxed on receipts if he does not have the necessary connection with the source. Once the connection has been identified, it is necessary to look behind the receipts in the tax year in question to see if the source of income continues or has ceased. But that necessity says nothing about the nature of the connection which must be demonstrated.

353. They explained, at [81], that HMRC took the view that it was the recipient of the share's status as a counterparty to an absolute obligation of the borrower to pay interest on the loan (an obligation satisfied by the issue of the shares) that was relevant as demonstrated by a comparison between *Drummond* and *Stedeford v Beloe* as follows:

> "In the former, the will which permitted the payment to be made also limited the class of persons who would be entitled to any payment made pursuant to it to the named beneficiaries. The beneficiaries, therefore, by virtue of that status, were entitled to the payment, had a sufficient connection to the source, and were liable to tax on the income. By contrast, in the latter, the payment was made pursuant to the college statutes, under which only the College was a beneficiary. It could therefore not be said that the former headmaster was entitled to the payment by reference to that instrument. He had no identifiable source of the income beyond the College's generosity, but a voluntary payment of that kind was not taxable."

354. The UT continued, at [82], to explain further that it was argued by HMRC that:

> "the source of the Share Recipient's income was the Loan Agreement, in which it was the named beneficiary. It was entitled to receive the shares, by reason of its being so named, even if it did not have the capacity to enforce that entitlement itself: it was in a similar position to that of the beneficiaries in *Drummond v Collins* but not in an analogous position to that of the former headmaster. Although, in *Cunard's Trustee*, the court was addressing the question whether the payments were or were not voluntary, what Lord Greene said (see para 67 above) was equally relevant to the question whether there was a connection between the recipient and a source. The source in that case was "the joint operation of the will and the exercise of their discretion by the trustees." Once it was accepted (as the taxpayers had done in their skeleton argument) that the shares were derived from the Loan Agreement there was no need to enquire further: the source of the shares was identified, and sufficient."

355. They said, at [83], that they preferred HMRC's arguments. Although they accepted that the categories of property and activities demonstrate what constitutes a necessary connection, they did not consider that the test for necessary connection is limited to them. In their view, "possession" of a connection is not to be equated with ownership; the beneficiaries in *Drummond* and *Cunard's Trustee* did not own the fund from which their income was derived, but they were nevertheless found to

"possess" (if that is the right word) a sufficient connection to the source. They concluded rather at [84] and [85]:

> "*The required connection between taxpayer and source need not be limited to legal rights but can include the situation where the payment is made pursuant to any legal duty owed by the payer*. That proposition is consistent with what was said by Lord Greene in the passage we have set out at para 67 above, in which the focus was on the payer's obligation to the recipient, and not on the recipient's ability to enforce it.
>
> In our view Mr Prosser's approach in saying that the Share Recipient must have a legal right to have the shares issued and allotted to it is, as we have said, too narrow. The Borrower had an absolute and unconditional obligation to allot and issue the shares to the Share Recipient, that obligation was in no sense voluntary and we consider this obligation to be a sufficient legal basis to constitute the necessary connection between the Share Recipient and the Loan Agreement. The fact that the Borrower might have failed (although in fact it did not) to issue the shares, thus breaching its obligation, does not give the issue of the shares the character of a voluntary payment."

Manduca

356. In *Manduca* the UT held that a payment of £310,000 received by the appellant from another party, Dexia, under the terms of an out of court settlement of litigation was taxable under schedule D Case VI. The taxpayer had brought proceedings in the High Court to recover what he claimed was a form of bonus payment due to him from Dexia in the sense that it was not a bonus in the usual employment sense but a payment of consideration for securing, within a particular timeframe, the successful transfer to Dexia of his business of running a fund. Dexia defended the action on the basis that the bonus was a performance related bonus that had not been earned. It was common ground that the correct tax treatment of the settlement sum is the same as the correct treatment of the bonus if it had been paid by Dexia to the appellant.

357. The UT noted, a [27], that it was argued that the bonus was not a payment of the same kind as those listed in the other Cases of Schedule D relying on the decision in *Leeming v Jones* (H M Inspector of Taxes) (1930) 15 TC 333. In outline, in that case, the taxpayer was held not to be taxable under schedule D Case VI on a sum he received as a member of a syndicate which had sold interests in two rubber estates. The UT recorded, at [27] and [28], that having set out the principles referred to above, Viscount Dunedin held that in the case of an isolated purchase and sale, the receipt could only be income under schedule D Case VI if the transaction was in the nature of a trade but the Commissioners had found that was not the case.

358. The UT set out details, at [29], of the case of *Brocklesby v Merricks (HM Inspector of Taxes)* (1934) 18 TC 576 (CA). In that case:

(1) The taxpayer was an architect and surveyor who was assessed to tax under schedule D Case VI on certain income arising in the following circumstances:

(a) The taxpayer arranged a meeting between (i) a person, P, who at a social occasion told the taxpayer that he was anxious sell an estate he owned and (ii) a client of the taxpayer's, D, who later bought the estate.

(b) D did not agree to make any payment to the taxpayer at the time of the meeting or at the time of the sale.

(c) A few weeks after the sale, the taxpayer and D agreed that the taxpayer would help D dispose of the estate and would also carry out all architect and surveyor work involved without charge in return for one third of the profits on the sale.

(d) The taxpayer's evidence was that he took no part in the acquisition and resale of the estate and carried out no work as architect or surveyor.

(2) Finlay J noted that the taxpayer undoubtedly had a contractual right to sue for the one third profit. He said that the money would not be taxable if it were an ex gratia payment made after the rendering without charge of the introduction effected by the taxpayer to P. However, he held that it was a payment for services even though the taxpayer had done very little because the onward sale had been achieved without much difficulty and without the need for much involvement of the taxpayer. He acknowledged that the very favourable price for the services rendered was the result of the previous introduction that the taxpayer had made without charge but said (page 583):

> "….the circumstance that, so to speak, an inducement for the favourable terms which he there got was the fact that he had rendered an important service to them, does not prevent it, to my mind, from being a contract in respect of services rendered. After all one has to consider what he was paid for. He was paid this sum, because he had an enforceable right to get it, and that enforceable right was based on this, that he had got a contract in respect of which, for certain services to be rendered by him specified in the contact, he was to be entitled to remuneration."

(3) As the UT, therefore, noted at [30], the Judge, therefore, "upheld the assessment holding that it was a case in which, induced very probably by the voluntary service, the parties chose to enter into a contact for remuneration in respect of services".

359. At [31], the UT set out details of a case falling on the other side of the line: *Bradbury (HM Inspector of Taxes) v Arnold* (1957) 37 TC 14. In that case:

(1) The taxpayer had a controlling interest in a company which arranged ice shows and reviews. The company proposed to put on an ice show in a theatre in London. Major Martineau was a keen ice skater and wanted to be involved in the production.

(2) The company had assets and activities other than ice shows so it was not practicable to transfer part of the interest in the company to the taxpayer.

(3) It was agreed that Major Martineau would pay the taxpayer £9,000 in return for a half share in the profits of the show.

(4) The Inland Revenue assessed the sum as taxable under Case VI but the Commissioners upheld the taxpayer's contention that the £9000 was in fact paid for a right to future profits of the ice show and was therefore a capital transaction.

(5) Upjohn J noted that the Commissioners had accepted that any services of introduction rendered by him to Major Martineau were only trifling and that the payment of the £9000 would not be attributable to such services. This was not challenged by the Crown on appeal. Upjohn J said (page 669):

> "There is no doubt that a contact for services may, and clearly does, form a matter for assessment under Case VI of Schedule D, and not the less so that the services to be rendered are trivial or that they are to be rendered once and for all so that the remuneration may be regarded as a casual profit arising out of a single and isolated transaction."

360. At [32] the UT said that the question in *Bradbury* was whether the £9,000 was remuneration for the taxpayer having introduced Major Martineau to the company and

for procuring the company to enter into the agreement to share the profits of the show and explained that the Judge:

> "emphasised that the transaction stood entirely on the documents and his decision was particular to the facts of the case. He asked "can you really say as a matter of business common sense that in and by that transaction, [the taxpayer] undertook to perform services?" He did not think you could and he therefore held that the payment was not income."

361. At [33] the UT also considered *Versteegh Ltd and others v HMRC* [2013] UKFTT 642 (TC) where the tribunal rejected the submission that the issue of shares to the share recipient in a complex transaction was income chargeable under Case VI. They held that the role of the share recipient had been passive and a failure to do something, for example, disclaim the shares could not be regarded as having any similarity to a trading or professional activity (see [135]).

362. The UT noted, at [34], that HMRC's counsel argued as follows:

> "He said first that the principles derived from the case law showed that there was no need to consider what the taxpayer actually did in performance of the agreement under which the payment was made. It was enough that the payment was made under a binding agreement (rather than as a gratuity) and that the agreement bound the taxpayer to provide some kind of services. Alternatively, if it was necessary to look at what Mr Manduca did in return for the Bonus, then there was sufficient evidence to show that he did in fact perform services that fell within Case VI."

363. At [35] the UT concluded that the bonus was remuneration for services provided to Dexia by Mr Manduca and "those services fall firmly within Case VI" and accepted HMRC's submission that:

> "*Brocklesby v Merricks* and *Bradbury* show that once it is established that the payment was an income receipt rather than a capital receipt and that it was paid pursuant to a binding contract in return for some kind of service then there is no need to go further to inquire into the extent of the services in fact provided."

364. The UT continued, at [36], that further it was clear that the bonus was to pay for services which are akin to profits and gains that fall within the other Cases. The UT referred to an extract from Whiteman and Sherry on Income Tax (paragraphs 12-001 to 12-041) where, after discussing *Leeming v Jones*, the authors give as examples of income which is not ejusdem generis, betting winnings, gifts and receipts by finding. The UT noted that the taxpayer's counsel argued that what Mr Manduca did was so limited that the supposed services were akin to the passive receipt of shares in *Versteegh* or the introduction of Major Martineau to the ice show promoter in *Bradbury.* At [37], the UT said that characterisation of the facts was not correct noting, in particular, at [38], that the taxpayer and his business partner were the key people on whose reputation the continued confidence of employees and investors rested and it was important for Dexia to obtain their commitment to the transfer of the business, before the formal employment relationship started:

> "The role they would play in facilitating the transfer was to cooperate and so conduct themselves as to ensure that staff and investors stayed on board and that such a drift of money and talent did not occur in that interim period. I do not see any difficulty in describing that as a service provided by Mr Manduca or in holding that that service is ejusdem generis with the services listed in the other Cases in Schedule D."

365. In *Manduca*, therefore, the UT accepted that, once it was established that the payment in question was an income receipt rather than a capital receipt and that it was

paid pursuant to a binding contract in return for some kind of service, then there was no need to go further to inquire into the extent of the services in fact provided in order to establish that s 687 applied. I do not take from that, as the appellants seemed to suggest, that the UT was laying down a rule that s 687 cannot apply as regards receipts relating to services unless there is such a binding contract whatever the circumstances.

Dickinson v Abel and Scott v Ricketts

366. In *Dickinson v Abel*, in summary:

(1) The taxpayer was a farmer who, through introductions from M and M's father, received offers from companies to purchase a farm which belonged to his wife's late grandfather's estate in which neither he nor his wife had an interest. He sent the offer to the trustee of the estate, a bank.

(2) Shortly after M introduced him to a representative of the companies who offered £100,000 for the farm. The farmer said that the offer should be made to the bank and asked what was in it for him. The representative said the gravel companies would pay him £10,000 if they bought the property for £100,000.

(3) The farmer's evidence, which was accepted, was that he did not know what was in the representative's mind and he did not often speak to the bank.

(4) The following day he told the bank the offer was on the way and, when asked to comment, said that he personally would accept it but he did not reveal the promise of the £10,000. The bank accepted the offer and the farmer received the £10.

(5) The High Court rejected the Inland Revenue's position that the £10,000 was taxable under Schedule D Case VI.

367. As HMRC pointed out, it is notable that it was common ground in this case that the £10,000 was taxable only if it was paid in pursuance of an enforceable contract. Given the agreed scope of the issue, the focus was necessarily on whether or not there was an enforceable contract between the farmer and the representative as regards the provision of his services for a fee. The court did not consider, therefore, whether the parties' common view was in fact correct. On that basis, I consider that this case does not add to the debate on whether a payment for services must be paid under a binding enforceable contract to be taxable under s 687.

368. In *Scott v Ricketts*:

(1) The taxpayer was an estate agent, who from 1955 onwards acted for a retailing society in negotiations with the local authority about compensation for the acquisition of a bomb site, the C site, and the terms for a building lease from the local authority of a fresh site, the M site.

(2) During the negotiations, the taxpayer offered the society a site owned by another client which suited the association better. Since the society wished to retain its rights over the M site for the purpose of obtaining compensation for the C site, and the taxpayer was interested in acquiring the M site on his own account (although on the terms then available it had no premium value) they reached an understanding that the society would, in due course, endeavour to assign its rights in the M site to him. An agreement in writing to that effect was drafted but never executed.

(3) On becoming aware of the society's interest in the alternative site, the local authority broke off the negotiations and eventually the society instituted an action for specific performance.

(4) At that stage, R Limited, a development company which had already made an abortive approach regarding the M site, proposed through the taxpayer a settlement on the terms that it would acquire that site and would make up the compensation for the C site to a specified sum. The society indicated to R Limited that the taxpayer's agreement to the proposals in his private capacity should be obtained because of the understanding it had with him.

(5) R Limited accordingly offered, in consideration of the taxpayer withdrawing any claim to participate in the development of the M site, to pay the taxpayer personally £39,000, when the proposals went through and duly paid him that sum.

(6) The Court of Appeal rejected HMRC's argument that the sum was a reward for services in the general capacity which was taxable under schedule D case VI.

369. In the Court of Appeal, Lord Denning MR (as he then was) commented at page 320 that the reason for the payment appeared to be that the parties thought that the taxpayer had some sort of claim to an interest in the M site because at one stage in the negotiations it was proposed he should take over the site either on his own or jointly with R Limited but in the end R Limited took the site over themselves and the taxpayer was left with no interest in it. He said that his ensuing claim "may have been a business claim, a moral claim or a legal claim. But whatever it was, he was bought out for £39,000". He continued, at page 321, that R Limited made the payment under the terms of a letter which the taxpayer signed in which he agreed to withdraw any claim. So he withdrew any claim he might have had to participate in this proposed investment in return for the sum of £39,000. He then said the following, also at page 321:

> "The one point now is whether this £39,000 is chargeable under Case VI. That Case is a "sweeping-up" provision. It catches "annual profits or gains" which have not been caught by the other provisions. It is difficult to construe and we have to go by the decided cases…..In *Ryall v Hoare*, Mr Justice Rowlatt staked out the guidelines and there had been other cases following it ...... Some things are clear. 'Annual profits' does not mean profits which are made year by year. It is satisfied by profits made in one year only. "Profits or gains" includes remuneration for work done, services rendered or facilities provided. They do not include gratuitous payments, which are given for nothing in return, nor do they include profits in the nature of capital gains…."

370. Lord Denning MR continued, at page 321, that the crux of the case was that the taxpayer had no legal ground to be paid anything. All he had was a moral claim or nuisance value. He noted that in the High Court the Judge had concluded that because the payment "was "dressed up" as a contract – to use the Judge's own words" it was taxable under Schedule Case VI. Lord Denning did not agree. He noted that (a) where a person gives up a good legal claim in return for money, that is not a sum within Case VI; for tax purposes that is the sale of an asset for a price, (b) a payment made for an unfounded claim, which strictly is not an asset, has the same quality for tax purposes as if the claim were well founded, and (c) even a sum paid in respect of claim which is only a moral claim with no legal basis has the same quality for tax purposes. In his view, in all of those cases the sum is not an annual profit or gain within Case VI. He concluded, at page 321 to 322, that:

> "The Judge seems to have thought that, as the payment was made under contract, that was enough to bring it within Case VI. I cannot agree with him.

It must be a contract for services or facilities provided, or something of that kind. The present case is rather like *Leeming v Jones*…If the sum was taxable at all, it was taxable as part of the profits of [the taxpayer's] trade or profession. Once that is negatived, it becomes simply a sum received in compromise of a disputed claim; whether legal or moral makes no difference."

371. Davies LJ and Russell LJ essentially agreed that, whist it was highly doubtful that the taxpayer had any kind of valid legally enforceable claim, the sum was plainly paid to buy out that claim and did not have the quality of income.

372. Davies LJ noted, at page 323, that the payment was made under a contract in return for the taxpayer giving up any rights he may have. He said there was some suggestion that it could be said that the taxpayer's undertaking in the contract to sign any necessary documents to implement the agreement might be the consideration for the payment and that therefore in some way the payment was a payment for services to be rendered or things to be done in the future. In his view, the signing of any such document would be in exactly the same position as the execution of a conveyance on the sale of a piece of land. He concluded that this was not in any form an annual receipt of a profit or gain but rather "the buying out" of the taxpayer's claim.

373. Russell LJ noted, at page 324, that if the taxpayer's claim had been a legal claim:

> "it is plain that the £39,000 would be outside Case VI: it would be payment received by way of realisation of an asset, and as such would lack the quality of income for tax purposes which is necessary to come within annual profits or gains under that head. The Crown says that this cannot apply to a case where there is no legal right."

374. He noted that the question was whether the receipt had the quality of income and concluded that:

> "…for this purpose there is a true analogy between a sum received on the sale of an asset, or a sum received in settlement of a legally enforceable claim (or, I may add, one arguable legally enforceable), and a sum received, as here, in payment for the withdrawal of a moral or business-world claim, a spes acquisitions such as this. By such analogy I think the sum paid is not shown to have the quality of income necessary to attract tax, and is, therefore not within Case VI."

375. I note that Mr Goldberg placed much emphasis on this case. I do not agree, however, that it provides clear authority that for a payment for services to fall within Schedule D Case VI/s 687, it must be made under a binding contract under which payment is enforceable by the recipient:

(1) Each of Lord Denning, Davies LJ and Russell LJ concluded that the relevant payment was in the nature of a capital sum paid for the withdrawal of "buying out" of a claim (albeit there was no legal basis for the claim) rather than a payment with the quality of income. In other words, it was not a payment for the provisions of any services as the Crown had argued.

(2) Lord Denning rejected the proposition that the fact that the payment was made under a contract was sufficient to render it taxable under Case VI. His following comment that: "*It must be a contract for services* or facilities provided, or something of that kind" (emphasis added) has to be read in that context. He was simply saying that, for Case VI to apply in the circumstances of that case, the contract in question, which, in effect, was argued to be the source of the relevant payment, would have had to be for the provision of services and not one whereby a payment was made for the withdrawal of a

claim. He was not saying that, in all circumstances, the provision of services (or something akin to a service) can only fall within Case VI where provided under a binding contract.

(3) Similarly, I do not think that Davies LJ can be viewed as making any such suggestion in his comments at page 323, in effect, that the contract in question was for a payment to be made in return for the withdrawal of a doubtful claim and not for services to be rendered.

Conclusion

376. I have concluded that the Members are subject to income tax under s 687(1) on the sums received when Special Capital was reallocated to them. In summary, my view is that the requirements for that section to apply, as explained in the case law set out above, are met on the basis that:

(1) The sums received by the Members on withdrawing Special Capital reallocated to them by PSCL is their income and is of a type analogous to employment income or income from a trade.

(2) The "source" of that income is the Members' continued activity as members of Odey and their ongoing provision of their fund management services for the benefit of Odey and PSCL as a Member of Odey (albeit it was a Member with a special purpose to further Odey's business).

(3) That is a source with sufficient connection to the Members for the reasons set out below.

377. It is clear from *Spritebeam* that the circumstances in which s 687 may be taken to apply to tax sums are not limited to cases where the sums are paid under a contractual obligation which is enforceable by the recipient:

(1) In discussing whether the requirement for the sums received to be income of the recipient was met, the UT said that "what matters is whether there is an obligation on the payer to pay". They contrasted *Stedeford v Beloe* where the headmaster was not subject to income tax on payments received from the governors because there was no obligation on the governors to make the payments with the trustee cases, such as *Drummond*, where the beneficiaries were liable to income tax on sums received from the trustee because, whilst the trustee had discretion to make the payments, it was under an enforceable obligation to exercise that discretion and make a payment to one or more of the beneficiaries as circumstances required.

(2) Similarly, in discussing whether the requirement for there to be a sufficient connection between the source and the recipient was met, the UT said that the "required connection between taxpayer and source need not be limited to legal rights but can include the situation where the payment is made *pursuant to any legal duty owed by the payer*" (emphasis added). They noted that proposition is consistent with the decision in *Cunard's Trustee*, where the focus was on the payer's obligation to the recipient, and not on the recipient's ability to enforce it; Lord Greene focused on the fact that whilst the trustees in that case "had an absolute discretion" whether to make a payment or not, "the question whether they should do so is one which they were bound to take into their consideration". They could not refuse to consider whether they should do so and "the fact that, after examining that matter, they might come to the conclusion" not to exercise it did not "give to a payment, if and when made, the character of a voluntary payment in any relevant sense".

(3) On that basis the UT held that these requirements were met in *Spritebeam* notwithstanding that the recipient of the shares had no legally enforceable right to have the shares issued and allotted to it is. It sufficed that the borrower had an absolute and unconditional obligation to allot and issue the shares to the share recipient; that obligation was "in no sense voluntary".

378. I note that Mr Goldberg said that the decision in *Cunard's Trustee* is not in point because the sums in question were held to be taxable under Schedule D Case III and Schedule D Case VI/s 687 was not in point. However, as Mr Chacko noted, in *Spritebeam,* the UT plainly did not consider that such circumstances could constitute a source for the purposes of Schedule D Case III but not of Schedule D Case VI/s 687. For the reasons already set out, I do not consider that *Manduca*, *Dickinson v Abel* or *Scott v Ricketts* provide authority that a payment for services, of the kind under consideration here, can be taxable under s 687 only if made under a binding contractual obligation which the recipient is able to enforce as regards the payment.

379. In my view, the evidence establishes that the Members were rewarded for their work for and membership of Odey, not only by the direct allocation of profits in the year of allocation, but also by the reallocations of Special Capital made to them by PSCL in subsequent periods which was made in respect of the individual shares "awarded" to them in the year of allocation. I refer to the analysis of how the arrangements worked in a contractual sense, at [319] to [333], and highlight that:

(1) As set out at [322], RemCom determined any individual share "awarded" to a Member by reference to the Member's performance in the relevant period (see also [55], [56] and [103] above). It was not disputed that profits equal in amount to the individual shares would have been allocated and paid to the relevant Members in the year of allocation but for the introduction of the Remuneration Policy and related measures required to give effect to it.

(2) The rationale underpinning the Plan was to incentivise and retain key Members by, in broad terms, "deferring" the time at which their right or entitlement to the individual shares crystallised so that they became entitled to those shares only if they remained as Members of Odey at the specified date and the relevant monies were not required for other business purposes of Odey (in particular to maintain capital for regulatory purposes) on the basis that, in the meantime, the funds would be invested in Funds which the relevant Members managed.

(3) PSCL was formed specifically for the purpose of facilitating the operation of the Plan and the individual shares were transferred to it expressly for that purpose.

(4) ExCo/RemCom was obliged to comply with the terms of the Remuneration Policy in allocating profits to Members and dealing with individual shares awarded to Members to the extent and as explained in further detail above.

(5) In line with its obligations under the Remuneration Policy, (a) ExCo/RemCom made initial recommendations to PSCL that it should reallocate Special Capital to Members who had been "awarded" individual shares, and (b) before the scheduled date for a Member to receive a reallocation it notified PSCL of whether the conditions set out in the Remuneration Policy were satisfied, namely, whether the Member remained as such and whether Odey had sufficient capital.

(6) As set out in further detail at [319] to [333], whilst Members did not have an enforceable right to require PSCL to make reallocations of Special Capital to them, for all the reasons set out above:

(a) PSCL had a form of fiduciary role in relation to the Plan in that its sole purpose was to further the business interests of Odey by making contributions of Special Capital and reallocations of Special Capital on receipt of recommendations from ExCo/RemCom and, accordingly it "adopted" the Remuneration Policy, and

(b) in exercising its discretion to make such reallocations under the reallocation provision, PSCL was obligated to the Members, acting honestly, in good faith and rationally, to consider any recommendation made by ExCo/RemCom for it to make reallocations and, in doing so, to take account of the Remuneration Policy.

380. In my view, s 687 is deliberately widely drawn as something of a flexible "sweep up" provision in order to capture income which ought to be taxable but which somehow lacks the characteristics for it to fall within the other specific provisions in the income tax code. Whilst this case is not on all fours with the circumstances of *Spritebeam* or the trustee cases, it seems to me that it is sufficiently analogous to the circumstances in which the courts in those cases held there was a taxable source of income for the relevant sums to fall within the terms of s 687.

381. This is not a situation where, like in *Stedeford v Beloe*, the receipt of the sums depended entirely on the goodwill of the payer such that it is a mere voluntary gift which is not in a true sense of the word income as "a casual payment which depends on someone else's goodwill". Rather, in the context of the overall operation of the Plan:

(1) The sums paid by Odey to Members following a reallocation of Special Capital by PSCL retained the same character as the individual shares to which the Special Capital related, as a reward for the Member's continued membership of and performance of activities for Odey. Taking into account all the factors set out above, the fact that the Awards were crystallised and realised through the Special Capital mechanism did not somehow change the reason the relevant sums referable to those Awards were received by the relevant Members. In other words, for the purposes of s 687, the fact that the sums were paid through the Special Capital mechanism did not remove their clear link with the Members' membership of and activities for Odey.

(2) There was a sufficient connection between that source and the Members given that PSCL was under (a) a duty to its shareholder to further Odey's business by making reallocations of Special Capital where it received a recommendation to do so, and (b) a contractual obligation to other Members to consider exercising its discretion to reallocate Special Capital in good faith, honestly and rationally according to the recommendation made by ExCo/RemCom and the Remuneration Policy.

(3) By analogy with the trust cases set out above, either (a) the existence of that obligation and duty of itself suffices for there to be source with a sufficient connection for the purposes of s 687, or (b) such a source with a sufficient connection came into existence when PSCL exercised its discretion to allocate Special Capital thereby entitling the Member to the relevant sums under the contractual mechanism which then came into play under the 2011 LLP Agreement.

Part D - Sale of Occupation Income

382. Finally, HMRC argued that if the sums paid to Members following the reallocation of Special Capital to them fall outside s 687 ITTOIA, then they are taxable as income under ss 773 to 778 of chapter 3 of part 13 ITA.

383. In the remainder of Part D references to sections of legislation are to sections in chapter 2 of part 13 ITA unless there is an express statement to the contrary.

Law

384. A tax charge may arise under ss 773 to 778 where the following requirements are met:

(1) (a) An individual carries on an occupation wholly or partly in the UK (under s 777(2)), which is defined as "any activities of a kind undertaken in a profession or vocation…" (under s 774) (Condition A);

(2) "transactions are effected or arrangements are made to exploit that individual's earning capacity by putting another person (see section 782) in a position to enjoy –

(a) all or part of the income or receipts derived from the individual's activities in the occupation, or

(b) anything derived directly or indirectly from such income or receipts" (under s 777(3) (Condition B);

(3) "as part of, or in connection with, those transactions or arrangements, a capital amount (defined as an amount of money or money's worth which is not otherwise taxed as income) is obtained by the individual for the individual or another person" (under s 777(5) (Condition C);

385. Where the above requirements are met:

(1) s 778(1) states that it applies if the capital amount obtained as mentioned in s 777(5) does not consist of - (a) "property which derives substantially the whole of its value from the individual's activities", or (b) "a right which does so".

(2) In that case, the capital amount is treated for income tax purposes as income arising to the individual in the tax year in which the capital amount is receivable (under ss 777(2) and (3)). A capital amount is not regarded as having become receivable by a person for the purposes of this section until the person can effectively enjoy or dispose of it (under s 777(4)).

(3) Under s 773, it is provided that income is treated as arising under s 778 only if two conditions are satisfied. The first condition repeats that set out in Condition B above. The second is that "the main object, or one of the main objects, of the transactions or arrangements is the avoidance or reduction of liability to income tax".

386. It was not disputed that if HMRC's arguments on the above points are not accepted, condition C is satisfied.

Submissions

Condition A

387. HMRC submitted that it is apparent that the purpose of these anti-avoidance provisions is to catch schemes in which individuals, in effect, sell their earning potential in exchange for capital payments. Accordingly, the phrase "activities of a kind undertaken in a profession or vocation" in Condition A is intended to be of wide

application. It should not be approached in a forensic and technical way or construed in a narrow and antiquated manner; that would frustrate the purpose of the provision.

388. HMRC referred to the following dicta of Scrutton LJ in *CIR v Maxse* (1919) 12 TC 41 at page 61 and Du Parcq LJ in *Carr v IRC* [1944] 2 All ER 163 at page 166 which make it clear that how the word "profession" is to be interpreted varies over time with social change and is to be determined according to the meaning a reasonable person would ascribe to it at the time in question:

(1) In *Maxse,* Scrutton LJ said:

> "… what is a "profession"? I am very reluctant finally to provide a comprehensive definition…it seems to me… that a "profession" in the present use of language involves the idea of an occupation requiring either purely intellectual skill, or if any manual skill, as in painting and sculpture, or surgery, skill controlled by the intellectual skill of the operator, as distinguished from an occupation which is substantially the production, or sale, or arrangements for the production or sale of commodities. The line of demarcation may vary from time to time. The word "profession" used to be confined to the three learned professions, the Church, Medicine and Law. It has now, I think, a wider meaning.
>
> It appears to me clear that a journalist whose contributions have any literary form, as distinguished from a reporter, exercises a 'profession'; and that the editor of a periodical comes in the same category. It seems to me equally clear that the proprietor of a newspaper or periodical, controlling the printing, publishing and advertising, but not responsible for the selection of the literary or artistic contents does not exercise a 'profession', but a trade or business other than a profession.
>
> What then is to be done if the same man is both proprietor, editor and contributor? In my view, it can always be determined as a question of fact what is his reasonable remuneration as contributor ..."

(2) In *Carr,* Du Parcq said:

> "I think that everyone would agree that, before one can say that a man is carrying on a profession, one must see that he has some special skill or ability, or some special qualifications derived from training or experience. Even there one has to be very careful, because there are many people whose work demands great skill and ability and long experience and many qualifications who would not be said by anybody to be carrying on a profession. Ultimately one has to answer this question: Would the ordinary man, the ordinary reasonable man – the man, if you like to refer to an old friend, on the Clapham omnibus – say now, in the time in which we live, of any particular occupation that it is properly described as a profession?..."

389. HMRC said that the ordinary observer looking at the specialism, skill and remuneration of the Members of Odey would say that they were financial professionals providing professional services: they would not say that they were tradesmen:

(1) The skills of an analyst and a fund manager are based on intellect and judgement and the two roles require very similar skills.

(2) Furthermore, Odey's income, like that of other professional firms, is fee income for services provided and not the profit on buying or selling (trading) in goods, financial instruments or any other asset. Investors invested money in Funds managed by Odey. The Funds were in effect Odey's clients since they agreed to pay fees for the management of the Funds. Whilst some of the Members had their own money invested in the Funds that simply put them in

the same position as, for example, a solicitor who obtains advice from their own firm in a personal capacity.

(3) The great majority of Odey's income came from management fees and performance fees. While performance fees were linked to the performance of the Funds, management fees were not except indirectly in that they were linked to the value of Odey's assets under management.

(4) Some Members had management roles with Odey, but they had a background in fund management (except Mr Pearey who had an accounting background). In any event, the partners in a law firm are engaged in managing the lawyers but that does not mean that they are not engaged in professional activities. While Odey employed traders, the traders were not Members of Odey apart from the head of trading who essentially had a management role.

(5) All these are the hallmarks of professional activity today. We no longer live in a world where a person is not regarded as undertaking professional activities because their work involves markets, financial or otherwise. The tribunal should adopt a modern and common-sense approach to this issue, just as Judges were prepared to do a century ago.

390. HMRC continued that, alternatively, the Members' activities are of a kind undertaken in a vocation on the basis of caselaw where it has been held that a vocation constitutes any way of earning money which is systematically carried on but is not a form of buying and selling. In their view, the Members set out to make profits in a systematic manner by providing investment management services and, as noted, their income derived from fees paid by their clients and not from buying or selling on their own account.

391. HMRC relied on *Partridge v Mallandaine* (1886) 2 TC 179 where, at page 181, Denman J held that bookmakers carried on a "vocation" as follows:

> "….I think the word 'vocation' is a still stronger word. It is admitted to be analogous to the word 'calling', which is a very large word; it means the way in which a person passes his life, and it is a very large word indeed. These persons goes to races and they systematically bet, and for this reason, it must be assumed, make profits. Does it lie in their mouths to say that they are not to be assessed to income tax because they cannot bring an action in respect of the bets which they make ... so many of theirs bets paid as puts, say, £1,000 a year in their pockets; and to say that because they cannot bring an action to recover the bets they make, betting being made illegal ... therefore they cannot carry on a vocation, it seems to me is putting a construction upon the Act which would be giving a very undue favour to persons with whom the legislature is by no means to deal with favour, inasmuch as the thing they do is a thing which is hampered by the legislature because it is supposed to be mischievous, namely, the recovery of bets by actions so as to facilitate the making of bets and carrying on of vocations such as this. But I go the whole length of saying that, in my opinion, if a man were to make a systematic business of receiving stolen goods and to do nothing else, and he thereby systematically carried on a business and made a profit of £2,000 a year, the Income Tax Commissioners would be quite right in assessing him, if it were in fact his vocation. There is no limit as to its being a lawful vocation, nor do I think the fact that it is unlawful can be set up in favour of these persons as against the rights of the Revenue to have payment in respect of the profits that are made. I think this does come within the definition of the word 'vocation' according to common sense."

392. HMRC also relied on *Graham v Green* (1925) 9 TC 309 where, at pages 313 to 314, the court reached the following conclusion relying on the earlier case:

> "It has been settled that a bookmaker carries on a taxable vocation. What is the bookmaker's system? He knows that there are a great many people who are willing to back horses and they will back horses with anybody who holds himself out to give reasonable odds as a bookmaker. By calculating the odds in the case of various horses over a long period of time and quoting them so that on the whole the aggregate odds… are in his favour, he makes a profit. That seems to me to be organising an effort in the same way that a person organises an effort if he sets out to buy himself things with a view to securing a profit…"

393. Finally, HMRC submitted that the reference in s 774 to professions and vocations, but not trades, is intended to exclude from its ambit those who earn money by buying and selling assets and profiting on the sale. If a person makes money by selling stock-in-trade, he cannot dispose of that to someone else without incurring a charge to income tax, either as a commercial sale or on the principle in *Sharkey v Wernher* [1956] AC 58. This principle does not apply to professions (see *Mason v Innes* 44 TC 326). There was, therefore, no need to apply this anti-avoidance machinery to those who made money by selling their stock, but the exclusion should not be extended more widely than that.

394. The appellants submitted that Odey and so its Members in fact carry on a trading activity in acting as fund managers trading in investments and it/they profit from the performance of the funds by way of management and performance fees, calculated by reference to the value of funds under management, namely, from how well the traders perform in buying and selling investments. The business consists of selling services to customers (the Funds under management) and is as much of a trade just as selling train journeys to passengers is a trade. The concept of trade is not limited to purchases and sales of assets.

395. Mr Goldberg said that the law on this point was laid down in 1919 or earlier and is very clear. In addition to the cases which HMRC referred to, Mr Goldberg also referred to the following cases:

(1) *Burt & Co v IRC* [1919] 2 KB 650 where Scrutton LJ said the following, at page 658:

> "whatever may be the limitation of a profession, I do not think it applies to the exercise of commercial knowledge in connection with the sale of goods, or export or import of goods".

(2) *Christopher Barker & Sons Ltd v IRC* [1919] 2 KB 222 where Rowlatt J held that a stockbroker's business was not a profession and commented as follows, at page 229:

> "Now is a stockbroker's business a profession within the meaning of the section. It seems to me that what a stockbroker does is to buy and sell a commodity on the market. It is true he does not expect to have to pay for it himself or to be responsible ultimately to satisfy the contract itself, as he's a buyer and seller in the market for an undisclosed principal to whom he looks to indemnify him from liability. It does not seem to me that that is a profession within the meaning of this section. A stockbroker is remunerated by a commission, which he receives from his principal. The person who takes the liability off his shoulders. In my opinion, the advice given by a stockbroker comes within the dictum of Lord Justice Scrutton in *Burt & Co v IRC* because it is the exercise of commercial knowledge in connection with the sale of commodities in the market. Therefore, it seems to me that although the appellant does a certain amount of advising for which they were remunerated by fees, it is advice given in connection with the exercise

> of the business of a stockbroker, and that in giving that advice, they are not exercising any profession at all, even assuming that part of the business can be severed from the purely stockbroking part of their business of buying and selling stocks and shares for which they are remunerated by commission."

(3) *Asher v London Film Productions Limited* [1944] 1 KB 133 in which Lord Greene MR (with whom MacKinnon and Goddard LJJ) was, at 139, "entirely unconvinced" that, on the facts of that case, a film producer was, "carrying on any 'profession or vocation' at all according to the true meaning of those words".

(4) *Kowloon Stock Exchange Limited v Commissioner of Inland Revenue (Hong Kong)* [1984] UKPC 38 where the Privy Council rejected the argument that the Kowloon Stock Exchange carried on a profession and was not a trade association at pages 209 and 210. They rejected the argument that the taxpayers more naturally answered to the title of a professional or business association on the basis that, whilst a stockbroker is engaged in the buying and selling of shares he does so only as an agent for his clients and not on his own account and his involvement in doing so "is only one of the functions he performs for his clients. Of equal importance is his role as a person exercising specialist professional skills in giving advice to his clients". They concluded that:

> "A stock exchange in unquestionably a market….Stocks and shares are traded in that market. The trading in that market is done by brokers, who are therefore traders. An association which is formed by traders to hold and manage premises for the purposes of their trade is a trade association."

396. Mr Goldberg pointed out that at the hearing Mr Stewart said that the description in *Kowloon* of how the stockbroker's viewed their business corresponded to Odey's business. Mr Goldberg submitted that, on the basis of the caselaw, the business of Odey is not a profession because (a) it involves the exercise of commercial knowledge in relation to assets, namely, knowledge and experience of the markets, and (b) does not necessarily involve long training or a formal qualification. He added that it is notable that there are several companies which are Members of Odey. It is highly unusual for a company to be able to carry on a profession. (Certain companies formed before 1930 can carry on the profession of dentist, but that is because there is a special statutory rule that allows them to do it). In his view, the business of Odey is plainly not a vocation. Mr Goldberg noted that the decision that bookmakers were carrying on a vocation is, so far as he was aware, the only business that has ever been described as a "vocation".

397. Mr Chacko said that the circumstances of these appeals are not wholly analogous to those of the stockbroker cases Mr Goldberg referred to. In those cases. it was held essentially that persons who make money by selling things with an advisory side were not professionals. Here, however, the tribunal is concerned with fund managers (and analysts) who use their expertise to advise people how to manage the funds albeit that is implemented by buying and selling underlying assets. Hence, the principal income received by Odey is not commission on sales as such but the fees Odey receives.

Condition B

398. On Condition B:

(1) Mr Chacko said that if, contrary to HMRC's view, the deferred share was allocated to PSCL in the year of allocation, it necessarily follows that Condition B is satisfied. In his view, it is necessarily the case that, in those circumstances,

PSCL is put in a position to enjoy part of the income derived from each Member's activities.

(2) Mr Goldberg submitted that, on the contrary, no other person (which, it is accepted, can include Odey itself) is put in a position to enjoy any relevant income of the Members. In fact, Odey was the person with the income and receipts from the fund management business and it put the individual Members in a position to enjoy part of that income by allocating it to them as Members in accordance with their profit sharing rights under the 2011 LLP Agreement. PSCL did not get anything derived from the individual Members' activities; rather it had its own income derived by it as a partner in Odey. No Member, taken on his own, has income or receipts which another person can enjoy. In other words, there is nothing equating to a sale of occupational income in this case; the Members may, in subsequent years following the year of allocation, acquire Special Capital but they did not sell their income to get it. This is supported by *Vaines* and *Mackinlay* (see the passages set out in Part B above).

Main purpose test

399. On the requirement in s 773 that the main object, or one of the main objects, of the transactions or arrangements is the avoidance or reduction of liability to income tax:

(1) Mr Chacko submitted that the reduction in a potential liability to tax was plainly one of the main objects of the Plan. He noted that:

(a) As the legal question is about the object of the arrangements, not the object of the parties, the question is not entirely subjective but includes the reasons for the arrangements being designed in the manner they were by the advisers and promoters who designed them and encouraged the taxpayer to use them (see Nugee J in *Seven Individuals v HMRC* [2017] STC 874 at [104]).

(b) The witness and documentary evidence set out above (in the form of the note from Ernst & Young) establish that achieving a reduction in tax was one of the main objects of the Plan. It is notable that the witnesses make reference to avoiding an "unfair" tax charge on deferred remuneration. A main object to avoid a tax charge perceived by the taxpayer as unfair is still a main object to avoid that tax charge.

(2) Mr Goldberg said that none of the main objects of the Remuneration Policy was the avoidance or reduction of tax:

(a) The persons whose objects are relevant here are Odey and its Members and, perhaps, those of PSCL (and its directors) when making allocations of Special Capital (see *Oxford Instruments UK 2013 Ltd v Revenue & Customs Commissioners* [2019] UKFTT 254 (TC) at [99]).

(b) An object is to be distinguished from a consequence, so that the presence of a tax consequence does not mean that obtaining the consequence was an object of what was done (see *Lloyds Bank Leasing (No.1) Ltd v Revenue and Customs Commissioners* [2015] UKFTT 401 (TC) at [37]). Moreover, an object can be significant without being main (see *Travel Document Service & Anor v Revenue & Customs* [2017] UKUT 45 (TCC) at [48]).

(c) The introduction of the Remuneration Policy and its operation had commercial and regulatory objects. There was, of course, a tax consequence of the Plan, which was that PSCL rather than anyone else

(c) was taxable on the deferred shares allocated to it. But this was a consequence of achieving the commercial objects and not an object at all.

(d) Alternatively, given the commercial objects of introducing the Policy, the tax consequences cannot, even if regarded as an object, be a main object; it is wholly subsidiary to the achievement of the commercial and regulatory objects.

Conclusions

400. I deal with Condition B first as, in my view, that condition is not satisfied, so that I do not need to deal with the other conditions. In my view, even if the Members can be viewed as carrying on activities of a kind undertaken in a profession or vocation, under the arrangements made under the Plan, no transactions were effected or arrangements made to exploit the Members' earning capacity by putting another person in a position to enjoy all or part of the income or receipts derived from their activities in the occupation:

(1) Odey was the person who, as a legal matter and for tax purposes, generated and received income from the fund management business which it carried on (see the description of how the tax charge works in *Vaines* and *MacKinlay* as set out in Part B).

(2) Odey, acting through ExCo/RemCom, calculated and allocated the profits generated from its fund management business to the Members in accordance with their profit sharing rights under the 2011 LLP Agreement.

(3) For all the reasons set out in Part B, my view is that the individual Members had no rights in the sense of a legal entitlement to the individual shares "awarded" to them in the year of allocation. Only PSCL had an entitlement to those individual shares. The fact that they were allocated to it solely for the purposes of the Plan does not affect this analysis. The individual Members' entitlement to or interest in those shares crystallised only when, in later years, PSCL exercised its discretion to reallocate Special Capital to them.

(4) It follows that when the individual shares were allocated to PSCL, PSCL was not put in a position to enjoy all or part of the income or receipts of the Members derived from their activities of a kind undertaken in a profession or vocation (if they may be classified as such). Rather PSCL received its own income, in the form of its own share of the profits of Odey, derived by it as a Member in Odey (in its special role in relation to the Plan). The individual shares were not in the first place the income or receipts of the relevant Members conceptually or actually.

401. I note that HMRC's own view is that the purpose of these anti-avoidance provisions is to catch schemes in which individuals, in effect, sell their earning potential in exchange for capital payments. However, for the reasons already set out, on the correct analysis of the operation of the Plan under the partnership arrangements, there is no such sale by the individual Members.

402. On that basis, it is not necessary for me to conclude whether the other requirements set out above are satisfied. As the points were argued, I comment, however, that:

(1) In my view, the activities of all of the appellants are akin to those of a profession for the reasons set out by HMRC. I agree with HMRC's view that the tribunal should adopt a modern and common-sense approach to this. Over a 100 years ago, Scrutton LJ noted, in *Maxse*, that that the "line of demarcation may vary from time to time" and Parcq LJ said the issue was best approached

by asking whether the ordinary reasonable man "say now, in the time in which we live, of any particular occupation that it is properly described as a profession". In my view, the modern ordinary reasonable man would consider that the Members' activities are those of a profession given, in particular, the intellectual skill and special ability their activities evidently require. It is not evident to me that the Members' activities are on all fours with those of the stockbroker in *Kowloon* but in any event, in my view, a different view may well be taken of their activities today.

(2) In my view, whilst there were plainly other commercial reasons for the transactions or arrangements implemented under the Plan, *one of* the main objects of those transactions or arrangements is the avoidance or reduction of a liability to income tax. I note, in particular that, (a) as is apparent from the note prepared by Ernst & Young, the Plan in this form was designed by Ernst & Young with a view to achieving a considerable reduction in the overall effective rate of tax on the relevant profits which were subject to the Plan, (b) Mr Pearey, Mr Odey and Mr Stewart all said, in effect, that they wanted to avoid the upfront tax charge which applied under the ad hoc incentive arrangements which Odey used before the Plan was put in place, and (c) the tax saving plainly was an important feature in making the Plan palatable to Members (see, in particular, [58], [91], [98] and [190] to [203]). Given those factors, I consider that the witnesses' view that the tax saving was not a main objective of the Plan but merely a consequence of the Plan or that the tax saving is incidental only is unrealistic.

Part E - Procedure

Overview

403. The appellants challenged the validity of the following assessments made under s 30B TMA and s 29 TMA for the reasons explained below:

(1) The discovery amendment made under s 30B TMA to Odey's partnership tax return for the tax year 2011/12 issued on 22 March 2016.

(2) The discovery assessments made under s 29 TMA to the self-assessment tax returns of:

(a) Mr Pearey for the tax years 2011/12 and 2012/13 issued on 1 April 2016 and 31 March 2017 respectively.

(b) Lord Roborough for the tax years 2011/12 and 2012/13 issued on 31 March 2016 and 31 March 2017 respectively.

(c) Mr Stewart for the tax year 2011/12 issued on 31 March 2016.

(d) Mr Feras Al-Chalabi for the tax year 2011/12 and 2012/13 issued on 31 March 2016 and 31 March 2017 respectively.

(e) Mr Fletcher for the tax year 2011/12 and 2012/13 issued on 31 March 2016 and 31 March 2017 respectively.

(f) Mr James Hanbury for the tax year 2011/12 and 2012/13 issued on 1 April 2016 and 31 March 2017 respectively.

(g) Mr Bruce Hubbard for the tax year 2011/12 and 2012/13 issued on 1 April 2016 and 28 March 2017 respectively.

(h) Mr Benjamin Lambert for the tax year 2011/12 and 2012/13 issued on 1 April 2016 and 28 March 2017 respectively.

(i) Mr Orlando Montagu for the tax year 2011/12 and 2012/13 issued on 1 April 2016 and 31 March 2017 respectively.

(j) Mr Feras Al-Chalabi for the tax year 2013/14 issued on 31 March 2018.

(k) Mr Bruce Hubbard for the tax year 2013/14 issued on 21 March 2018.

(l) Mr Pearey for the tax year 2013/14 issued on 21 March 2018.

404. HMRC asserted that the assessments referred to in (1) and (2)(a) to (i) were made by Ms Rachel Frusher and those referred to in (2)(j) to (l) were made by Mr Ben Blakely.

405. Ms Frusher and Mr Colin Williams of HMRC gave evidence in relation to these assessments and attended the hearing and were cross examined. Mr Williams supervised Mr Blakely who was not available to give evidence due to taking a career break. I found them to be honest and credible witnesses.

Law

406. All reference in the remainder of Part E of this decision to sections, chapters and parts of legislation are to sections, chapters and parts of the TMA unless it is specifically stated otherwise.

407. Section 29(1) and 30B provide a mechanism respectively for HMRC to make an assessment where the usual time limit of 12 months for them to enquire into an individual's self-assessment return or a partnership tax return has expired.

408. By way of background, the self-assessment tax regime for individuals operates as follows:

(1) Section 8 requires a taxpayer to provide a self-assessment tax return for each tax year where HMRC gives him notice to do so which, under s 9 must include the taxpayer's self-assessment of the amounts in respect of which he is chargeable to income tax and capital gains tax for the tax year and of the amount payable by him by way of income tax.

(2) The self-assessment tax regime essentially operates on a "process now - check later basis". For each tax year a person is required to pay (a) sums on account of income tax during the tax year and (b) (i) capital gains tax and (ii) any balance of income tax payable shortly after the end of the tax year according to the figures set out in his return as set out in ss 59A and 59B.

(3) Within a specified time limit, a person can amend a return made under s 8 by notice to an officer of the Board and an officer of the Board can amend such a return to correct (a) an obvious error or (b) anything else in the return that the officer has reason to believe is incorrect.

(4) Under s 9A(1), HMRC have the power to enquire into a return made under s 8 within a specified time limit. Usually, the time limit expires 12 months after 31 January following the end of the relevant year of assessment. An enquiry may extend, among other matters to "anything contained in the return, or required to be contained in the return, including any claim or election included in the return" (under s 9A(4)(a)).

(5) Such an enquiry "is completed when an officer of the Board by notice (a "closure notice") informs the taxpayer that he has completed his enquiries and states his conclusions" (under s 28A(1)). A closure notice must either "(a) state that in the officer's opinion no amendment of the return is required, or (b) make the amendments of the return required to give effect to his conclusions" (under s 28A(2)).

(6) Otherwise, HMRC have limited powers to issue discovery assessments where certain conditions are satisfied (under s 29) or to recover overpayments of tax (under s 30).

409. Partnerships or LLPs such as Odey are required to submit a partnership tax return in relation to which HMRC operates a similar process now check later regime as follows:

(1) Under s 12AA, HMRC may give notice to a partner in a partnership such as Odey to submit a partnership return for each year of assessment for the purpose of facilitating the establishment of (a) the amount in which each partner chargeable to income tax for any year of assessment is so chargeable and the amount payable by way of income tax by each such partner, and (b) the amount in which each partner chargeable to corporation tax for any period is so chargeable.

(2) Under s 12AB(1), each such partnership return must include a partnership statement for each specified period of sums including under (a) (i) the amount of income or loss from each source which, on the basis of information contained in the return and taking into account any relief or allowance…..has accrued to or has been sustained by the partnership for the period in question, and under (b) for such periods and each of the partners, "the amount which, on that basis and (where applicable) taking into account any such relief or allowance, is equal to his share of that income, loss…."

(3) Under s 12ABA, a partnership tax return may be amended by the partner who made and delivered it within certain time limits and under s 12ABB an officer of the Board may correct it. Under s 12AC an officer of the Board may enquire into a partnership tax return within a specified time limit under similar provisions to those in s 9A.

410. Section 29 contains the following provisions of relevance:

(1) Section 29(1) is stated to apply where "an officer of the Board or the Board discover" as regards any person (the taxpayer) and a year of assessment" that, amongst other circumstances, "(a) any income which ought to have been assessed to income tax has not been assessed" or "(b) that an assessment to tax is or has become insufficient". By way of shorthand, I refer to these circumstances and the equivalent circumstances set out in s 30B(1) as "an insufficiency of tax". In that case the officer or the Board "may, subject to subsections (2) and (3), make an assessment "in the amount, or the further amount, which ought in his or their opinion to be charged in order to make good to the Crown the loss of tax".

(2) Where a taxpayer has made and delivered a self-assessment return under s 8 or 8A he cannot be assessed under s 29(1) in respect of that year of assessment and in the same capacity as that in which he made the return, unless one of two conditions is satisfied (under s 29(3)), namely:

(a) that the insufficiency of tax was brought about carelessly or deliberately by the taxpayer or a person acting on his behalf (under s 29(4)), or

(b) when an officer ceased to be entitled to give notice of his intention to enquire into the taxpayer's return or had informed the taxpayer that he had completed his enquiries into that return, he "could not have been reasonably expected, on the basis of the information made available to him before that time, to be aware of [the insufficiency]" (under s 29(5)).

HMRC do not argue that s 29(4) is in point but that s 29(5) is applicable.

(3) For the purposes of s 29(5), information is made available to an officer of the Board if (under s 29(6)):

> "(a) it is contained in the taxpayer's return under section 8 or 8A of this Act in respect of the relevant year of assessment (the return), or in any accounts, statements or documents accompanying the return;
>
> (b) it is contained in any claim made as regards the relevant year of assessment by the taxpayer acting in the same capacity as that in which he made the return, or in any accounts, statements or documents accompanying any such claim;
>
> (c) it is contained in any documents, accounts or particulars which, for the purposes of any enquires into the return or any such claim by an officer of the Board, are produced or furnished by the taxpayer to the officer, whether in pursuance of a notice under section 19A of this Act or otherwise; or
>
> (d) it is information the existence of which, and the relevance of which as regards the situation mentioned in subsection (1) above—
>
> (i) could reasonably be expected to be inferred by an officer of the Board from information falling within paragraphs (a) to (c) above; or
>
> (ii) are notified in writing by the taxpayer to an officer of the Board."

I note that, as set out in the case law section below, it is established that the above represents an exhaustive list of the documents and information which is made available to an officer for the purposes of these provisions.

(4) Under s 29(7):

(a) the reference to a taxpayer's return under s 8 or 8A in respect of the relevant year of assessment in s 29(6) includes:

(i) a reference to any return of the taxpayer under that section for either of the two immediately preceding years of assessment (under s 29(7)(a)(i)), and

(ii) where the return is made under s 8 and the taxpayer carries on a trade, profession or business in partnership, a reference to any partnership return with respect to the partnership for the relevant year of assessment or either of those periods (under s 29(7)(a)(ii)),

(b) and (b) any reference in s 29(b) to (d) to the taxpayer includes a reference to a person acting on his behalf (under s 29(7)(b)).

411. Under section 30B(1):

(1) Section 30B1 similarly applies where "an officer of the Board or the Board discover as regards a partnership statement made by any person (the representative partner) in respect of any period" that "(a) any profits which ought to have been included in the statement have not been included", or "(b) that an amount of profits so included is or has become insufficient". In that case the officer or the Board "may, subject to subsections (3) and (4), by notice to that partner, so amend the partnership return….as to make good the omission or deficiency….".

(2) Under s 30B(2) where a partnership return is amended under s 30B(1), the officer "shall by notice to each of the relevant partners amend (a) each partner's

return under s 8 or 8A of this Act, or (b) the partner's company tax return, so as to give effect to the amendments of the partnership return".

(3) Pursuant to s 30B(4) the same conditions are imposed in s 30B(5) and s 30B(6) as those as set out in s 29(4) and s 29(5) in relation to careless and deliberate behaviour and the sufficiency of information. Section 30B(7) provides that s 29(6) and s 29(7) applies for the purposes of s 30B(6) as they apply for the purposes of s 29(5) as though any reference to the taxpayer were a reference to the representative partner and any reference to a taxpayer's return made under s 8 or 8A were a reference to the representative partner's partnership tax return but with the omission of s 29(7)(a)(ii).

(4) Under s 30B(9)(a) "profits" include, in relation to income tax, income and in relation to corporation tax, profits as computed for the purposes of that tax and "relevant partner" means any person who was a partner at any time during the period in respect of which the partnership statement was made.

Use of s 30B

412. The appellants argued that the amendment issued to Odey in respect of the 2011/2012 tax year is invalid because s 30B cannot be used to adjust the allocation of income between the Members in the relevant period. In their view, that provision enables HMRC only to adjust the total profits of Odey and not the individual allocations of those profits between the Members. Mr Goldberg noted that:

(1) HMRC do not claim that the profits included in Odey's partnership statement for 2011/12 are in any way insufficient. Rather HMRC's complaint is that the allocation of profits between the Members is wrong. Even if that is correct (which is disputed), there are simply no profits which ought to have been included in the partnership statement which have been omitted from it.

(2) The reference in s 30B(1) to profits not being included in the partnership statement is plainly to the income which under s 12AB(1)(a) must be included in the partnership statement, namely, the income from each source which has accrued to the partnership for the period in question (see also s 30B(9)(a)). However, all of that income has been included in the relevant partnership statement.

(3) On that basis, HMRC are bound by the partnership statement for 2011/12 as originally filed.

(4) In support of their submissions, the appellants relied on the decision in *Albermarle 4 LLP v Revenue & Customs* [2013] UKFTT 83 (TC) ("*Albermarle*") at [64] to [69].

413. HMRC said that, on the contrary, it suffices for s 30B(1) to apply that any amount required to be shown in the partnership statement under s 12AB(1)(b) is wrong, namely, for each partner, the amount which is equal to his share of the income required to be shown under s 12AB(1)(a). On that basis, where too much income has been allocated to one partner, the partnership statement will inevitably show an amount of income allocated to other partners which is too small and so insufficient within the meaning of s 30B(1). Mr Chacko added that:

(1) It would be extraordinary if s 30B does not enable HMRC to amend the amounts to which any given partner is chargeable to income tax unless they amend the total income of the partnership. The whole point of requiring a partnership to provide a tax return is to provide information on each partner's income and ensure consistency between the partners.

(2) The appellants' interpretation of s 30B would mean that, if HMRC discover that the allocation of income between partners in the partnership statement is incorrect, they would have to raise discovery assessments against each individual who had been allocated too little income, with no apparent means of correcting the position for the individuals who had been allocated too much (and had paid too much tax). In cases of careless or deliberate error, those individuals might be out of time to make a claim even if HMRC informed them of the position.

(3) Judge Mosedale observed in *Gibbs v HMRC* [2013] UKFTT 236 (TC) at [55] that the system of partnership returns and amendments is intended to avoid individual partners challenging the total partnership income in inconsistent ways, but the reverse is equally true: the allocation between partners is in the partnership return, and must be amended in the partnership return, as otherwise disputes could give rise to a case where the partnership's profits were either over-allocated or under-allocated.

(4) In any event, the discovery assessments for 2011/12 were raised to deal with and the tribunal can impose additional liabilities on the individual partners on the basis of those assessments if the s30B amendment is ineffective.

414. In my view, on the plain and natural meaning of the relevant provisions, Mr Goldberg's view is correct. Essentially, I agree with the comments on which the appellants relied in the case of *Albermarle* at [64] to [69] and do not need to add anything:

> "My starting point is that the interpretation the appellant seeks falls within the plain meaning of the words of s30B TMA 1970. This is not a situation where profits or income have not been included when they ought to be included, or where profits or income have been included which are or have become insufficient. Conversely the interpretation HMRC seeks departs from the ordinary meaning of the words "profit" and "income" so as to encompass negative amounts. Beyond asserting that the provisions may be read in that way, HMRC have not put forward reasons which persuade me that "profit" /"income" in the particular context of this provision should be read in that way. On the contrary the interpretation HMRC suggest appears to me to be at odds with the preceding provisions in TMA 1970 dealing with partnership returns and partnership statements which take care to specify whether amounts are net and which specifically mention losses in distinction to income.
>
> Section 12AA TMA 1970 which provides the basis for the partnership return refers in s12AA(1) to establishing the amount each partner is chargeable to income tax and then goes on in s12AA(1A) to specify that this is a net amount which take into account any relief or allowance for which a claim is made. Section 12AB TMA 1970 which requires the partnership return to include a partnership statement refers in s12AB(1)(a)(i) to the amount of "income or loss". Given the approach in these preceding provisions, if "profit" in s30B TMA 1970 were intended to cover negative amounts I would have expected the drafting to have dealt with this explicitly.
>
> The heading of s30B TMA "Amendment of partnership statement where loss of tax discovered", although only indicative, helpfully belies the purpose of the provision in my view. In contrast to the wider power of amendment to make corrections (under s12AB TMA 1970) the provision's purpose is to enable amendment where a loss of tax is discovered. That will clearly be the case where positive amounts of profits not been declared or are under-stated, or if reliefs or allowances are excessive. Given the underlying purpose I have

considered whether, if the appellant is correct and s30B TMA 1970 does not provide a statutory basis for the amendment, whether that result would undercut the purpose so significantly as to support HMRC's more expansive interpretation of "profit".

I do not think it does. If HMRC are correct that the loss is a property business loss and not a trading loss, it is not that fact by itself which means there is a tax loss but the fact of whether and to what extent a partner seeks to relieve the loss against other income. The issue of whether any tax loss would arise in this way if HMRC are correct, or the ability or otherwise for amendments to be made to the partners' personal returns is not before me. It is sufficient for the purposes of the issue before me to note that a conclusion that s30B TMA 1970 does not apply does not give rise to an obvious gap in the statutory provisions which, given its underlying purpose, cannot have been intended.

The appellant's argument that there is no statutory basis for the amendment accords with the plain words of the provisions in s30B TMA 1970, it is consistent with the drafting of other provisions where specific mention is made when losses are intended to be included, and it is not inconsistent with the underlying purpose of the provision. On that basis I agree s30B TMA 1970 does not apply so as provide a basis for HMRC's stated amendment. I do not therefore deal with Ms Yang's specific submissions made in reply to HMRC's arguments grateful though I was for them.

The amendment is ineffective and the appeal in relation to the amendment of the partnership statement for 2005-06 is therefore allowed."

Validity of assessments

Overview of submissions

415. It is well established that for the purposes of ss 29 and 30B it is for HMRC to demonstrate, to the usual standard of proof (on the balance of probabilities), that an officer of HMRC made a "discovery" of an insufficiency of tax and that the other relevant requirements are met, namely, s 29(5) and s 30B(6). On the basis of the recent caselaw such as *HMRC v Mr Raymond Tooth* [2018] UKUT 38 TCC ("*Tooth*"), for any discovery assessment to be validly issued pursuant to either of these sets of provisions, any such discovery must not have lost its "essential newness" or, as it is sometimes put, must not have become "stale" by the time the assessment in question was made.

416. The parties detailed submissions are set out below but in summary:

(1) In HMRC's view, they have satisfied the burden upon them to demonstrate that these requirements are satisfied in relation to the amendment and all of the discovery assessments the validity of which is disputed in this case. The evidence establishes that:

(a) Ms Frusher and Mr Blakely made the relevant discoveries as set out in Ms Frusher's and Mr Williams' evidence and that they plainly had not lost their essential newness when the amendment and assessments were made in March 2016, March 2017 and March 2018.

(b) There was plainly insufficient information and documents in the tax returns the individuals and/or Odey submitted and/or, in the case of Mr Fletcher and Mr Stewart in the information they provided during the course of HMRC's enquiry into their tax position in the 2011/12 year, for a hypothetical officer reasonably to be expected to be aware of the insufficiency of tax by the relevant deadline. The information made available needs to be sufficient to justify raising an assessment, not merely

to prompt further enquiries (see the summary of the law in *Beagles v HMRC* [2019] STC 54 ("*Beagles*") at [100(5) and (6)]).

(2) The appellants submitted that:

(a) The evidence indicates that an officer of HMRC made a discovery of an insufficiency of tax within the meaning of ss 29 and 30B in respect of all relevant tax returns probably as early as November 2013 but certainly before Ms Frusher, Mr Williams and Mr Blakely became involved in considering Odey's tax affairs and they made the relevant assessments. As the party with the burden of proof, it is for HMRC to bring evidence to refute this position but they have failed to do so. On the basis of recent cases such as *Tooth*, (i) there can only be one relevant discovery (an officer cannot discover something which another officer has already discovered,) and (ii) given the relevant discovery was made in November 2013, it had plainly lost its essential "newness" by the time all of the assessments were issued so that they were invalid.

(b) Even if the tribunal does not accept that a discovery was made in late 2013 (or sometime before Ms Frusher became involved), the only relevant discovery was made by Ms Frusher in early 2016 and that discovery had lost its essential "newness" by the time the discovery assessments issued in 2017 and 2018 were made.

(c) It is apparent that HMRC had a wealth of information about Partnership Incentive Plans and in particular about the Plan used by Odey well before the enquiry window for 2011/12 closed let alone the windows for 2012/13 and 2013/14. HMRC have not explained why, in the light of the information they had, the hypothetical officer could not reasonably be expected to know that there was an insufficiency of tax in the relevant returns by the time the enquiry window closed for each year. Ms Frusher was able to make the assessments in March 2016 without any further information than she had when she took the matter on. HMRC's failure to bring any further evidence on this issue means they have not satisfied the burden of proof.

Evidence and facts

Enquiry into the 2011/12 tax returns of Mr Stewart and Mr Fletcher

417. The bundles included the following correspondence relating to the enquiries which HMRC made into the tax returns of Mr Stewart and Mr Fletcher for the 2011/12 tax year:

(1) The letters in which Mr White of HMRC opened their enquiries into those returns dated 24 July 2013 and 30 July 2013 respectively. In the letters, Mr White asked each of Mr Stewart and Mr Fletcher (a) whether any portion of his allocated profit share from Odey was deferred until some future date and whether he was subject to any arrangements, as a member of Odey, such that he may receive allocation of capital from other members and, (b) if so, to provide further details of the arrangements and related documents.

(2) In relation to Mr Stewart:

(a) A letter dated 13 September 2013 from Mr Stewart's advisers to Mr White with which they enclosed Mr Stewart's replies to the letter of 24 July 2013. Mr Stewart gave the following responses to HMRC's enquiries:

(i) His allocated profit share was not deferred.

(ii) Odey operated a retention and incentivisation plan designed to incentivise and retain key members under which he was eligible to be considered for a discretionary reallocation of Special Capital by the directors of a corporate member of Odey, PSCL.

(iii) He stated that:

> "The Plan works by creating a pool of special capital that may, at the sole discretion of the directors of PSCL, be reallocated in the future to individual members provided that certain eligibility criteria are met…..
>
> After meeting its expenses and liability to corporation tax PSCL uses profits allocated to it by the LLP to contribute capital to the LLP. This special capital is used to acquire shares in investment funds managed by the Odey group or shares in [OHAG]…..OHAG is the ultimate parent company of the Odey Group."
>
> The nature of the investment assets held as special capital provide the individuals, who might be considered for a reallocation of capital, an economic interest in the funds managed by the Odey Group. The Plan is also intended to help meet the expectation of investors that fund managers will be rewarded over a period of time that is commensurate with the investors' own period of investment in the funds.
>
> Under the terms of the Plan, the Remuneration Committee of the LLP may make recommendations to the directors of PSCL that certain individual members should be considered for a future reallocation of capital. If the eligibility criteria are met, the directors of PSCL may at their discretion assign entitlement to part of the company's special capital account in the LLP to other members.
>
> Please note that none of the profits allocated to me by the LLP were deferred.
>
> After the end of each accounting period, [RemCom] determined how the LLP's profits are to be allocated to the members under the terms of the partnership agreement. Please note that I was not entitled to any amount in respect of the next, or any subsequent year."

(viii) He set out details of the Awards made to him in respect of the 2011/12 tax year and attached a copy of a letter dated 13 April 2012 from PSCL which provided details of the allocations under the Plan for 2011 and 2012. He explained that as he left Odey on 31 December 2012 he did not meet the criteria to be considered by the directors of PSCL for a potential reallocation of capital for 2012 in the form of shares in OHAG and was no longer eligible to be considered for a potential further reallocation of capital in the form of shares in OHAG for 2011. He also attached a copy of a letter dated 19 December 2012 which he received from Odey confirming the position when he left Odey.

(b) A letter dated 10 October 2013 from Mr White to Mr Stewart's advisers in which he asked for further information to be provided by 15 November 2013, namely, details of the arrangements under which the salary was deferred, the circumstances in which the potential entitlement

is lost and copies of any correspondence in connection with the initial provisional allocation.

(c) A letter dated 7 November 2013 from Mr Stewart's advisers to Mr White in response to his letter of 10 October 2013. The advisers made the following main points:

(i) The introduction of the Plan did not alter the mechanism whereby profits were allocated to members of Odey. As before, profits were allocated in full and no part was held back or deferred.

(ii) They set out again that the purpose of the plan was to retain and incentivise members with the same explanation as before of the arrangements. It was stated:

> "In no sense is profit deferred, although it can be said that any reallocation of special capital is deferred until such time as the directors of PSCL are satisfied that the eligibility criteria are met and choose to exercise their discretion to reallocate capital held by the company to an individual partner."

(iii) Mr Stewart was a partner in the LLP and not an employee and so never received salary. The partnership profits allocated to Mr Stewart were not deferred under the Plan.

(iv) "To be eligible for a reallocation of capital an individual must remain a member of Odey during the eligibility period. This is fundamental to the retention effect that the Plan is designed to have. Moreover, the directors of PSCL must exercise their discretion in favour of the individual."

(v) They repeated the information given previously regarding Mr Stewart's departure from Odey. They said that the letter dated 13 April 2012 confirmed to Mr Stewart that PSCL had received an initial recommendation from RemCom that he should be considered for a possible reallocation for 2012. The letter describes the terms under which PSCL would consider the initial recommendation and the eligibility period.

(d) A letter dated 20 December 2013 from Mr White to Mr Stewart's advisers noting he had issued a closure notice to Mr Stewart on that day and that he had no further questions in relation to Odey at this time.

(3) In relation to Mr Fletcher:

(a) A letter dated 30 July 2013 from Mr Raymer of HMRC to Mr Fletcher in which he noted that the High Net Worth Unit was dealing with his tax affairs. It appears Mr White was a member of this unit.

(b) A letter dated 20 September 2013 from Mr Fletcher's advisers to HMRC noting that their enquiries in relation to the Plan had been forwarded to Odey. They also enclosed responses to HMRC's enquiries in substantially the same form as those set out at (2)(a) above in relation to Mr Stewart. He set out details of the relevant awards made to him in a letter from PSCL dated 13 April 2012 providing details of the allocations under the Plan for 2011 and 2012.

(c) A letter dated 7 November 2013 from Mr White to Mr Fletcher in which he notified him that he had closed the enquiry and noted that he had not made any amendment to Mr Fletcher's tax return for the 2011/12 tax year.

418. The bundles also contained internal documents prepared by HMRC in relation to their enquiries into the tax returns of Mr Stewart and Mr Fletcher for the 2011/12 tax year:

(1) An undated document headed "HNWU [High Net Worth Unit] Enquiry Plan" stated to relate to HMRC's enquiry into Mr Stewart's tax return for the 2011/12. This included the following statement:

(a) Under the heading "Risk Area": "OAM LP Income".

(b) Under a heading "Summary of proposed response": "Check if [taxpayer] is a user of a deferred profit scheme. Risk lead by Steve Gannon (LBS) – feed outcome back".

(c) Under a heading "Key matters arising": "Customer has provided details of deferred profit scheme in use. Referred back to Steve Gannon (L&C) and provided with further questions to take forward".

(d) Under the heading "final conclusion": "No further risk areas identified from responses given to questions. Close risk."

(2) A similar undated document relating to Mr Fletcher in which Odey was again identified as a "Risk Area" and under the heading "Summary of proposed response" it was stated: "Potential user of deferred profit scheme. Risk being led by Mr Steve Gannon (LBS)".

(3) A note of a call from Mr Stewart to Mr White on 1 August 2013 in which Mr White noted that:

> "Stewart also stated that a deferral scheme was in use at Odey. The scheme was administered by Deloittes and Stewart had contacted them for details which he could pass to White. Stewart also advised he had recently resigned as a partner at Odey."

(4) A note which seemed to be a record of a call from Mr Fletcher's adviser to Mr White on 8 August 2013. Mr White noted that:

> "Advised that in response to the questions regarding the partnership income they were having to contact the agent for the partnership and duly it was going to take more time in which to provide a response…"

(5) A document dated 16 October 2013 which appeared to be a file note made by Mr White regarding Mr Fletcher in which he said:

> "Risk area satisfied:
>
> <u>OAM LLP</u>
>
> The risk area was taken forward on behalf of Steve Gannon, the CRM for OAM. The issues are being addressed through another Odey individual – therefore we do not need to ask further questions in relation to this risk.
>
> NFA required."

(6) A "HNWU [High Net Worth Unit] Settlement Report" relating to a settlement reached on 5 November 2013 in relation to Mr Fletcher:

(a) It was noted that: "OAM LLP issue" was:

> "taken forward with 2 individuals with OAM LLP, on behalf of Steve Gannon (L&C) [Large and Complex unit within the Business team] as a collaborative working issue. Both responses received were identical and further questions were asked of the other partner as he responded first and we have ongoing local risk issue. I do not propose to repeat this process with Fletcher

as it appears the local risks have been satisfied and I cannot justify drawing out the enquiry."

(b) In the summary, it was stated that:

"All identified risk areas have been addressed satisfactorily, therefore, I have no grounds in which to continue this enquiry and I propose to settle."

(7) A memo dated 5 November 2013 to Mr Raymer from Mr White regarding the enquiry into Mr Fletcher's return for the 2011/12 tax year. Again, Odey was identified as a risk area and Mr White made the same comment as in the above document. Mr White asked if Mr Raymer agreed to settling and closing the enquiry.

(8) Another file note dated 22 November 2013 relating to Mr Stewart in which under a heading "OAM LLP" Mr White recorded his discussion with another officer, Mr Jones, as follows:

"LW advised this risk was led by the Hedge Fund Team in Euston Tower.

The current state was that they had a similar case, which they were currently awaiting advice on from CTISA as to whether distributions from the deferral scheme were taxable in the hands of the recipient.

LW was concerned that all local issues had been settled - could he justify holding the case open any longer on the basis of advice from CTISA, which may or may not result in further risks?

LW advised he was not absolutely sure that the customer had received anything from the deferred profit scheme. An email from Steve Gannon on the Hedge Fund team had [intimated] that he may have, but had not confirmed that he absolutely had:

LW advised he was also concerned that he had taken the risk forward with another customer who was also a member of OAM LLP. With that case, once all of the local issues had been settled the case had been closed down.

MJ advised that due to the uncertainty regarding the customer's distributions from the scheme and that another LLP member had had his case settled swiftly upon resolution of the local issues we must be seen to be applying a fair and consistent approach,

Duly his view was to close the risk without awaiting the response from CTISA.

LW agreed this and advised he would close the case in its entirety.

Result: risk to be closed – nil."

(9) A memo dated 10 December 2013 relating to Mr Stewart in which Mr White said:

"In terms of the 11/12 ITR [tax return], we also find ourselves back at the position as per my file memo dated 22/11.13 [the memo referred to at [4].]

I will convey to the agent that the 11/12 enquiry will now be closed, with nil penalties charged…

Agreed by M Jones."

HMRC's internal documents relating to general enquiries

419. The bundles contained a number of documents indicating that prior to the involvement of Ms Frusher and Mr Williams, in addition to the specific enquiries into

Mr Stewart and Mr Fletcher, HMRC were concerned with the Plan on a more general basis.

420. In an email dated 11 September 2014 from Mr Winston Taylor of "LB Risk Task Force" to Mr Robert Page and Mr Paul Jackson, Mr Taylor enclosed a "CT risk assessment" relating to Odey dated 10 September 2014 for discussion the following week. Ms Frusher explained this Task Force is a separate team within the Large Business unit. Mr Taylor noted that an "EC risk assessment" would follow and requested the recipients to forward the email to the remaining members of the Odey case team. Ms Frusher explained that "EC" stands for "employment compliance". She did not know who was on the Odey case team at this time but said that it would have been made up of a customer relationship manager and individual tax specialists.

421. In the risk assessment dated 10 September 2014 referred to in the email of 11 September 2014:

(1) It was noted that Mr Steve Gannon's original risk assessment, a group structure chart prepared from information in the 2013 accounts and the partners' profit shares were attached.

(2) The following was stated under a heading "PSCL":

> "There is a PIP [Partnership Investment Plan] mark 1 corporate partner avoidance scheme whereby just over £6m has been allocated to special capital in the Period February 2011 to 5 April 2013. As SG [Mr Gannon] says, this has been confirmed by informal enquiries made by HNWU (on Stewart). If all the special capital has been reallocated to individual partners before FA 2014 bites the tax at risk is approximately £1.7 m which is relatively small beer given the amounts at risk elsewhere. Nevertheless, I recommend that enquiries are opened before the enquiry window closes at the start of October (given that we are still awaiting a handling strategy for these schemes)."

Ms Frusher thought that a handling strategy meant "a direction from a board such as, the anti-avoidance board, for cases where there are different customers who have similar planning arrangements, or similar issues, and it is more efficient to run the cases alongside one another and have a similar handling strategy for consistency in ensuring that people are not going down different directions…."

422. The risk assessment prepared by Mr Gannon which was referred to in the assessment of September 2014 was dated February 2013 although, from the information in it, it is likely the reference to 2013 is a typo and that it should be dated 2014 (in particular, I note that it is plain from this paper that Mr Gannon had seen Odey's accounts for the period ended on 5 April 2013). In this:

(1) There was reference to PSCL and a statement that:

> "It is clear from the accounts that this is a PIP using Special Capital. SC of £1.9m was acquired up to March 2012 and will presumably be allocated to other partners in the LLP in due course. This is the less objectionable version in that they are recording the gross income and paying tax at CT rate on the whole profit share. The profit allocation for the period to 31 March is £4.6m. We now have some information from HNWU on the workings of the scheme which confirms its nature (see separate pdf)…."

The pdf Mr Gannon referred to contained Mr Stewart's replies to the enquiries HMRC made into his return for the 2011/12 tax year.

(2) Under a heading "Summary of risks for all entities and further action needed", it was stated that:

> ".....Corporate partners – these have been put on the team potential list along with the other [redacted] and related issues.
>
> Individuals – copy of this risk assessment to HNWU [High Net Worth Unit] with covering memo highlighting issues found in relation to the individual partners (new corporates etc.)"

(3) The document contained a list of all the Members and their profit shares for the year ended 5 April 2013.

423. The bundles also contained an email dated 18 September 2014 from Mr Paul Jackson, a senior indirect tax specialist at the Large Business Service to Mr Nick Hagan relating to Odey. Ms Frusher explained that Mr Jackson later became the customer relationship manager for Odey and that Mr Hagan was the tax specialist who at this time was responsible for Odey within the Large Business Service. In this email Mr Jackson referred to gaining "access to the CAF" which, as Ms Frusher explained, is HMRC's electronic customer file to which an officer is given access only if he or she is working on the case. The email continued:

> "I went to a meeting yesterday morning which was organised by Bob and Winston about the TF risk assessment…...Winston went through his risk assessment which I attach if you had not seen it…Winston recommends that we open enquiries".
>
> [Below this under a heading "Summary of risks" there was reference to "Corporate partner avoidance – [PSCL]……
>
> I now realise that you should have been there, as your views would be valuable and you should be in the loop.
>
> The expiry window for Odey closes on the 7 October…..If you cannot issue the enquiries, can you suggest a colleague who could help?.."

424. Finally, the bundles contained an undated paper headed "Official – Sensitive" described as an "Anti-Avoidance Board – Technical Paper" ("**the 2014 technical paper**"). This included details of the type of planning undertaken by Odey and HMRC's views on its tax effects which, broadly, correspond to the arguments they raised in this case. Ms Frusher said that she thought that this was produced in the autumn of 2014.

Enquiries into Odey's partnership tax returns

425. The time limit for opening an enquiry into Odey's partnership tax return for the 2011/12 tax year expired on 25 July 2013 and no enquiry was opened into that year However, as Mr Jackson had requested, Mr Hagan opened enquiries into Odey's partnership tax returns for the 2012/13 and 2013/14 tax years on 6 October 2014 and 12 August 2015 respectively

426. In the letter of 6 October 2014, Mr Hagan asked for a copy of Odey's computation of profit for tax purposes and its profit and loss account to be provided by 30 November 2014.

427. In the letter of 12 August 2015, Mr Hagan asked for more detailed information to be provided by 31 October 2015 in relation to the 2013/14 tax year including:

(1) copies of (a) all documents relating to Odey such as the agreement governing it, (b) the Remuneration Policy, (c) notices to Members showing how the Plan was intended to work, (d) all documents concerning the profit allocations for 2013/14, (e) documents notifying the Members of their initial profit allocation, (f) any document whereby any limited partner subscribed for capital in Odey and documents concerning any such subscription, (g) documents

whereby any limited partner reallocated capital to the Members of Odey and documents concerning any such reallocation, (h) documents in which any Member was notified of the amount of capital to be reallocated, (i) any tax advice received by Odey or its members in connection with the plan and minutes of Odey in which the tax treatment of the Plan was explained or discussed, and (j) the investment management agreements for the Funds managed by Odey; and

(2) details of (a) the amounts and dates on which any subscriptions for and reallocations of capital were made by Odey both during and subsequent to the 2013/14 tax year, (b) by whom and by what process (i) the amount of capital to be reallocated to other Members of Odey and the recipients of reallocated capital was decided and (ii) the concept of the plan was introduced to Odey and its Members, (c) in each case, the commercial reasons for the introduction of each of the limited partners as members of Odey, (d) why each limited partner received a profit allocation and how the level of the profit share was determined, (e) whether Members were offered any alternatives to the Plan, and (f) whether Members had the option to say "no" to the Plan and whether any Members declined to participate.

428. Odey responded to the requests for information set out above on 29 September 2015. In the covering letter:

(1) Odey set out details of the commercial rationale for the Plan noting it was introduced to engage with the FSA's Code. Odey said it was compulsory for all Members other than Mr Odey and set out the thresholds for Cash Awards and noted that "Deferred amounts are on risk and since the inception of the Plan, three members have left and all forfeited their potential awards in full" (and Odey listed the Members and the relevant sums).

(2) Odey said they were not aware of any significant communication sent by email which had been omitted but that, whilst they had performed a preliminary check of their files for emails, they had not carried out a full scanning of their computer drives or a complete search of their paper files as they considered that would be unduly onerous and time consuming as HMRC's enquiries would be resolved by the completeness of their responses.

(3) Odey said that some of this information had been supplied to HMRC previously in the context of enquiries into two partners' individual returns which, so far as they were aware, were closed with no adjustments.

(4) Odey said that some of the information requested pertained to actions by PSCL and, in order to supply HMRC with any of their communications and internal documents, they had sought their written authorisation.

429. According to the list accompanying the letter, the documents which Odey sent to HMRC at this time included (a) copies of the 2011 LLP Agreement and related documents such as deed of adherence executed by Members and notices given when they left, (b) the Remuneration Policy dated 31 May 2011, (c) as regards the tax year 2013/14, minutes of RemCom meetings, notes from RemCom to ExCo, copies of letters from Odey to PSCL, board resolutions of PSCL including in relation to reallocations of Special Capital, letters from Odey to Members detailing their profit shares, letters from PSCL to Members regarding the reallocation of Special Capital, and (d) copies of investment management agreements between Odey and the Funds it manages. The various documents listed appear to comprise all those evidencing how the Plan was implemented in the 2013/14 tax year in line with the description of the processes used set out above.

430. The list also included an explanation of the commercial rational for the Plan (which in short form corresponds to that set out above) and of the role of PSCL which was described as "owned by a Business Purpose Trust with a fiduciary responsibility to act for the advancement and protection of the Odey Group". It was stated that:

> "The Remuneration Policy….details the process by which any profit share is deferred. The board of PSCL determine the reallocation of capital in accordance with their duties and the Remuneration Policy of [Odey] upon the satisfaction of certain commercial hurdles detailed in the Remuneration Policy."

Enquiry into Members' tax returns

431. As set out above, HMRC enquired into Mr Stewart's and Mr Fletcher's tax returns for the 2011/12 tax year. Otherwise HMRC did not make any relevant enquiry into the tax returns of the Members to whom discovery assessments were issued for that year or for 2012/13 or 2013/14.

432. Ms Frusher said that the deadline for HMRC to raise enquiries into the tax returns of the Members who participated in the planning in the 2012/13 tax year expired between 7 October 2014 and 31 January 2015 depending on when the particular Member had submitted his tax return to HMRC.

Ms Frusher's and Mr Williams' initial involvement and knowledge of prior investigations

433. Ms Frusher explained that when she joined HMRC in November 2015 as a member of Large Business Task Force she was allocated to the case team for Odey as the tax specialist and assigned to reviewing the Odey planning. She said that she and Mr Williams were both part of the large business taskforce who "come in where there is high risk cases, maybe there is a lot of tax attached to them or they have been under-resourced….and we are almost brought in to kind of accelerate the cases and move them forward".

434. Mr Williams explained that he lead HMRC's "Corporate Partner Avoidance" Project between October 2015 and June 2019. He said that the purpose of this project was to coordinate HMRC's approach to arrangements of the type entered into by Odey and PSCL. He had oversight of HMRC's enquiries into such arrangements and provided guidance and support to the tax specialists who worked on those enquiries.

435. Ms Frusher said in her witness statement that her understanding was that prior to Mr Hagan's involvement no other officer had undertaken a review of the arrangements. However, when questioned at the hearing she fully accepted that she had no knowledge of what others in HMRC had looked at in relation to Odey prior to her involvement in the matter:

(1) She was not sure who the Euston tower hedge fund team were who Mr White referred to in the documents set out above. She thought they were probably a team within the Large Business Unit. She did not know what information that team had in relation to this case.

(2) She did not know who was on the Odey case team in 2014 but thought it would have comprised a customer relationship manager and individual tax specialists.

(3) She did not know what work Mr Hagan did on the Odey enquiry or know how far the other people referred to in the documents set out above had got with looking into the planning before she became involved. She thought that, looking at the previous documents, Mr Gannon appeared to have undertaken a review of the accounts, but not of other information.

(4) She said that it was difficult to know if Mr Gannon would have known who the partners in Odey were; if he was the customer relationship manager, he would have probably met at least two or three partners in person at a meeting and HMRC would have a detailed list of all the partners which she assumed he could access.

436. Ms Frusher accepted that prior to her involvement HMRC's officers had identified risk in relation to the planning used by Odey, as she thought was clear from the risk assessment document. She said that she assumed Mr Hagan opened enquiries for the period 2012/13 and 2013/14 within the normal time limit because he saw that risk.

437. In re-examination she clarified that she thought that before her involvement HMRC had identified "potential risk" in:

> "identifying that something may or may not have happened, and then further work is needed to confirm that. You wouldn't necessarily start issuing enquiries or assessments on the basis of such limited information. What I know now is, having seen the plan documentation for Odey, seeing the tax advice and the further information which has been provided as part of the bundles, it is a much fuller view in terms of understanding how the plan formed part of the profit sharing arrangements….when I say "tax advice", I mean the one-page document that has been referred to, which I think has been prepared by EY or the partnership itself and shared with the partners around the time the arrangements were being implemented. It has the pros and cons listed at the bottom…."

438. Mr Williams confirmed that at one time Large Business did have staff at Euston Tower, but at a certain point they all moved to Bush House. He said there were "a number of overlapping teams in this picture". There was a team of tax specialists of which he thought Mr Gannon was one (although he had never met him), who were managed within Large Business, by Mr Steve Terry. He explained that that team asked for help from his taskforce in late 2015.

439. He said that the "Corporate Partner Avoidance Project", until his involvement, "was a fairly loose grouping of tax specialists within Steve Terry's team, who happened to be dealing with inquiries into arrangements of this sort. They met periodically to support each other, but it was quite informal and it was only really when he was appointed as project lead that it was formalised a bit more by the introduction of a project plan and a project manager. He thought there were around a dozen members of the team and that there had been four project managers across a four-year period.

440. He did not know precisely what Mr Hagan and Mr Gannon did. He had met Mr Hagan but did not know he was involved in this case until the hearing. Mr Hagan's involvement ended by the time Mr Williams came on board but he was aware what his duties are generally; as a tax specialist his function would have been similar to Ms Frusher's in conducting enquiries into partnerships. He had seen Mr Gannon's name on the papers but did not know him. He assumed Mr Gannon had a similar role to Mr Hagan.

441. Mr Williams confirmed that Mr Gannon had retired from HMRC and that Mr Hagan was still working for HMRC on a part time basis. He thought Mr Hagan could have been called to give evidence so far as he knew but he thought that Mr Hagan's involvement in the Odey case would have been at the very early stages of the inquiry. He said that, to the best of his knowledge, "the substance of the work" in this case, and certainly the making of the discovery assessments was done by Ms Frusher.

When questioned about this, however, he confirmed again that he did not know what Mr Hagan considered in relation to this case.

442. On 8 December 2015 Mr Jackson wrote to Mr Williams with a list of cases that his team could take over "to work the CPA enquiries", one of which was Odey. Against Odey's name it was stated: "Not worked. Initial documents require review". Mr Jackson then said that:

> "As you can see there is a mixture of the amount of work we have done, From Odey, that has not been reviewed at all, to [redacted name] where they claim to have given us everything that they can. 3 of the cases were worked by a TS before they left the team…"

443. When asked what the "not worked" and related comments meant in re-examination, Ms Frusher said that her understanding was that this meant that the response that was provided by Odey on 29 September 2015 had not been reviewed in particular by Mr Hagan as the tax specialist attached to the case before Ms Frusher; it meant that he had not worked the case any further from that point.

444. On 10 December 2015 Mr Williams emailed Mr Jackson confirming that Ms Frusher would look at the two cases where there are records to review one of which was Odey. He asked Mr Jackson to arrange for Ms Frusher to have access to the documents. Ms Frusher said that her mandate at this time was to review the information received from Odey on 29 September 2015 and advise how HMRC should take that forward.

445. In an email of 21 December 2015 Mr Paul Jackson wrote to Ms Frusher noting that his team had started the "PDFing" of the Odey documents and had worked their way up to six tabs on the folder. He asked her if she had access to the case file and said that, if not, he would arrange access.

446. Ms Frusher said that when she became involved she ascertained that HMRC had not raised any enquiry into Odey's partnership tax return for 2011/12 or into the individual tax returns of the Members who participated in the Plan in relation to that year. She noted that whilst Odey's partnership tax return showed a profit allocation to PSCL, there was no explanation in the return or the supporting documents of how the arrangements worked in practice.

447. When asked how she had found out that there were no enquiries into the 2011/12 tax year, she said that she had "read-only access" to HMRC's "Self-assessment software system" which records basic information for a tax year for an individual such as whether there is an enquiry open. She noted that the partnership tax return would also sit within that system. She could not say whether officers looking into Odey's tax affairs before she did would have had access to this system as an officer has to request access specifically:

> "Because Large Business focuses on corporate entities, you automatically get given access to corporate tax software…. The equivalent in the income tax field is the self-assessment system. Again, it is automatically given to colleagues dealing with self-assessment returns on a daily basis. So, I requested that access, and was given it. I don't know whether other tax inspectors within large business would have done the same thing although they could have done."

448. Ms Frusher said that having gone through all of the material set out above she felt that, when she carried out her review in 2015/2016, she did not have all the information held within HMRC that she might have had. Some of these documents she only saw for the first time at the hearing.

Further information requests

449. On 17 February 2016 Ms Frusher asked Odey for further information and documents:

(1) She noted that she had reviewed the documents provided in respect of the 2013/14 tax year and required further information in respect of the 2012/13 tax year in order to gain a better understanding of the Plan. For that year she asked for copies of documents in which (i) the profit allocations for that period were discussed, described or agreed, (ii) members were notified of the profit allocations, (iii) any limited partner subscribed for capital, (iv) any subscription by a limited partner for capital or any reallocation of capital to other members was set out, and (v) members were notified of any reallocation and the amounts of, and (b) the amounts in which and dates on which any subscription for and reallocations of capital were made.

(2) In relation to the tax year 2013/14 she:

(a) Asked for copies of any capital call agreements, side agreements, conditions or understandings outside of the LLP Agreement in respect of the profit allocations received by members.

(b) She asked for Odey to carry out a wider check for all relevant email correspondence.

(c) She noted that Odey had advised that some of the information previously requested required the written authorisation of PSCL and said that HMRC assumed that this confirmation had now been received and the relevant documents could be provided.

(d) She asked for tax advice received by Odey in relation to the Plan, copies of all communications, documentation, presentations or other written notices provided to any member showing how the Plan was to work (in addition to the Remuneration Policy which had already been provided) and copies of any documents and communications in which the tax treatment of the Plan was discussed.

(3) Ms Frusher also asked for (a) further details with supporting documents of PSCL's activities in the 2012/13 and 2013/14 tax years, (b) a description of what other checks and measures the directors of PSCL undertook in terms of the performance of the individuals other than the recommendations made by RemCom, (c) copies of any correspondence with the Members in respect of their performance, (d) copies of any supporting documentation (including emails) where Special Capital awards are described, discussed or agreed by the directors of PSCL, (e) details of whether there had been any circumstances where the directors of PSCL decided not to follow a recommendation from RemCom or under which rewards had not been paid (other than as regards Members leaving Odey), (f) for the tax years 2012/13 and 2013/14, a breakdown of each Member's Special Capital account detailing the dates of the reallocations and withdrawals, copies of the notices from PSCL to ExCo of the decision to reallocate Special Capital, and copies of the vesting schedules as referred to in PSCL's board minutes, (g) details of the treatment of any Special Capital not paid to member in line with the recommendations of RemCom, (j) confirmation of whether PSCL has operated its own bank account, a copy of the trust deed of the trust which owed PSCL and other related trust documents, details of the group's intentions for PSCL in future accounting periods and what PSCL intended to do with the remaining special capital of £7.9 million as at 5 April 2015, and (k) details of on what terms Members profit shares have been

deferred in the accounting period ending on 5 April 2015 if PSCL had not been used as part of the deferral process.

450. Prior to sending the above information requests to Odey, on 27 January 2016 Ms Frusher had sent an email to Mr Jackson with a draft of the letter to Odey. She said that a lot of basic information was still to be provided such as tax advice, documents where tax treatment is discussed and email communications. She added that she thought "they had done a fairly good job of implementing the EY planning, and have documented each stage accordingly but there is a distinct lack of evidence of any real review of the special capital awards/individual performance by the corporate vehicle and its directors. There appears to be no deviation from the LLP recommendation". She queried whether an enquiry should be opened into the 2015 period and the 2011/12 tax year.

Asserted discovery in February 2016 and issue of discovery amendment

451. Ms Frusher said that in February 2016, from the information which had then been provided by Odey, she came to the view that, on a realistic view of the facts, the profits which were apparently allocated to PSCL were intended to be and were in fact allocated to the relevant Members who participated in the Plan. As regards the information which Odey provided to HMRC in September 2015, she noted that:

(1) Odey stated that whilst PSCL considered recommendations by RemCom in respect of the allocation of Special Capital to individuals, PSCL retained absolute discretion as to whether it should be reallocated.

(2) The documents showed that Mr Odey was a member of RemCom and a director of PSCL and so responsible for evaluating a member's performance and exercising discretion as to whether Special Capital would be paid to a member.

(3) There was limited evidence of a review process by either RemCom or PSCL whereby a partner's performance was discussed in connection with the payment of future awards of Special Capital. For example, the minutes of RemCom noted that Line Managers and ExCo "had been consulted extensively over recent weeks" but evidence of this consultation was not included with the minutes nor linked back to whether an award would be paid based on an individual's performance.

(4) No other evidence was provided of PSCL's discretion to award Special Capital.

452. It appeared to her that subject to Members remaining as such the anticipated result of the arrangements was that the deferred profit share allocations would ultimately end up as the income of the Members. Her conclusions were based on and limited to the documentation provided by Odey on 29 September 2015.

453. On 22 March 2016:

(1) Ms Frusher made a discovery amendment to Odey's partnership tax return in respect of the tax year 2011/12 which she said was to give effect to her view that the profits allocated to the relevant Members in respect of that year were understated by a sum equal to the total profits Odey had shown in the return as allocated to PSCL. She considered that the right way to proceed was to correct the position at the partnership level by making amendments to Odey's tax return under s 30B.

(2) She also wrote to the Members notifying them she would shortly issue discovery assessments to them in respect of the 2011/12 tax year (as she did at the end of March/early April). In the covering letters she said that she considered the individual's tax returns to be inaccurate and:

> "HMRC believes that the allocations of profit made by [Odey] to [PSCL], which are subsequently distributed to members of [Odey] in the form of capital, should be treated as allocations of profit to the individual members and be chargeable to income tax.
>
> If contrary to HMRC's view, PSCL is found to be entitled to receive the share of [Odey's] profits, then the reallocation of sums by way of special capital to an individual member would be considered to be the income of the individual member. This is because amounts received are rewards for services to the partnership, and as a result are taxable as income.
>
> It is necessary to issue assessments to protect HMRC's position and to prevent the loss of tax. The amount of income tax will be based on a percentage of the total unit shares and bonus shares awarded in respect of the "2012 allocation". This percentage will be applied to profit share allocated to PSCL in the [Odey] partnership statement in the year ended 5 April 2012…..
>
> At the time when I was able to enquire into your tax returns for 2011/12 I was not aware of the situation which gave rise to the loss of tax. The assessment is therefore being raised under s 29(1) TMA 1970 to make good to the crown the loss of tax."

454. Ms Frusher said in her witness statement that she considered that, on her review of the documents, she had ascertained that it was HMRC's primary position that any changes to the allocations of Odey's partnership profits should be dealt with at partnership level under s 30B. She said that the basis of assessing the Members directly, as an alternative position and/or in case the approach of using s 30B was incorrect, was only considered by HMRC in February or March 2016 after advice was sought from HMRC's technical experts. There were also discussions with HMRC technical specialists at this stage, with regards to concerns raised by other customers operating similar arrangements as to whether a valid amendment could be made to the partnership return under section 30B. HMRC specialists advised that an assessment under s 29 would also be appropriate in light of these contentions and this approach was adopted across all of the cases involving these arrangements. She issued discovery assessments to the relevant Members following the receipt of this advice.

455. When it was put to her that that this advice was available to HMRC in autumn 2014 in the 2014 technical paper (see [424]) she said the following:

> "My reading of the anti-avoidance board document….is it sets out HMRC's primary challenge, which is the section 850 argument, and then the alternative analysis is the miscellaneous argument……in terms of when the Special Capital comes out to the members and what the tax treatment of that is.
>
> In my witness statement, what I'm trying to say…..is in February 2016 and March 2016, it was flagged to our team - first, that Colin Williams, who shared this information with the tax specialists, that under section 30B, on the plain reading of it, we potentially have a problem because we are not looking to increase profits to any individual party, we just want to share them differently across the partners in terms of how we think the tax treatment should be.
>
> So, a customer had raised a contention saying, on the plain reading of section 30B, it doesn't look like you can do that. So, in the alternative, we did assessments on the individual partners under section 29. Just in case section 30B didn't work, we would fall back on to section 29. The advice of our specialists is that section 30B should work, but it was kind of a belt-and-braces position to adopt. But also you could say the assessments for 11/12 would cover the miscellaneous secondary argument position, although I

> think, from memory at this point, there isn't any Special Capital being paid to members that early on in the arrangements…..
>
> We knew in 2014 we would put alternative challenges under the miscellaneous arguments. To my knowledge, we didn't know in autumn 14 about the potential issues with section 30B, and why we might need section 29 instead, if on the plain reading of 30B that we couldn't amend the allocations between the partners…..".

456. It was put to Ms Frusher that she must have known in 2016 that she would need to use s 29 or open an enquiry to impose the miscellaneous income charge; that could not have been done by s 30B. She said that she did not know if that was necessary because at that stage there may have not been Special Capital coming out to the Members.

Provision of further information

457. Odey replied to Ms Frusher's letter of 17 February 2016 on 12 April 2016 although, in her view, "very little" additional information was provided. In that letter, Odey set out that they intended to focus for the time being on the documents and information required for the 2013/14 tax year in relation to which, in Odey's view, Odey had already provided a significant amount of information. The reasons they gave for their approach included that:

(1) The documents for the 2012/13 tax year would be substantially the same as those for the 2013/14 tax year which they had already provided except that, for example, the quantum would be different. They said that they had provided a detailed summary of the amounts of Special Capital reallocated to Members for the 2012/13 and 2013/14 tax year.

(2) HMRC appeared still to be reviewing the documents already provided and once they had provided a view of that it may not be necessary to provide documents for the earlier year.

(3) They understood that in discussions with Ernst & Young, Mr Williams had indicated that he agreed this was a sensible approach.

(4) They had provided responses to new questions that were not included in the letter of 12 August 2015.

(5) They had already provided documents and information in relation to PSCL to the extent they had received authorisation from it to do so; Odey was not in a position to provide any further detail as it had no legal nexus over the affairs of PSCL as it is a separate legal entity.

458. On 22 June 2016, Ms Frusher wrote to Odey again requesting Odey to provide the outstanding information and documents by 29 July 2016. She said that HMRC:

> "believe that the allocations of profit made by [Odey] to [PSCL], which have been subsequently distributed to members of [Odey] purportedly as capital, ought to be treated as allocations of profit to individual members and chargeable to income tax. As such, it is important for HMRC to understand the full facts relating to the Plan, before reaching a decision on the appropriate tax treatment."

459. In that letter, her comments regarding the information/documents requested from Odey, include that (a) although the documents relating to the 2012/13 tax year may be substantially similar to those already provided by Odey for the 2013/14 year, she considered they were reasonably required as they related to a different accounting period, (b) the tax advice was needed as it was important to the issue of whether the Plan formed part of the profit sharing arrangements and to whether s 773 ITA applied.

The information request included with the letter included a new request for details of the specific roles and activities of the Members who had participated in the Plan.

460. On 22 June 2016 Ms Frusher also wrote to PSCL asking for information to be provided by 29 July 2016:

(1) She noted that HMRC were aware from their correspondence with Odey that recommendations were made by RemCom to PSCL in respect of profit allocations to individuals participating in the Plan. She asked for details of what other reviews the directors of PSCL had undertaken in terms of the performance of the individuals and for copies of all relevant documents in that respect.

(2) She asked for copies of any documents relating to capital awards and tax advice received by PSCL in relation to the Plan, copies of notices from PSCL to ExCo of the decision to reallocate Special Capital to Members for the tax year 2013/14, further details of the intention of the directors of PSCL in respect of the £7.9 million of Special Capital remaining within PSCL as at 5 April 2015 and any other information or documents connected to the Plan which would assist in HMRC's understanding of how the Plan operated.

461. On 8 July 2016, Odey replied stating that they considered they had already complied with many of HMRC's requests and that they thought it had been agreed at a meeting between Mr Williams and Ernst & Young that until such time as HMRC were in a position to present the substantive issues of their enquiry and related technical support that no further such information requests would be made. They said they understood that a further meeting was to take place between HMRC and Ernst & Young on 19 July 2016 to discuss these issues and they proposed to await the outcome of the meeting to determine what if any further information was required.

462. Ms Frusher replied on 12 July 2016 asking for confirmation that Ernst & Young was acting for Odey and, if so, for the required form authorising Ernst & Young to act as their agent. She said that if she received this and Odey agreed to abide by any agreements arising from HMRC's discussions with Ernst & Young on this matter, she was able to allow an extension to the deadline for providing the outstanding information to 31 August 2016.

463. On 29 July 2016 Mr Jackson of HMRC notified Odey that HMRC "were content to let the deadline slip" for the provision of information essentially in light of the ongoing discussions with Ernst & Young.

464. Odey did not provide any further information on the arrangements during 2016. Ms Frusher thought that discussions at that time centred on whether Odey would be included in Ernst &Young's "project plan" whereby they proposed to act as a single point of contact with HMRC in relation to a number of taxpayers who had used similar arrangements to the Plan. On 9 November 2016, Ernst & Young confirmed that Odey had agreed to this approach and meetings with HMRC were then arranged for 1 February 2017.

465. On 4 January 2017 Ms Frusher wrote to Odey setting out HMRC's summary of the facts as they understood them and HMRC's views on the correct tax treatment which, in summarised form, corresponds to the arguments put forward at the hearing. She asked for the outstanding information and documents to be provided by 1 February 2017. She also wrote to PSCL at the same time asking for the outstanding information requests to be dealt with by 1 February 2017. She wrote to them again on 19 May 2017 asking for the information to be provided by 31 May 2017.

466. Odey responded at some length on 27 January 2017 and made various corrections to the facts set out by HMRC. The notes of the meeting with HMRC on 1

February 2017 show that Odey provided detailed information on how the Plan was intended to work. Odey provided further information and documents between May to September 2017.

467. Ms Frusher said that the corrections made by Odey to HMRC's summary of the facts and the explanations they gave at the meeting in February 2017 provided some further background detail of the Plan but did not change her view. She added that the limited further information provided in 2016 or early 2017 did not change her view that the profits allocated to PSCL were in fact taxable as income of the relevant Members or that the alternative position applied.

Issue of assessments in March 2017

468. Ms Frusher raised assessments on the relevant Members for the 2012/13 tax year at the end of March 2017 in respect of sums received on the reallocation of Special Capital made to Members in that tax year. She said in her witness statement that she did not make the assessments until this time because:

(1) Although at this time her view of the correct tax position remained as set out above and she felt Odey were not cooperative with her requests for information during 2016 she felt that it was important to remake the requests for information to be provided and give Odey time to comply before making the further assessments.

(2) She also wanted to give time for a more open dialogue with Odey that was possible only once they confirmed they were taking part in the Ernst &Young "project plan".

469. These assessments were made by another officer at HMRC on Ms Frusher's instructions. She explained that she made the assessment in terms of the figures contained in them, and she instructed colleagues in the High Net Worth Unit that she wanted these assessments to be made. It was considered to be more appropriate to issue the assessments through the taxpayers' normal point of contact.

470. When asked at the hearing for a further explanation, Ms Frusher said that there was a delay as at the time she was still trying to obtain information from Odey before she made any further assessments and she was obviously, mindful of the time limits. She said that she would not have raised assessments for 2012/13 when she was still information-gathering and still trying to open a dialogue with Odey and that she had issued the discovery assessments for 2011/2012 because she was coming up against a time limit.

471. When asked whether she had made a discovery when she issued the assessments for 2011/12 she said: "I made a discovery based on the information I had available, which formed my initial view, and I made a discovery for 11/12 on that basis".

472. When asked why she did not at that time make a discovery in respect of the 2012/13 tax year, she said:

> "because I wanted to get the outstanding information….to further develop that view. There were key pieces of information outstanding from the partnership in terms of the tax advice they'd received. I was pushing for evidence of the review process because this wasn't evident in the company minutes or the remuneration committee minutes. They were very thin in terms of detail and understanding to what extent PSCL applied its discretion in paying those awards out to individuals two years down the line, and I wanted to use the time in 2016 to obtain that information from the partnership, which is why I entered into the correspondence that I did."

473. It was put to her that she did not need the information she referred to make a discovery. She said that:

> "in terms of looking at the alternative arguments, the Special Capital amounts coming out and also the s 773 argument, sales of occupational income, looking at the purpose of the arrangements in terms of if there is a tax motivation, that is a key piece of information. We would always try, you know, to keep having a conversation with a customer to get information. And as you see in early 2017, we actually had a face-to-face meeting for them for the first time and there was a possibility they may have chosen to settle with us and we would not issue assessments before that if we were in a good time window, which may have been detrimental to those conversations."

474. She was not sure when HMRC first became aware of planning such as that undertaken by Odey but she thought it was around 2012. It was put to her that a submission was made in the *BlueCres*t case, in which she also gave evidence for HMRC, as set out at [30] of the decision in that case, that in the appellant's view HMRC's analysis had remained, essentially, static since 2013 in the case of planning of the type Odey entered into. She confirmed that in that case HMRC had accepted that was the case. She was asked why they did not accept that in this case. She said:

> "The BlueCrest arrangements…..were implemented quite a few years before some of the arrangements we were looking at, including [Odey]. Whilst there is a common theme across these arrangements, they are all very, very fact dependent. So, in the anti-avoidance box handling document from 2014, that obviously identifies what the main challenges could be, but it was very much about going out and finding the evidence and facts to support those challenges we were going to make and having those conversations with the customers."

475. Ms Frusher said in re-examination that she probably read the 2014 technical paper in early 2016. When asked why she did not make the assessments of all the individuals at that time, she said:

> "Because I made the 11/12 assessments, as I said, because I was coming up to a time limit, so it was important that I did do that. In terms of the secondary arguments, understanding the purposes of the planning - one of those being the tax purpose - is important, so obtaining any tax advice documents which I didn't have in early 2016, I don't think I obtained until summer of 2017. That's why I wouldn't have done all of the assessments in one go at that time.
>
> I wouldn't have also had information on what Special Capital amounts had been paid to individuals. The first assessments done in 11/12 were very much estimates based on the information we had."

476. She was asked what is involved in forming a view, in respect of an individual Member's potential assessment, as opposed to the partnership as a whole. She said:

> "I would have looked to see what amounts they were allocated per the award letters; I would want to see the potential review process that may have been attached to them via the company minutes; where they weren't available, I asked for other correspondence, emails, et cetera, which I was never given; and I would have looked at the individual's tax return to see if they made any specific disclosure in terms of these arrangements, and perhaps what their analysis was. I think as well going back to the tax advice point, seeing that documentation and seeing from a partner's perspective when these arrangements started, what they would have seen entering into those arrangements and what their understanding would have been."

477. There was the following further main correspondence in 2017 and early 2018:

(1) On 31 March 2017, Odey wrote to HMRC stating that it was taking longer than they had anticipated to compile the outstanding documents and information requested by HMRC.

(2) On 10 May, Ms Frusher replied stating that this should be provided no later than 31 May 2017.

(3) Odey provided some of the requested items on 12 May 2017 including the documentation requested for the 2012/13 tax year.

(4) On 15 June, Ms Frusher wrote to Odey reiterating the request for email correspondence and further details of the particular roles and activities of individual Members who had participated in the Plan for the purposes of determining if the Sales of Occupation income legislation applies.

(5) On 14 July 2017, HMRC wrote to Odey with their final view of the Plan.

(6) On 15 September 2017, Odey provided further outstanding items.

(7) On 19 September 2017, Ms Frusher sent Odey closure notices for the enquiries into its partnership tax returns for the tax years 2012/13 and 2013/14 and made amendments to those returns by reducing the profits allocated to PSCL and increasing those allocated to the relevant Members.

(8) On 24 October 2017, Ms Frusher wrote to Odey offering a review of HMRC's decision in respect of these years under s 49C TMA. Odey accepted this offer in a letter of 20 November 2017 and HMRC notified them of the outcome of the review on 18 January 2018.

Issue of assessments for 2013/14

478. Mr Williams explained that:

(1) When, in early November 2017, Ms Frusher began a period of maternity leave, he initially asked Mr Nick Haynes to assume temporary responsibility for Odey as a tax specialist but in late November 2017 Mr Ben Blakely was appointed to this role.

(2) Around this time, Odey took up HMRC's offer of a statutory review (as set out above) and Mr Blakely's immediate task was to prepare a submission for HMRC's Review Team. Mr Williams supported him in this, offering advice and ultimately authorising the submission.

(3) In January 2018 Mr Blakely organised the making of enquiries into individual partners' tax returns for 2015/16, where those were required. Again, Mr Williams supported and advised him in this task.

(4) On 13 February 2018 Mr Williams asked Mr Blakely to consider whether discovery assessments were required for the year ended 5 April 2014. In the email to Mr Blakely he said: "Please could you check whether discovery assessments are required to protect the miscellaneous income argument?" Mr Williams said that this request was prompted by an e-mail he received from Mr John Deuchars who was responsible for coordinating Wealthy and Mid-sized Business's activity on the Corporate Partner Avoidance project. Whilst he could not be certain he thought it likely that the analysis Mr Blakely produced which appeared to be dated 20 February 2018 was prepared in response to his e-mail of 13 February. This comprises a spreadsheet which set out reallocations of Special Capital to the relevant Members of Odey in the 2013/14 tax year.

(5) On 13 March 2018, a meeting of the Corporate Partner Avoidance Project took place to consider, amongst other things, "discovery assessments", with Mr Williams listed as the responsible person. At that meeting he asked the Tax

Specialists to consider whether discovery assessments were required for the year ended 5 April 2013 for cases within the project. Later that day Mr Blakely e-mailed him twice, at 16.26 pm and 16.40pm, with queries about the preparation of the assessments and it appears tried to call him.

(6) He did not recall speaking to Mr Blakely on the morning of 14 March 2018 but it seems likely that he did, both from the nature of his response and from the fact that Mr Blakely e-mailed Mr Nick Griffiths with instructions to prepare the assessments at 11.31am on that day. Mr Griffiths is an officer of HMRC, working in the Individuals and Small Business Compliance Directorate. He and his team did much of the work in preparing notices of assessment for the Corporate Partner Avoidance project, under the direction of the relevant Tax Specialist.

(7) In an email sent at 11.31am on 14 March 2018, Mr Blakely enclosed a spreadsheet with the details to be assessed. As shown in emails of 16 March 2018 Mr Griffiths provided sample letters and calculations, which were agreed by Mr Blakely.

(8) The assessment for Mr Al-Chalabi was issued by HMRC's Wealthy and Mid-sized Business Compliance Directorate. Between 15 March and 19 March 2018 there was an e-mail exchange between Mr Griffiths and two officers from that directorate to arrange for the notice of that assessment to be issued in Mr Blakely's name.

(9) There was also email correspondence between Mr Blakely and Mr Deuchars in which Mr Deuchars asked for instructions as to whether assessments are required for certain individuals and Mr Blakely responded that no assessments are required.

479. At the hearing, Mr Williams confirmed that he did not make any of the assessments in this case. Mr Blakely made the relevant assessments but was on a career break at the time of the hearing. He understood that Mr Blakely made a discovery of an insufficiency of tax in relation to the relevant individuals' tax returns for the 2013/14 tax year in March 2018. When asked what he discovered, he said "that the assessments for the particular individuals for that year were insufficient. He reached that conclusion". When asked why he asked Mr Blakely to consider whether discovery assessments were required, he said:

> "It was my custom to raise this with the tax specialists each year, so obviously I would be aware that there was an assessing time limit coming up. But in this case, I think I had actually forgotten about it, and….I was prompted when I received an email from John Deuchars [in February 2018], asking me whether assessments were required."

480. It was put to him that, in effect, he asked Mr Blakely whether assessments were needed because s 9A inquiries had not been opened. He said:

> "No. What I would expect somebody to do in those circumstances is to consider a number of things. One is certainly that, whether assessments were required. I would also expect them to consider - given in this case the assessments were in relation to the miscellaneous income argument, I would have expected Ben to consider whether the individuals had, in that year, received any allocations which could have potentially been subject to that assessment. I would have expected him to consider what disclosures had been made so that, you know, to judge whether or not he was entitled to make a discovery assessment; and I would also expect him to consider whether any amounts had been returned as taxable income."

481. It was put to him that the wording in his email of 13 February 2013 does not seem to constitute a request for Mr Blakely to consider whether there was an insufficiency of tax. He said that was how he intended it. It was put to him that his request was capable of meaning that the insufficiency of tax was taken for granted, and the question for Mr Blakely was whether action was needed to remedy it. He said that he could see that the email could be read that way, but it is certainly not what he intended.

482. He did not know in detail what Mr Blakely did when he received the email. He referred to the spreadsheet in the bundles which set out reallocations of Special Capital to the relevant members in the 2013/14 tax year which he assumed was considered by Mr Blakely. The date on the spreadsheet appeared to state 20 February 2016 but Mr Williams could not confirm when HMRC received this information. He did not know when this spreadsheet was produced or who had considered it before Mr Blakely.

483. It was put to him that Mr Blakely might have discovered that no assessment had yet been issued and that somebody else might have already thought there was an insufficiency of tax. He said that was possible but he had seen no evidence of it. It was put to him that Ms Frusher would have thought there was an insufficiency if she had looked at this. He said that was possible but noted he could not say what she would have thought. He agreed that if she had carried out the same "exercise", he would have expected her to come up to the same conclusion.

484. In re-examination he was asked what "exercise" he meant. He said:

> "the exercise of looking at the tax returns and then considering, partly, whether there was an inquiry, so an assessment might be required; whether the individual had received any sums of money that could be regarded as miscellaneous income; whether there are any notes on the tax return that would have constituted a disclosure that prevented a discovery assessment; and whether the individual had returned that what we say is income as taxable income…. It has happened in other cases within the project, that people have regarded the amounts -- have included the sums they received as special capital coming out that they have actually included it in their tax returns as taxable income".

485. In re-examination Mr Williams was asked what the phrase "Not worked. Initial documents require review" meant or signified in the email of 8 December 2015 sent to him by Mr Jackson of HMRC (see [414]). He said:

> "as Ms Frusher indicated, one of the reasons that the Taskforce was brought in was because of resource pressures. London Financials, as it then was, were unable to work all of these cases as quickly as was desirable, so these are - there were a number of cases where documents had been received where the tax specialists allocated to them had either moved on, or were simply not able to devote the resource to them, and therefore the additional resource was brought in. I was brought in to run the project; with me I brought in certain tax specialists, of which Ms Frusher was one, and the project manager, et cetera, to add that additional resource."

486. In re-examination he was asked to explain why he said "the substance of the work" was done later by Ms Frusher. He said:

> "I was involved from October 2015, when I became project lead for this project. At that time, my role was to provide advice and support to the tax specialists working on the project, and to oversee the inquiries. So, whilst I wouldn't have known the detail of each inquiry, I would have a general feeling for how the inquiries were progressing, and I am aware that pretty much all of them were at fairly early stages of information gathering. Most of

the making of technical arguments, for instance, the technical decisions, took place at meetings. As we heard from Ms Frusher, the meeting in this case took place in 2017. I attended that meeting.

So, that's when, having finished the information gathering, or at least partially gathered the information, we would have the sort of discussions about how the law applied to the facts of this case. Most of that took place after my involvement, and therefore after Ms Frusher's involvement."

When was a discovery made and did it become stale?

487. There have been a number of cases in the last few years in which the courts have considered the concept of "discovery" and accepted that a discovery may lose its essential "newness" with the result that the assessment subsequently issued is invalid. In 2012, the UT adopted that approach *Charlton v Revenue and Customers Commissioners* [2012] UKUT 770 (TCC) ("*Charlton*") and, more recently, it has been followed by the UT in *Tooth* and subsequently by the Court of Appeal (*HMRC v Tooth* [2019] EWCA Civ 826) and by the UT in *Beagles* and *Mr Richard Atherton v HMRC* [2019] UKUT 41 (TCC).

488. In *Charlton*, the UT held that a discovery requires a threshold to be crossed; that is, from the position of not knowing to the position of having reason to believe. In doing so they considered the judgment of the Court of Appeal in *Hankinson v Revenue and Customs Commissioners* [2012] STC 485 where Lewison LJ traced the provisions of s 29(1). The UT noted the following, at [21]:

> "He referred (at [15]) to the fact that the word "discovers" in this context has a long history, and that, even though the conditions under which a discovery assessment may be made have been tightened following the introduction of self assessment, nevertheless the meaning of the word "discovers" has not changed. Thus, in *R v Commissioners for the General Purposes of Income Tax for Kensington*, *ex parte Aramayo* 6 TC 279 at 283, Bray J said that it meant "comes to any conclusion from the examination he makes and from any information he may choose to receive" and Lush J said that it was equivalent to "finds" or "satisfies himself". Lord Justice Lewison then continued:
>
> > "*In Cenlon Finance Co Ltd v Ellwood (Inspector of Taxes)* (1962) 40 TC 176, [1962] AC 782, the House of Lords considered the meaning of the word 'discovers'. They rejected the argument that a discovery entailed the ascertainment of a new fact. Viscount Simonds said ((1962) 40 TC 176 at 204, [1962] AC 782 at 794):
> >
> > > 'I can see no reason for saying that a discovery of undercharge can only arise where a new fact has been discovered. The words are apt to include any case in which for any reason it newly appears that the taxpayer has been undercharged and the context supports rather than detracts from this interpretation.'"

489. The UT noted, at [24], that in the decision in *Aramayo* to which Lewison LJ referred, Bray J found that "discovers" cannot mean to ascertain by legal evidence. But, they said:

> "it is nevertheless the case that an officer's discovery must be a reasonable conclusion from the evidence available to him. To that extent, although the test in s 29(1) is a subjective test, an element of objectivity is introduced in examining the reasonableness of the officer's conclusion (see *R v Commissioners of Taxes for St Giles and St George, Bloomsbury, ex parte Hooper* [1915] 3 KB 768, at 782)."

490. They set out, at [27], that the taxpayer referred to what Lord Denning had said in *Cenlon Finance* (which Lewison LJ had also referred to) at 799, namely that "if a lawyer reads his text book and realises he was mistaken about the law he will make a discovery". The taxpayer accepted:

> "that the threshold is crossed when the lawyer learns a new point of law. However, if the same lawyer, having fully considered the matter and having reached a conclusion, then thinks about the matter further and (without the benefit of further research into the facts or the law) simply changes his mind, then Mr Gordon says that this is not a discovery that his first conclusion was wrong; it is merely a change of opinion."

491. At [28], they concluded that they agreed with the taxpayer that the word "discovers":

> "does connote change, in the sense of a threshold being crossed. At one point an officer is not of the view that there is an insufficiency such that an assessment ought to be raised, and at another he is of that view. That is the only threshold that has to be crossed. We do not agree that the lawyer, in Lord Denning's example, would be regarded as having made discovery any the less by waking up one morning with a different conclusion from the one he had earlier reached, than if he had changed his mind with the benefit of further research. It is, we think, evident that the relevant threshold for there to be a discovery may be crossed as a result of a "eureka" moment just as much as by painstaking research. There must be something new."

492. At [29], they said that the mere fact that a threshold must be crossed does not mean that something more than a change of opinion is required. At [30], they noted that in *Cenlon Finance*, Viscount Simmonds considered the following comment by Lord Norman in *IRC v Mackinlay's Trustees* 22 TC 305 (at page 312) was correct:

> "I do not think it is stretching the word "discovers" to hold that it covers the finding out that an error in law has been committed in the first assessment, when it is desired to correct that by an additional assessment."

493. They referred also, at [32], to what Lord Normand had said in *Mackinlay's Trustees* (at 311 and 313) as they explained had been approved in other cases:

> "I think the word 'discover' in itself, according to the ordinary use of language, may be taken simply to mean 'find out'. What has to be found or found out is that any properties or profits chargeable to tax have been omitted from the first assessment.
>
> Of course, if there were any reason in the context for restricting the word 'discover' to the discovery of an error in fact, that restriction would necessarily receive effect, but in my opinion the context points, not to any such restriction, but, on the contrary, to so wide a meaning that the word ought to be held to cover just the kind of discovery which was made here, when the Special Commissioners found out that, by reason of a misapprehension of the legal position, certain of the profits chargeable to tax had been omitted from the first assessment."

494. They concluded, as follows, at [37]:

> "In our judgment, no new information, of fact or law, is required for there to be a discovery. All that is required is that it has newly appeared to an officer, acting honestly and reasonably, that there is an insufficiency in an assessment. That can be for any reason, including a change of view, change of opinion, or correction of an oversight. The requirement for newness does not relate to the reason for the conclusion reached by the officer, but to the conclusion itself. If an officer has concluded that a discovery assessment should be issued, but for some reason the assessment is not made within a

> reasonable period after that conclusion is reached, it might, depending on the circumstances, be the case that the conclusion would lose its essential newness by the time of the actual assessment. But that would not, in our view, include a case, such as this, where the delay was merely to accommodate the final determination of another appeal which was material to the liability question…."

495. In the UT's decision in *Tooth* the UT set out, at [75], that a discovery of a situation set out in s 29(1) connotes "a change in a state of mind" as was held in *Charlton* at [28] and, at [76], that as was said in *Charlton* at [37], no "new information, of fact or law, is required for there to be a discovery". All that is required is that:

> "it has *newly appeared* to an officer, acting honestly and reasonably, that one of the situations set out in section 29 may pertain. That can be for any reason, including a change of view, change of opinion, or correction of an oversight."

496. In *Beagles*, the UT similarly said, at [70], that there is a relatively low threshold for there to be a discovery and:

> "The relevant officer must come to a conclusion or have "found out" from the evidence before him or her that there is an insufficiency in the return (see, for example, Bray J in *R v Commissioners for the General Purposes of Income Tax for Kensington ex parte Aramayo* 6 TC 279 at page 10283 or Lord Normand in *Inland Revenue v Mackinlay's Trustees* [1938] SC 765 at page 771). That conclusion must be "new" (per Viscount Simmonds in *Cenlon*). The cases also suggest that a discovery involves both a subjective and an objective element. The officer must believe that the available information points in the direction of a discovery and that belief must be a reasonable one for the officer to hold (*Anderson v Revenue and Customs Commissioners* [2018] STC 1210 ("Anderson") [28] –[30])….."

497. In *Tooth*, the UT continued, at [77], that whether or not there is a discovery "is essentially subjective": it is the officer's (or officers') state of mind that matters. At [79] they said that they agreed broadly with the statement at [37] of the decision in *Charlton* but they set out the position in greater detail:

> "(3) We entirely agree with the Upper Tribunal in *Charlton* that on making a discovery, HMRC must act expeditiously in issuing an assessment. If, to use the words of *Charlton*, an officer has made a discovery, then any assessment must be issued whilst the discovery is "new" [and they referred to *Pattullo v Revenue and Customs Commissioners* [2016] UKUT 270 (TCC) at [46] to [56]].
>
> (4) It follows from this that the same officer (or officers) cannot make the same discovery twice. We see no reason, however, why the same officer cannot, for different reasons, discover that one of the situations set out in section 29(1)(a), (b) or (c) pertains a second time….
>
> (6) What, however, if two different officers independently make the same discovery? In our judgment, as a matter of ordinary English, a discovery can only be made once. We accept that section 29(1) TMA is framed by reference to the subjective state of mind of an officer or the board, but what is a "discovery" is an objective term. It seems to us that in this case, the first officer makes the discovery; the second officer simply finds out something that is new to him. In particular if one officer is made aware of, and accepts, the conclusion of another officer it cannot be said that the first officer made a discovery.
>
> (7) We consider that such a construction is necessary for the protection of both the taxpayer and officers of HMRC…."

498. In *Beagles*, at [74], the UT similarly held that:

> "Whilst we accept that it might be possible for an officer to discover the same insufficiency in a return more than once if it is for different reasons, it is not, in our view, possible for an officer to make the same discovery twice for the same reasons. The insufficiency cannot "newly appear" to the officer for a second time (to use the words of Viscount Simmonds in *Cenlon*)."

499. The UT accepted at [79] that "a discovery can lose its quality of "newness" such that a valid assessment cannot be made under s29(1)".

500. In the Court of Appeal's decision in *Tooth* (*HMRC v Tooth* [2019] EWCA Civ 826), at [61], the court endorsed the concept of "newness" as set out *Charlton* stating that*:* "the requirement for the conclusion to have "newly appeared" is implicit in the statutory language "discover"".

501. Mr Chacko said that HMRC does not accept, in principle, that "staleness" should have any role at all in a case of an assessment that is issued within the applicable statutory time limits. In an appropriate case HMRC will argue that point in the higher courts. They accept, however, that as matters stand, there is case law, which is binding on the tribunal, that "staleness" operates as a ground of invalidity even if the assessment is made in time. Mr Chacko referred to the UT's earlier decision in *Pattullo v Revenue and Customs Commissioners* [2016] UKUT 270 (TCC) ("*Pattullo*"), which was cited in *Tooth* and *Beagles*.

502. At [52] of the *Pattullo* case the UT said that, quite apart from the "highly persuasive passages" in *Charlton* at [37] and *Corbally-Stourton v Revenue and Customs Commissioners* [2008] STC (SCD) 907 at [44] "the requirement for the discovery to be acted upon while it remains fresh" appears to arise on the natural meaning of s 29(1) itself given it applies "if" HMRC discover certain matters:

> "The word "if", like many words in the English language, has a variety of shades of meaning. It may be purely conditional. But it may equally have a temporal aspect, as in the expression "if and when" (e.g. if the sun comes out we shall go to the beach). I do not regard this as stretching the meaning of "if". The context makes it clear that an assessment may be made if and when it is discovered that the assessment to tax is insufficient. It would, to my mind, be absurd to contemplate that, having made a discovery of the sort specified in s 29(1), HMRC could in effect just sit on it and do nothing for a number of years before making an assessment just before the end of the limitation period specified in s 34(1)."

503. The UT continued, at [53], that the word "if", as used in the "if and when" sense does not mean "immediately" and each case would turn on its particular facts:

> "Mr Gordon was right, in my view, to accept that the discovery could be kept fresh for the purposes of being acted upon later…..each case would turn on its particular facts. He gave the example of notification being given to the taxpayer of the discovery in the expectation that matters could be resolved without the need for a formal assessment to be made. No doubt there are many other examples which could be given. The UT in *Charlton* at para 37 recognise that the decision in each case will be fact sensitive. I do not think it would be helpful to try to define the possible circumstances in which a discovery would lose its freshness and be incapable of being used to justify making an assessment. But I consider that Mr Gordon was right to accept that it would only be in the most exceptional of cases that inaction on the part of HMRC would result in the discovery losing its required newness by the time that an assessment was made."

504. The UT concluded, at [57], that in the circumstances of that case, a delay of some 18 months or more would have made the discovery stale.

505. Mr Chacko noted that *Pattulo* was referred to in *Beagles* and considered that the UT in that case also endorsed the view that it is only in exceptional cases that inaction on the part of HMRC would result in a discovery losing its essential newness by the time an assessment is made (referring to [50], [53] and [87]).

506. Mr Goldberg made the following main points:

(1) From the evidence there is a prima facie case that Mr White made a discovery, in that he was certainly aware of the possibility of insufficiencies of tax in the appellants' tax returns, as early as in November 2013 and/or that one of the many other officers involved did so by no later than September 2014. At that time there was an Odey case team who considered the risk assessments which set out the risk in relation to the Plan and the 2014 technical paper was produced which clearly demonstrates that HMRC had a strategy for dealing with risks arising from this type of planning.

(2) The fact that Mr White seemed fully aware of risk in relation to Mr Fletcher and Mr Stewart before he received any information beyond that in their tax returns, plainly indicates that there is sufficient information within the tax return made by the appellants for an officer of HMRC to see at least the possibility of an insufficiency. Moreover, the tribunal must bear in mind the overall context as regards what HMRC knew of planning of the type undertaken by Odey which they refer to as a "Partnership Incentive Plan". For example, the evidence given by HMRC in the *Bluecrest* case was taken to show that HMRC's enquiries into Partnership Incentive Plans were static by the end of 2013.

(3) There is a lack of information about HMRC's activities in relation to Odey in the period from September 2014 until Ms Frusher became involved in late 2015, in particular, as regards Mr Hagan and Mr Gannon. Ms Frusher and Mr Williams were not able to shed any light on this. It is known, however that at that time Mr Hagan had sufficient information to open an enquiry into Odey's partnership return for 2012/13 and the statement that Mr Hagan's involvement was at the early stages of the enquiry into the Plan is clearly wrong. He was involved at a stage by which HMRC had a developed analysis and strategy.

(4) As set out below, on her own evidence Ms Frusher was in a position to make such a discovery for all relevant tax years in March 2016 notwithstanding that she had not received all of the requested information from Odey. On that basis it is overwhelmingly probable that Mr Hagan and Mr Gannon were in position to make relevant discoveries and did make discoveries while they were handling the matter.

(5) If HMRC do not accept the position is as set out above, it is for them to establish by positive evidence that the discovery was not made earlier than Ms Frusher and Mr Williams assert to be the case but they have not done so. They could have called other witnesses (such as Mr Hagan or Mr Gannon) but have simply chosen not to do so. The fact that it was apparent to Ms Frusher when she opened the Odey files in late 2015 or early 2016 that HMRC would want to claim there was an insufficiency of tax in the relevant tax returns of the appellants, raises the question why that was not apparent to Mr Hagan who held the files for some considerable time.

(6) It is clear from the UT's decision in *Tooth* that an officer who becomes aware of an insufficiency of tax which another officer had already become aware of does not make a discovery for the purposes of s 29. On that basis, the

appellants' primary case is that the only relevant discovery is that made by Mr White in November 2013 and that the delay between the making of that discovery and the issue of the assessments is so lengthy that that discovery must have become "stale". As regards all of the relevant assessments, that delay exceeds by far the 18 months of delay which in *Pattulo* the UT held made the discovery "stale" in that case. The point is particularly clear in relation to the assessments made in respect of Mr Fletcher and Mr Stewart; Mr White made a discovery but decided not to pursue it.

(7) Even if there was no discovery until the autumn of 2014 or during 2015, there is still a very lengthy time lag until the assessments were issued such that the discovery is "stale" or, at any rate, that must be the case as regards the assessments issued in 2017 and 2018.

(8) If the tribunal accepts that no officer of HMRC made a relevant discovery prior to Ms Frusher's involvement, Ms Frusher is to be taken as having made a discovery of insufficiencies of tax in respect of all the relevant tax returns in March 2016 and that discovery is "stale" as regards the 2012/13 and 2013/14 tax years:

(a) On her own evidence, Ms Frusher discovered the insufficiencies of income tax in respect of the appellants' returns for the 2011/12 tax year and issued assessments relating to that that year notwithstanding that she had not then received all the information she had requested from Odey. It cannot be the case, therefore, that she did not discover the insufficiencies of tax in relation to the returns for the 2012/13 and 2013/14 tax years because she was awaiting outstanding information. The information she says that she needed can hardly be key given that Ms Frusher made the discovery for the previous tax year and was able to act upon it.

(b) It is clear from Mr Williams' evidence that Mr Ben Blakely did not make any discovery but was merely involved in processing discovery assessments in cases where they were regarded as necessary; he was told to collect a liability, not to decide whether one existed.

(c) It is quite apparent that there was no need for Ms Frusher to wait until March 2017 to make the assessments for the 2012/13 tax year, and there is no reason why HMRC could not have issued the assessments for the 2013/14 assessments, which were in fact issued in March 2018, as early as March 2016.

507. HMRC responded that:

(1) A discovery of an insufficiency of tax must relate to the particular taxpayer's position as shown in the particular tax return. It is not relevant, therefore, that officers at HMRC who were involved in dealing with the tax affairs of Odey (or of Mr Fletcher or Mr Stewart) were aware of the type of planning undertaken by Odey in a general sense and had formed a view in 2014 that it does not work (as set out in the 2014 technical paper).

(2) Moreover, it is clear from the authorities that the question is: has an officer come to the view that there is an insufficiency or satisfied himself that there is an insufficiency. The question is not: has the officer come to the view that there is a risk in this case, or there is a possible insufficiency if he were to look into it? The risk assessments made in 2014 were not specifically about the Plan; they were a general assessment of revenue risk connected to the Odey Group. The existence of an Odey case team and an identification of a risk in relation to the Plan certainly does not mean that there was an investigation into

the Plan going on at this stage. The fact that Mr Hagan opened an enquiry does not mean that he must have made a relevant discovery; there no threshold test to open an enquiry.

(3) An officer simply cannot make a discovery of an insufficiency of tax before the relevant tax return is filed as Mr Goldberg seems to suggest in his assertion that the discovery in relation to all relevant tax years was made in 2013/14, before the relevant tax returns for 2013/14 were filed.

(4) Before Ms Frusher became involved in dealing with Odey's tax affairs, in considering a number of partnerships, officers of HMRC may have suspected Odey was involved in this type of planning but no real investigation was carried out until she took the matter on. As the evidence shows the case had not been "worked" until then. Whilst some documents had been received from Odey, they were not reviewed until Ms Frusher carried out that task.

(5) Whilst in 2013 HMRC made brief enquiries into the tax position of Mr Fletcher and Mr Stewart as regards the tax year 2011/12 tax year, it was only during the much more substantive enquiry into Odey's tax affairs that HMRC obtained substantial information. It was only during that enquiry that, in March 2016, (a) Ms Frusher formed her view that there were insufficiencies of tax in relation to the 2011/12 tax year, on the basis that the deferred share paid to PSCL was in fact taxable income of the relevant Members in the year of allocation, and (b) accordingly she made an amendment to Odey's partnership tax return for that year under s 30B and issued discovery assessments to the relevant Members.

(6) It does not automatically follow from the fact that Ms Frusher made that discovery that she then also discovered insufficiencies of tax according to HMRC's alternative arguments that the relevant Members are subject to income tax on sums received on the reallocation of Special Capital. In fact, Ms Frusher discovered that the individual Members had under-declared their income on that basis only when she went through their individual returns in light of the particular information relating to each of them and so formed a view in relation to their individual tax positions. An officer could in the course of the required exercise form a view on the basis of his/her estimates of figures as Ms Frusher had to do in relation to the 2011/12 year, as she was running out of time. However, HMRC are not required to undertake that exercise as early as they possibly can on the basis of estimated amounts but are entitled to wait until they have had as full an explanation as they consider is required and they are likely to obtain. It is clear from the documents that no one at HMRC carried out this exercise and formed a view on this before Ms Frusher and Mr Williams became involved.

(7) The UT in *Pattullo* considered that an assessment may lose its "newness" only in exceptional cases. It is clear from the cases that it is not only the lapse of time between the discovery and the issue of the assessment or determination which is relevant. The tribunal must consider all the surrounding circumstances and, in particular, the reason for any delay and activity in the period between the two events. A discovery should not be regarded as losing its "essential newness" where, in the period before the assessment is issued, there are on-going active discussions/correspondence between the parties in relation to the tax issue in question such that the taxpayer cannot be in any doubt that HMRC intend to issue it. "Staleness" is about HMRC not being able just to sit on their hands when they could act on their discovery. This principle is not intended to

discourage full enquiries, attempts to settle or to provide a windfall to a taxpayer where an enquiry has been slow due to the actions of the taxpayer and information has been provided very gradually.

(8) In this case, HMRC were taking action throughout the relevant period such that the discoveries are not "stale" even if Ms Frusher is taken to have made all relevant discoveries in the early to the middle part of 2016. HMRC continued throughout 2016 and part of 2017 to request substantial amounts of information which Odey delayed sending them such as the documents relating to the Plan for 2012/13. As has been illustrated at the hearing, the documentation in place in each of the relevant years has significant differences. In fact, the majority of the outstanding information was not provided until May 2017 and some of it was not provided at all before the enquiries were closed. Moreover, there was no comprehensive discussion of the Plan between the taxpayers and HMRC until early 2017.

Conclusion on discovery issue – amendment and assessments for 2011/12

508. I have concluded that HMRC have established to the required standard of proof (on the balance of probabilities) that Ms Frusher discovered that insufficiencies of tax may pertain in relation to the amendment and discovery assessments made for the 2011/12 tax year in February or March 2016 following the completion of her review of the documents and information provided by Odey on 29 September 2015. I do not consider that the documentary evidence on which the appellants rely raise a viable case that another officer made an earlier discovery of an insufficiency of tax in respect of the relevant tax returns such that there is an onus on HMRC to rebut the appellants' argument in that respect.

509. To recap, s 29(1) applies where an officer of the Board or the Board *discovers* as regards "*any person (the taxpayer) and a year of assessment*" (emphasis added) that, amongst other circumstances, "(a) any income which ought to have been assessed to income tax has not been assessed" or "(b) an assessment to tax is or has become insufficient". Section 30B(1) is couched in very similar terms. As interpreted by the courts and on their plain meaning, these provisions are intended to operate where an officer/the Board finds out or forms the view (as the courts have held, acting honestly and reasonably) that *a particular taxpayer for a particular year of assessment* has income which ought to have been assessed or that, where applicable, his self-assessment to tax as contained in his tax return (or other assessment) is or has become insufficient such that a discovery assessment ought to be issued. As set out in the caselaw, the discovery test in these provisions is essentially a subjective one; the question is what an officer actually found out, on the basis of the materials he or she has, and not what he or she ought to have found out or ought to have done (although I note that it has been suggested in the cases that any view an officer forms that there is an insufficiency of tax has to be reasonably held).

510. With that context in mind, I note the following:

(1) As set out at [417] and [418], as regards Mr White's involvement in 2013:

(a) Mr White dealt only with an enquiry into the tax affairs of Mr Stewart and Mr Fletcher in relation to their tax returns for the 2011/12 tax year and, once they had responded to his initial enquiries, he decided not to pursue any issue in relation to their tax position as regards the Plan.

(b) In relation to Mr Fletcher that was on the basis, essentially, that the risk identified had been dealt with satisfactorily "at the local level". In relation to Mr Stewart, Mr White set out in an internal note that (i) advice

was awaited from another part of HMRC as to whether distributions from the deferral scheme were taxable in the hands of the recipient, (ii) he was concerned as to whether he could justify holding the case open any longer on the basis of advice which may or may not result in further risks given local risk had been resolved, (iii) he was not "absolutely sure that the customer had received anything from the deferred profit scheme", and (iv) for another customer who was also a member of Odey (presumably Mr Fletcher), he had closed down the case once all the local issues had been settled. Mr White also recorded that another officer advised that in light of these concerns and given "we must be seen to be applying a fair and consistent approach" the risk should be closed without awaiting the response.

(c) Overall, this indicates that in fact Mr White had not found out or formed the view that there was an insufficiency of tax for the tax year 2011/12 as regards Mr Fletcher's and Mr Stewart's participation in the Plan. Indeed, he expressed doubt that was the case for the reasons set out.

(d) I note that Mr White was in contact with other officers of HMRC (such as Mr Gannon) who appeared to be concerned with the tax affairs of Odey and its Members in a broader sense. However, there is no evidence that Mr White himself had any broader knowledge of Odey or its other Members. It seems to me, therefore, that, in light of this and the fact that he decided not to pursue matters with Mr Stewart and Mr Fletcher, it would be speculative to conclude that Mr White may have formed the view that one of the situations in s 29(1) or 30B(1) pertained in relation to the partnership tax return of Odey for 2011/12 or the tax returns of other relevant Members for that year due to the operation of and, the relevant Members participation in, the Plan. Indeed, such indications as there are, suggest that it is highly unlikely he did so.

(2) The preparation and consideration of the tax risk assessments in 2014 (see [420] to [424]) demonstrate that officers within HMRC were aware that Odey used what they termed "Partnership Incentive Planning" whereby Special Capital was allocated to PSCL and they were aware of the amounts so allocated to PSCL. It was noted in these tax risk assessments that if all the Special Capital for the period February 2011 to 5 April 2013 was reallocated to Members "before FA 2014 bites the tax at risk is approximately £1.7m" and that Special Capital of "£1.9m was acquired up to March 2012 and will presumably be allocated to other partners in the LLP in due course". Whilst this shows that HMRC officers had a general view there was a risk that additional income tax was due from Members of Odey in respect of the arrangements under the Plan, it does not demonstrate that any officer involved formed a view of any particular insufficiency of tax in relation to particular Members of Odey or Odey itself for the relevant periods. Indeed, on the contrary, it is clear that the officers considered further information was required to form any such view; hence, the recommendation was that enquiries should be opened into Odey's partnership tax returns for 2012/13 and 2013/14 which Mr Hagan proceeded to do.

(3) Given the nature of the statutory test in s 29(1) and s 30B(1), it does not suffice to indicate that any officer had formed a view that there may be an insufficiency of tax in the tax returns of Odey and its Members for any particular period in respect of the Plan that (a) HMRC had a "wealth" of general

information on planning of the type Odey implemented, (b) HMRC had formed a view in general terms of the tax effects of the type of planning undertaken by Odey as set out in the 2014 technical paper, (c) in the *Bluecrest* litigation it was accepted that HMRC's stance on "Partnership Incentive Plans" was static from 2013. As Ms Frusher recognised, whilst there is "a common theme across these arrangements, they are all very, very fact dependent" and, accordingly, whilst the 2014 technical paper set out what the main challenges could be HMRC had to establish the evidence and facts to make challenges in particular cases (see [474] above).

(4) There are few details of the activities of Mr Gannon and Mr Hagan in relation to Odey before Ms Frusher and Mr Williams became involved. However, that neither they nor any other officer had taken a closer look at the precise tax effects of the Plan for Odey and the Members prior to that time is plainly indicated by the email of 8 December 2015 in which Mr Jackson notified Mr Williams that his team could deal with the enquiries into Odey's partnership tax return. In that email there is a note that the Odey file was "Not worked. Initial documents require review" and a comment from Mr Jackson that Odey had not been reviewed at all. Ms Frusher said that her understanding was that this meant that the response provided by Odey to HMRC on 29 September 2015 had not been reviewed, in particular, by Mr Hagan as the tax specialist attached to the case before Ms Frusher became involved; it meant that he had not worked the matter any further from that point. That accords with Ms Frusher's explanation that the team of which she was a member was brought in to speed up dealing with cases such as this. Mr Williams gave a similar explanation (see [485] and [486] above).

Conclusion – discovery for the tax years 2012/13 and 2013/14

511. I consider that Ms Frusher also discovered in the early part of 2016 (and no later than the end of April or May) that there may pertain an insufficiency of tax in respect of the tax returns of the relevant Members for 2012/13 and 2013/14, on the basis that they were taxable on the sums they received in those years following an allocation of Special Capital. As explained in further detail below, the fact that Ms Frusher wanted to continue to gather more information and to engage with Odey it seems to refine and firm up on some of HMRC's arguments (notably, as regards ss 773 to 778 ITA) and to give Odey an opportunity to consider its position does not detract from the fact that she had found out that there was an insufficiency.

512. I note the following as regards Ms Frusher's discovery as evidenced in the relevant documents:

(1) The documents provided by Odey on 29 September 2015 which Ms Frusher had reviewed by February/March 2016 appear to comprise a comprehensive suite of documents implementing the Plan for 2013/14 from which it must have been apparent how the Plan worked (hence why Ms Frusher made the discovery in relation to the earlier 2011/12 year) and which Members had received reallocations of Special Capital for that period (see [427] to [429]).

(2) It is apparent from the correspondence that, following the review of those documents Ms Frusher had plainly not only formed the view that the deferred share paid to PSCL was taxable as income in the hands of the relevant Members in the year of allocation but also, as a secondary argument, that sums received by Members when PSCL reallocated Special Capital to them were subject to income tax in the year of receipt.

(3) Ms Frusher expressly said this in the letters she sent to Members in respect of the 2011/12 tax year on 22 March 2016 (see [453]). It seems she had in mind that the sums were taxable as miscellaneous income under s 687 ITTOIA as she said in the letters that the sums were taxable as rewards for services to Odey. I cannot see how she can have had that view in relation to reallocations of Special Capital in relation to Members in 2011/12 and not in relation to such reallocations to Members in 2012/13 and 2013/14. That is particularly so as regards 2013/14 given that, as noted, Odey had provided on 29 September 2015 what appears to be a full suite of documents under which the Plan was implemented in that year (see [427] to [429]).

(4) Ms Frusher made a similar comment in a letter to Odey dated 22 June 2016 that HMRC "believe that the allocations of profit" made by Odey to PSCL "which have been subsequently distributed to members of [Odey] purportedly as capital, ought to be treated as allocations of profit to individual members and chargeable to income tax" (see [458]). She said in the letter that, therefore, it was important for HMRC to understand the full facts relating to the Plan, before reaching a decision on the appropriate tax treatment (see [458] above). It seems that at this point she also had in mind a charge under ss 773 to 778 ITA (regarding occupation income) as she asked for information she had not previously requested on the precise roles and activities of the Members.

(5) This indicates, as is reflected in her further on-going requests for information and her comments at the hearing, that Ms Frusher had formed a view that income tax was due as a result of the reallocation of Special Capital to Members but wished to firm up on which of HMRC's arguments to use to support this view and/or to garner evidence in support of these arguments. I note that in a number of places in her witness statement Ms Frusher stated that her view remained the same on the tax effects of the Plan it appears from when she first completed her review of the documents and information provided by Odey on 29 September 2015.

(6) I note that Ms Frusher appears to have been acting on the basis that the relevant Members had not included the sums which they received following an allocation of Special Capital in their relevant tax returns as taxable income and paid income tax on them. There would hardly have been any point in her pursuing the further information she sought throughout 2016 and part of 2017 if that was not the case.

513. In my view, Ms Frusher's responses when she was questioned at the hearing on why she considered that she had not made a relevant discovery in relation to the 2012/13 tax year until early 2017 and, so it seems in relation to the 2013/14 tax year at all (see [470] to [476]) can only be taken to indicate that:

(1) She accepted that in the earlier part of 2016 she had formed a view in principle that there was an income tax charge on Members who had received allocations of Special Capital in the relevant periods which they had not accounted for.

(2) However, in her view, that did not mean that she had actually discovered the relevant insufficiencies at that time; to her mind she did not do so until she had firmed up on the strength of all the arguments supporting her view, had given the taxpayer further opportunity to present their views or reach an agreement with HMRC and possibly until she/a colleague had actually computed the relevant additional tax with the benefit of the schedule of

reallocations of Special Capital provided in April 2016 (or that is what HMRC's counsel suggested).

514. I note the following as regards Ms Frusher's evidence in this regard:

(1) Ms Frusher's main reason for considering that she had not made a relevant discovery in respect of the 2012/13 and 2013/14 tax years in or around March 2016 was that she was not then up against a deadline as regards issuing assessments for those years (as she was for the 2011/12 tax year) and she wanted to get outstanding information to "further develop her view".

(2) In particular, she wanted any tax advice Odey/PSCL had received, email correspondence, further evidence of the review process PSCL undertook when awarding Special Capital and to look further at the argument that ss 773 to 778 ITA applied. She described whether there was a "tax motivation" and the tax advice, as "a key piece of information". I note that she said that she did not receive the tax advice (the Ernst & Young note) until the summer of 2017 but that did not prevent her issuing the assessments for the tax year 2012/13 in March 2017.

(3) She added that she thought it important to keep having a conversation with Odey (noting this did not happen until February 2017) and that there was a possibility Odey may have chosen to settle with and "we would not issue assessments before that if we were in a good time window, which may have been detrimental to those conversations".

(4) She also said on two occasions that when she issued the amendment and assessments for the 2011/12 tax year she did not have the details of the allocations of Special Capital (see [256] and [275]). I take it that she meant that, in March 2016, she did not have any details of such sums for 2011/12 and 2012/13 (as at that time no similar full suite of documents had been provided for those periods). I note that (i) details of the sums for 2013/14 must have been apparent from the documents which Odey provided for that year on 29 September 2015, and (ii) in any event, on 12 April 2016 Ms Frusher received from Odey a schedule of reallocations of Special Capital made to Members for both 2012/13 and for 2013/14.

515. Whilst the "discovery" test is essentially a subjective one that does not mean that an officer may be held to have discovered an insufficiency of tax only when the relevant officer herself believes that she did so if that view, albeit it may well be genuinely held, is not supported by the available evidence and appears to be a misconstruction of what is required under the statutory test. In my view, none of the factors referred to by Ms Frusher mean that she cannot be taken to have made the relevant discovery in the early part of 2016 as set out above. In particular:

(1) I consider that it is not relevant to the analysis that in the early part of 2016, Ms Frusher/HMRC may not have decided whether to pursue both of their possible arguments as to why the relevant sums were taxable (and I note Ms Frusher did not appear to be seeking additional information relating to the application of s 687 ITTOIA but rather her concerns appeared to be with ss 773 to 778 ITA) or that she may have wished to garner further evidence to support HMRC's stance. The important point is that, on the evidence, she plainly considered that the relevant sums were taxable in the hands of the Members albeit it seems she was still weighing up the strength of the particular arguments.

(2) I also consider that it is not relevant to the analysis that Ms Frusher was not certain that HMRC would actually proceed to act upon the discovery by

issuing assessments (as they would not do if, for example, they reached a settlement with the taxpayer). The fact that HMRC may choose not to pursue an insufficiency of tax and/or may make a settlement with the taxpayer cannot mean there was no discovery of that insufficiency until that process took place.

(3) Finally, it does not affect my conclusion that in the early part of 2016, Ms Frusher had not yet worked out the precise tax charge for each relevant Member; she plainly knew which Members had received allocations of Special Capital in the relevant tax years and so (in her view) had an insufficiency of tax for those years. In my view, the statutory test requires merely that the officer has detected that there is an insufficiency not that the officer has precisely quantified that insufficiency.

516. On that basis, I do not consider that Mr Blakely can have made a relevant discovery when he issued the discovery assessments for the 2013/14 year in late March 2018. It is established in the case law that, for the purposes of s 29(1) and s 30B(1), an officer cannot "discover" an insufficiency of tax for the same reason that another officer has previously done so. Moreover, in any event, the evidence set out at [478] to [486] does not indicate that Mr Blakeley did anything more than carry out or organise the process required to compute the tax charge and issue the assessments.

517. Even if, as is my view, all relevant discoveries were made by Ms Frusher no later than April 2016, I do not consider that those discoveries had lost their "essential newness" or become "stale" by the time that any of the relevant assessments were made and issued. In my view, on the basis of the case law, this is not just a question of simply how much time has elapsed between the discovery and the issue of the assessments and whether the assessments could have been made sooner. The status of discussions and awareness of the likely issue of the assessments must be a relevant factor in assessing whether the issue remains "live" or has becomes "stale".

518. I did not understand the appellants to argue that, if Ms Frusher is accepted to have made the relevant discoveries, there was any "staleness" issue as regards the issue of the amendment to Odey and the discovery assessments to the relevant Members for the tax year 2011/12. As regards the 2012/13 and 2013/14 tax years, the evidence demonstrates that HMRC and the appellants were engaged sufficiently actively during the period from when the discovery was made until the relevant assessments were issued in 2017 and 2018 that the relevant appellants must have been aware of the on-going issues in relation to their tax position and that, if they were not resolved, further assessments would be issued to them.

Was the condition in s 29(5) and s 30B(6) satisfied?

519. The parties referred to the Court of Appeal's decision in *Sanderson v Revenue and Customs Commissioners* [2016] EWCA Civ 19 ("*Sanderson*") as regards how the test in s 29(5) and s 30B(6) is to be applied. In that case, Patten LJ summarised the case law on this topic as follows at [17]:

> "…..It is clear as a matter of authority:
>
> (1) that the officer is not the actual officer who made the assessment….. but a hypothetical officer;
>
> (2) that the officer has the characteristics of an officer of general competence, knowledge or skill which include a reasonable knowledge and understanding of the law: see *HMRC v Lansdowne Partners LLP* [2012] STC 544;
>
> (3) that where the law is complex even adequate disclosure by the taxpayer may not make it reasonable for the officer to have discovered the

insufficiency on the basis of the information disclosed at the time: see *Lansdowne* at [69];

(4) that what the hypothetical officer must have been reasonably expected to be aware of is an actual insufficiency: see *Langham v Veltema* [2004] STC 544 per Auld LJ at [33]-[34]:

> "33. More particularly, it is plain from the wording of the statutory test in section 29(5) that it is concerned, not with what an Inspector could reasonably have been expected to do, but with what he could have been reasonably expected to be aware of. It speaks of an Inspector's objective awareness, from the information made available to him by the taxpayer, of "the situation" mentioned in section 29(1), namely an actual insufficiency in the assessment, not an objective awareness that he should do something to check whether there is such an insufficiency, as suggested by Park J. If he is uneasy about the sufficiency of the assessment, he can exercise his power of enquiry under section 9A and is given plenty of time in which to complete it before the discovery provisions of section 29 take effect.
>
> 34. In my view, that plain construction of the provision is not overcome by Mr. Sherry's argument that it is implicit in the words in section 29(5) "*on the basis of* the information made available to him" (my emphasis) and also in the provision in section 29(6)(d) for information, the existence and relevance of which could reasonably be inferred from information falling within section 29(6) (a) to (c), that the information itself may fall short of information as to actual insufficiency. Such provision for awareness of insufficiency "on the basis" of the specified information or from information that could reasonably be expected to be inferred therefrom does not, in my view, denote an objective awareness of something less than insufficiency. It is a mark of the way in which the subsection provides an objective test of awareness of insufficiency, expressed as a negative condition in the form that an officer "could not have been reasonably expected … to be aware of the" insufficiency. It also allows, as section 29(6) expressly does, for constructive awareness of insufficiency, that is, for something less than an awareness of an insufficiency, in the form of an inference of insufficiency."

(5) that the assessment of whether the officer could reasonably have been expected to be aware of the insufficiency falls to be determined on the basis of the types of available information specified in s.29(6). These are the only sources of information to be taken into account for that purpose: see *Langham v Veltema* at [36]:

> "The answer to the second issue– as to the source of the information for the purpose of section 29(5) - though distinct from, may throw some light on, the answer to the first issue. It seems to me that the key to the scheme is that the Inspector is to be shut out from making a discovery assessment under the section only when the taxpayer or his representatives, in making an honest and accurate return or in responding to a section 9A enquiry, have clearly alerted him to the insufficiency of the assessment, not where the Inspector may have some other information, not normally part of his checks, that may put the sufficiency of the assessment in question. If that other information when seen by the Inspector does cause him to question the assessment, he has the option of making a section 9A enquiry before the discovery provisions of section 29(5) come into play. That scheme is clearly supported by the express identification in section 29(6) only of

> categories of information emanating from the taxpayer. It does not help, it seems to me, to consider how else the draftsman might have dealt with the matter. It is true, as Mr. Sherry suggested, he might have expressed the relevant passage in section 29(5) as "on the basis *only* of information made available to him", and the passage in section 29(6) as "For the purposes of subsection (5) above, information is made available to an officer of the Board if, *but only if,*" it fell within the specified categories. However, if he had intended that the categories of information specified in section 29(6) should not be an exhaustive list, he could have expressed its opening words in an inclusive form, for example, "For the purposes of subsection (5) above, information … made available to an officer of the Board … *includes any of the following*"."

520. At [18] Patten LJ noted that there is scope for argument in relation to the level of awareness that the relevant information needs to create in order for the condition to bar the right to raise as assessment under s 29. He said that in *Corbally-Stourton* and *R (on the application of Pattullo)* v *Revenue and Customs Commissioners* [2010] STC 107 the court indicated that it may suffice if the information disclosed would lead the notional officer to conclude on the balance of probabilities that there is an insufficiency of tax. He continued, however, at [19], to note that in *Lansdowne* at first instance Lewison J (at [48] of that decision) took a different and more general approach. He considered that the right test was whether HMRC had sufficient information to make a decision whether to raise an additional assessment.

521. At [20] and [21], he explained that a not dissimilar test was applied in the Court of Appeal in *Revenue and Customs v Lansdowne Partners Ltd Partnership* [2011] EWCA Civ 1578, [2012] STC 544 ("*Lansdowne*") where the Lord Chancellor and Moses LJ commented as follows (at [56] and [69] to [70]):

> [56] "I do not suggest that the hypothetical inspector is required to resolve points of law. Nor need he forecast and discount what the response of the taxpayer may be. It is enough that the information made available to him justifies the amendment to the tax return he then seeks to make. Any disputes of fact or law can then be resolved by the usual processes…"
>
> [69]…As the Chancellor points out (at [56]), awareness of an insufficiency does not require resolution of any potential dispute. After all, once an amendment is made, it may turn out after complex debate in a succession of appeals as to the facts or law, that the profits stated were not insufficient. I have dwelt on this point because I wish to leave open the possibility that, even where the taxpayer has disclosed enough factual information, there may be circumstances in which an officer could not reasonably be expected to be aware of an insufficiency by reason of the complexity of the relevant law.
>
> [70] I also wish to express polite disapproval of any judicial paraphrase of the wording of the condition at s 30B(6) or s 29(5). I think there is a danger in substituting wording appropriate to standards of proof for the statutory condition. The statutory condition turns on the situation of which the officer could reasonably have been expected to be aware. Awareness is a matter of perception and of understanding, not of conclusion I wish, therefore, to express doubt as to the approach of the Special Commissioner in *Corbally-Stourton* v *Revenue and Customs Comrs* [2008] STC (SCD) 907 and of the Outer House in *R (on the application of Pattullo)* v *Revenue and Customs Comrs* [2009] CSOH 137, [2010] STC 107, namely that to be aware of a situation is the same as concluding that it is more probable than not. The statutory context of the condition is the grant of a power to raise an assessment. In that context, the question is whether the taxpayer has provided sufficient information to an officer, with such understanding as he

> might reasonably be expected to have, to justify the exercise of the power to raise the assessment to make good the insufficiency."

522. Lord Justice Patten said at [22] that it is important to emphasise that, as he thought was made clear at [55] of *Lansdowne*, the decision in *Lansdowne* did not involve any qualification of what Auld LJ in *Langham v Veltema* identified as the question posed by the second condition in s 29(5): "The hypothetical officer must, on an objective analysis, be made aware of an actual insufficiency in the assessment by the matters disclosed in the s 29(6) information".

523. He continued, at [22] and [23], to note that the sole dispute in *Lansdowne* was whether the disclosures made by the taxpayer's accountants were sufficient to cause the hypothetical officer to conclude that there was an insufficiency of tax. The comments he had cited from *Lansdowne* were directed to HMRC's argument that the disclosures made required inferences to be drawn about the accuracy of the self-assessment based on certain legal assumptions and that the officer could not be expected to resolve issues of law in determining the impact of the information supplied and, in the face of such uncertainties, the officer could not be taken to be "aware" of an insufficiency. Patten LJ concluded on this point that:

> "The decision in *Lansdowne* confirmed that the officer was not required to resolve (or even be able to assess) every question of law (particularly in complex cases) but that where, as Moses LJ expressed it, the points were not complex or difficult he was required to apply his knowledge of the law to the facts disclosed and to form a view as to whether an insufficiency existed. That is a matter of judgment rather than the application of any particular standard of proof. And the reference to the officer needing to reach a conclusion which justified the making of a discovery assessment has to be read in that context."

524. At [24], he explained that Mr Sanderson's case was that the UT over-stated the level of knowledge which needs to be imputed to the officer under s 29(5). The argument was that the threshold is a relatively low one which "merely requires the officer to be able to justify his belief that further tax is due". In Patten LJ's view that argument rested on eliding the requirement in s 29(1) (for an officer to discover that there is an insufficiency in the return) with the condition in s 29(5); the argument was that, "[u]nless….the threshold of knowledge is set relatively low it would be difficult, if not impossible, in most cases for HMRC to be able to raise an assessment under s.29(1)". At [25], he rejected the proposition that ss 29(1) and (5) import the same test and that HMRC's power to raise an assessment is therefore directly dependent on the level of awareness which the notional officer would have based on the s 29(6) information:

> "The exercise of the s.29(1) power is made by a real officer who is required to come to a conclusion about a possible insufficiency based on all the available information at the time when the discovery assessment is made. Section 29(5) operates to place a restriction on the exercise of that power by reference to a hypothetical officer who is required to carry out an evaluation of the adequacy of the return at a fixed and different point in time on the basis of a fixed and limited class of information. The purpose of the condition is to test the adequacy of the taxpayer's disclosure, not to prescribe the circumstances which would justify the real officer in exercising the s.29(1) power. Although there will inevitably be points of contact between the real and the hypothetical exercises which ss.29(1) and (5) involve, the tests are not the same."

525. Mr Chacko said that it is clear that (a) the question is not what documents would have warned a hypothetical officer that he ought to ask questions but what documents

would have caused him to become aware of the insufficiency of tax, and (b) the tribunal must not impute to the hyp"othetical officer the fact that the corporate partner avoidance team had a view on how Partnership Incentive Plans" work.

526. Mr Chacko said that the tests set out in s 29(5) and s 30B(6) are met in relation to the amendment made under s 30B TMA and all the discovery assessments issued to Members in relation to the 2011/12, 2012/13 and 2013/14 tax years:

(1) The very earliest that the hypothetical officer could be regarded as having sufficient information reasonably to be aware of the insufficiencies of tax in relation to partnership tax return for 2011/12 and the Members' tax returns for 2011/12 and 2012/13 is when HMRC received documents and information from Odey in September 2015. That date is long past the expiry of the time limit for Odey to enquire into any of the relevant returns.

(2) HMRC accept that, in relation to the discovery assessments made in respect of the 2013/14 tax year, under s 29(7) the information provided by Odey in September 2015 is to be taken into account. However, they do not accept that that information of itself suffices to demonstrate to the hypothetical officer that there was an actual insufficiency (nor to infer that there was something else HMRC could have asked for which would tell them whether or not there was an actual insufficiency). There was sufficient information only once the further information was provided after the relevant enquiry window had closed for the 2013/14 tax year such as the schedule showing the reallocations of Special Capital made to the Members for that year (which was provided in April 2016), the further explanation of the planning provided in January and February 2017 and important documents such as the letters which Odey sent to Members in January 2013 letters (which contained different wording to those sent the following year).

(3) The information which Mr Fletcher and Mr Stewart provided to HMRC during the enquiry into their tax returns for 2011/12 are also insufficient to demonstrate to the hypothetical officer that there was an insufficiency of tax in those returns as a result of their participation in the Plan. This is a complicated set of arrangements and there simply was not enough information provided beyond the idea that there was some kind of deferral scheme. Moreover, it was expressly stated very clearly in the responses given to HMRC's enquiries that there was no deferred amount of profit.

527. Mr Goldberg made the brief submissions that HMRC have not demonstrated that the tests in s 29(5) and s 30B(6) are met as set out above.

Conclusions on application of ss 29(5) and 30B(6)

528. I have concluded that applying the test set out in s 29(5) and s 30B(6) on the basis of the caselaw set out above:

(1) A hypothetical officer of general competence, knowledge or skill including a reasonable knowledge and understanding of the law, could not have been reasonably expected, on the basis of the information made available to him before the expiry of the time limit for HMRC to raise enquiries into Odey's partnership tax return for 2011/12 and the relevant Members' tax returns for that year and 2012/13, to be aware that there was an insufficiency of tax in those returns due to the operation of the Plan and the Members' participation in it:

(a) According to Ms Frusher's evidence, the time limits for HMRC to raise an enquiry into Odey's partnership tax return for 2011/12 and into

the Members' tax returns for 2012/13 expired on (i) 23 July 2013 and (ii) from 7 October 2014 and 31 January 2015 respectively.

(b) No evidence was given on the expiry of the time limits for HMRC to open an enquiry into the relevant Members' tax returns for 2011/12. I take the relevant date, under the rules which usually apply, to be 31 January 2014.

(c) By the relevant dates, under s 29(6) or 30B(5) the hypothetical officer would be regarded as having only the relevant returns and any accompanying documents such as Odey's accounts for the relevant period before him. Whilst those would show a portion of Odey's trading profits for the relevant period as allocated to PSCL and the portion of Odey's profits which were allocated to each relevant Member, that is hardly sufficient for the hypothetical officer to deduce that there was an actual insufficiency of income tax due to the Plan and related arrangements.

(2) However, such a hypothetical officer could have been reasonably expected, on the basis of the information made available to him before the expiry of the time limit for HMRC to raise enquiries into the tax returns of the relevant Members for the 2013/14 tax year, to be aware that there was an insufficiency of tax in those returns due to the Members' participation in the Plan:

(a) Neither Mr Williams nor Ms Frusher presented evidence on when the time limit for an enquiry to be raised into the tax returns made by the relevant Members for the tax year 2013/14 expired. In the absence of any evidence, I take that date to be 31 January 2016 under the usual rule. I note that HMRC proceeded on that basis in making their submissions.

(b) By 31 January 2016, as HMRC accepted, the hypothetical officer would be deemed to be in receipt of the set of documents and information which Odey provided to HMRC on 29 September 2015. As noted, those documents appear to comprise a full suite of the documents under which the Plan was implemented for the 2013/14 tax year including resolutions made by the board of PSCL in relation to the reallocation of Special Capital to Members (see [428] and [429]). I cannot see how the fulsome sight of the implementation and operation of the Plan which this provided would not lead such an officer to form the view that there was an actual insufficiency of tax in respect of the relevant Members' tax returns for that year. I note that HMRC asked for a specific schedule of all allocations of Special Capital for 2012/13 and 2013/14 which was not provided by Odey until 12 April 2016. However, in any event, the documents which Odey provided for 2013/14 would have shown the amounts and Members to whom allocations of Special Capital were made for that year.

(3) Finally, I also consider that such a hypothetical officer could have been reasonably expected, on the basis of the information made available to him by the time HMRC closed their enquiries into the tax returns of Mr Fletcher and Mr Stewart for the 2011/12 tax year, to be aware that there was an insufficiency of tax in those returns due to their participation in the Plan. The information provided explained how the Plan operated, the rationale for it and what sums Mr Stewart and Mr Fletcher had been allocated (see [417] above). I do not accept that the comments they made that their allocated profit share in the relevant period was not "deferred" means the test is not met. It is apparent from the rest

of the explanation given that, in effect, profits were accumulated in PSCL and reallocated to Members as Special Capital.

529. I note that the appellants also argued at the hearing that other amendments made by HMRC which are under appeal in these cases are invalid on the authority of the decision of the tribunal in *Inverclyde Property Renovation LLP & Clackmannanshire Regeneration LLP v Revenue & Customs* [2019] UKFTT 408 (TC). In that case the tribunal accepted the argument by certain LLPs that HMRC had had no power to open an enquiry into an LLP's partnership tax return under the income tax self-assessment provisions in section 12AC TMA, and accordingly that there had been no valid closure notices under section 28B TMA. The LLPs argued that any enquiry should have been made under the corporation tax self-assessment provisions in Schedule 18 to the Finance Act 1998. However, since the hearing that decision has been overturned by the UT (*Revenue and Customs v Inverclyde Property Renovation LLP & Clackmannanshire Regeneration LLP v Revenue & Customs Anor* [2020] UKUT 161 (TCC)) on the basis that, certainly where the LLP is carrying on a business with a view to profit (within the meaning of s 863 ITTOIA) as Odey is, that is wrong as a matter of law.

Conclusion and right to appeal

530. For all the reasons set out above, the appeals are dismissed except to the extent set out in Part E as summarised in [6(3)] above.

531. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

HARRIET MORGAN

TRIBUNAL JUDGE
RELEASE DATE: 4 February 2021