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STAMP DUTY LAND TAX BY MICHAEL THOMAS
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A REVIEW

by David Goldberg Q.C.

This is a good book.

As the author says in his preface, Stamp Duty Land Tax (SDLT) is a very important new tax and, as the author does not say, perhaps because it almost goes without saying, practitioners will need and will welcome a guide to it.

This book is that guide, providing sure signposts through the legislation.

I suppose the first thing one wants in a textbook is that it should be readable. It is, perhaps, too much to hope that it will read like a detective novel (after all every reader knows that it was the Chancellor who did it) but one hopes to be able to read even a tax textbook with ease and with enjoyment.

This is certainly true of this book: the author's style is easy and pleasant to read and so the book, although not lacking in detail, is not difficult to read.

Next, one hopes that a textbook will be sensibly ordered, so that it can, if the reader so wishes, be read as an entirety rather than just dipped into for the answer to particular questions.

Here, too, this book satisfies the requirement.

The first four chapters introduce the basic charge to the tax and explain how it is to be collected. Chapter 5 details the exemptions and reliefs. Chapter 6 deals with leases. Chapter 7 deals with structuring transactions and planning. Chapters 8 and 9 deal with the more mundane but no less essential matters of administration, compliance and commencement: these Chapters will be of particular relevance to practitioners involved in the detail of every day conveyancing.

I suppose the greatest test of any textbook is whether it provides answers to the questions that practitioners have.

I think this book will pass that test too: at any rate it has, so far, given me answers to the questions I have had, which have related mainly to the issue of what constitutes consideration for the purposes of this new tax. I happened to be in China when I needed to know the answer to this question. Happily I had a copy of this book with me and was able to find the answer. A sure sign, I think, that this book should be a *vade mecum* for all practitioners.

HOME THOUGHTS FROM ABROAD[1]

Milton Grundy

Practitioners in the United Kingdom are, not unnaturally, accustomed to look at the UK tax system from within: the landscape is familiar, and harsh. But when we look at the regime from the outside, the landscape is altogether more benign. Indeed, some aspects of it appear to have been expressly designed to replicate offshore facilities, ring-fenced for the benefit of non-residents. These facilities appear to have been, in the past, largely of academic interest – though undoubtedly valued in the world of the London trust companies and their international clientele. But over the last few years, they have acquired a new importance – as have other provisions in the UK tax code which facilitate the use of the United Kingdom as a kind of "stepping-stone" for non-resident investors investing abroad.

Why should non-resident investors start to prefer a UK *stepping-stone* to a simple tax haven vehicle? The answer lies, not in any changes which have occurred in the United Kingdom, but in changes which have occurred elsewhere. Many countries nowadays have some form of blacklist[2] and tax authorities everywhere have heard about *harmful features* and *harmful competition*[3]. Practitioners who might in the past have advised a client to conduct a transaction through a company incorporated in, say, the Cayman Islands, are now looking for the jurisdiction which is on nobody's blacklist and does not feature in the OECD or Primarolo lists – one where a company can show its face to a

French tax inspector and one which carries no aura of tax planning. The jurisdiction which eminently fits the bill is, of course, the United Kingdom.

Non-resident Company

Many readers will remember when the zero-tax non-resident English company was a popular offshore vehicle. Those happy days came to an end on the 15th March 1988[4], but the old non-resident company was effectively re-invented in 1994, in consequence of the coming into force of sections 249 – 251 of that year's Finance Act: under these provisions, a company incorporated in the United Kingdom, but qualifying as a resident of some other country for the purposes of a tax treaty, is to be treated for domestic purposes as not resident in the United Kingdom. At first blush, it does not look like a very interesting provision. Who would want to avoid tax in the United Kingdom in order to have the pleasure of paying tax in some other country? But that line of thought does not take into account the fact that some countries tax certain income very lightly, or not at all, and the United Kingdom has treaties with several of them. A company incorporated in the United Kingdom but resident in Mauritius may have a tax rate as low as 1.5%. One resident in Singapore will pay no tax on any of its foreign income, and most kinds of foreign income are similarly exempt in Malaysia. And if the company is resident in Barbados, it will pay local tax on its foreign income only if it remits such income to Barbados, which it is not obliged to do. None of these countries levies any tax on capital gains. One has to remember, of course, that shares in all UK-incorporated companies – whether they are resident or not – are subject to UK inheritance tax. If that is a problem, the UK company can have a parent company, incorporated elsewhere.

Corporate Partner

Another way of using a UK company is as the managing partner in a limited partnership formed under the 1907 Act, or a limited liability partnership, formed under the Act of 2000. Partnerships are transparent for tax purposes[5]: where a partner is non-resident and the partnership income has a non-UK source, the partner has no UK tax liability. Typically, the UK company will have only a tiny share, the bulk of the income going to one or more partners offshore. Customers, however, deal with the UK partner, and may by so doing be able to circumvent blacklist and similar problems.

One aspect of the transparency of the partnership is that – unlike a company – the tax liability is not affected by the "management and control" of the business. If the partners want to have partnership meetings in London and take decisions there about the management and control of the partnership business, they can feel free to do so. But if in the United Kingdom they do business with customers, their profits will have a UK source and be taxable accordingly. So if, for example, the partnership is in the business of buying refrigerators in Nigeria and selling them in Iceland, it needs to find somewhere outside the United Kingdom to negotiate with the customers and sign the contracts.

Corporate Trustee

A third use of the UK company is as a trustee. A trustee can carry on a trade, if it has power in its trust instrument to do so, and it can of course buy and sell assets and realise and re-invest gains. The UK tax system is very generous to UK-resident trustees of settlements made by non-resident and non-domiciled settlors. Moreover, the United Kingdom, unlike the offshore jurisdictions, does not require a company to have a licence to act as a trustee, nor does it require a trust company to have a name which suggests that it has anything to do with trusts. When the capital gains tax was introduced, in 1965, a tax-free regime was carved out for trusts established by non-residents. This was deliberately done, to protect the business of the established trust companies. A lot of tax planning involves taking advantage of loopholes the legislature never intended. But this is quite the opposite: Parliament has expressly provided a capital gains tax regime for the trust company incorporated in the United Kingdom, or managed and controlled there, which manages trusts as a business and acts as trustee of a settlement made by a settlor not domiciled, resident or ordinarily resident in the United Kingdom. While being fully taxable on the gains that it makes for itself, it is treated, in its capacity as trustee, as non-resident and is therefore not subject to capital gains tax on gains it makes in that capacity[6]. If there is a beneficiary who is absolutely entitled to the income, the trust will be “transparent” for income tax, just as a limited partnership is, with the result that non-UK income can pass through the trust to a non-resident beneficiary, without attracting any UK tax[7]. A "thin" trust – in which the non-resident settlor reserves to himself a life interest – is a simple, and cosmetically attractive, zero-tax vehicle. It has freedom from capital gains tax and freedom from income tax on its non-UK income.

Tax Treaties

Does the UK trust have a treaty-shopping aspect? The archetypal case is that of the Kuwaiti investor who plans to acquire a major share in a Spanish company. For any one or more of a variety of reasons, he may decide to establish a "thin" trust, appointing as trustee a company resident in the United Kingdom and inviting the trustee to make the investment. He is advised that if he were to make the investment himself, he would be liable to capital gains tax in Spain if he ultimately disposed of the shares at a profit. But what happens if the investments is made not by him but by the trust company? Article 13 of the tax treaty between the United Kingdom and Spain exempts a resident of the United Kingdom from Spanish tax on such a gain. At first sight, it seems illogical that the trust company can be non-resident by virtue of section 69(2) but at the same time resident for the purposes of the treaty. But that, it is submitted, states the position too simply. The use of the word "treated" in section 69, tells us that we are moving from the world of reality to the world of make-believe[8]. The section contains two statutory fictions. By subsection (1) the trust company is to be *treated* as a "single and continuing body of persons" (which it may or may not be), and the residence of that "body" is to be determined partly by reference to the residence of the trustees or a majority of them. By subsection (2) the trust company is to be *treated* (in the circumstances contemplated) as non-resident, which is the very opposite of the fact. These statutory fictions are not imported into the Income and Corporation Taxes Act: a resident trustee is liable to income tax on trust income without reference to income accruing to his predecessor or successor, and whether or not he is treated as non-resident for capital gains tax. Nor is there anything in the language of any of the tax treaties which suggests that these fictions are to be imported into them: the "alienator" entitled to the benefit of the treaty is the trust company; it is "liable to taxation" in the United Kingdom, by reason of its "domicile, residence, place of management or other criterion of a similar nature", as may be evidenced by its liability to corporation tax on its trust fees[9].

The "thin" trust does not offer any treaty relief on the *income* flowing into the trust. It is not every country which taxes gains arising from foreign investment, but countries as a rule do tax outgoing dividends, interest and royalties. Is there a UK trust appropriate to these? If there is no beneficiary with an interest in possession in the trust income, but the trustees are to accumulate the income or to distribute it at their discretion, the trust is not transparent: the income is that of the trustee, and the trustee is in principle liable to income tax on it. But if the UK trust company is only one of two or more trustees, and the other trustee or trustees are resident outside the United Kingdom, then, so long as the settlor is resident, ordinarily resident and domiciled outside the United Kingdom, the UK trust company will be treated for domestic purposes as non-resident (Finance Act 1989, s110), and the income may therefore be accumulated free of tax. It is submitted that income paid to the trust company is income of a resident of the United Kingdom for treaty purposes[10], although it is not "subject to tax" – a circumstance which is sometimes[11], but not by any means always, a condition of relief.

Stepping Stone

The "stepping-stone" concept is not new. Treaty shopping by interposing a Netherlands company between a copyright owner in a (say) the Bahamas and a user in a country with which the Netherlands has a tax treaty has been going on for many years. The Netherlands has tax treaties with a large number of countries and does not impose any tax on outgoing royalties. Tax authorities in some countries, however, have become intolerant of this royalty route, and practitioners looking for an alternative route have found the United Kingdom offers similar advantages without necessarily suggesting a tax avoidance motive. Outgoing copyright royalties (not in respect of a UK copyright) suffer no UK tax[12], but if the outgoing royalties are for the use of a patent, there is in principle a tax charge[13] – a charge which may not be suffered if the recipient is resident in a country with which the United Kingdom has an appropriate tax treaty. Barbados is attractive in this context: the royalties may be remitted to an international trust and distributed to beneficiaries elsewhere[14].

A UK company may also function as a kind of Stepping-stone for dividends. Suppose an operating company, resident in a high-tax country, is owned by an investor in a zero-tax jurisdiction. By interposing a UK holding company, dividends may be free of withholding tax, or suffer a lower rate of withholding tax than would be suffered if the dividends were paid direct to the investor: the UK holding company benefiting from a tax treaty or from the Parent/Subsidiary Directive. The United Kingdom gives tax relief to incoming dividends in the hands of the holding company, but does so in a different way from that adopted on the Continent. The Continental approach is to exempt the foreign dividend from tax, if the profits out of which the dividend is paid have suffered tax abroad. The British approach is to tax the foreign dividend, but to allow credit for the foreign tax, including tax paid on the operating company's profits[15]. The full rate of corporation tax in the United Kingdom is 30%. So it follows that so long as the operating company's dividend has suffered at least 30% tax abroad, the UK holding company enjoys the same freedom from domestic tax on the incoming dividends as is enjoyed under the Continental systems. Both systems offer an exemption from tax on gains on disposals of foreign direct investments (though the UK regime is new and not very user-friendly). But the United Kingdom does not nowadays levy any tax on outgoing dividends, so the zero-tax investor does not have to think about routing through the Antilles or funny gearing or prolonged liquidations, and it is this feature which has elevated the United Kingdom to the jurisdiction of first choice for this kind of Stepping-stone.

[1] This article is adapted from parts of a paper prepared for the meeting of the International Tax Planning Association in November 2003. Some of the material was published in the *International Tax Report* of October 2003.

[2] See Marshall Langer, in *ITPA Journal* Vol III No.3.

[3] From the Primarolo Report and the OECD Reports, respectively. See Philip Baker's article in this issue.

[4] Finance Act 1988 s.66.

[5] Income and Corporation Taxes Act 1988, ss.111, 112 and 182A; And see *GITC Review* Vol II No.1 page 67.

[6] See, now, section 69(2) of the Taxation of Chargeable Gains Act 1992, but note the provisions relating to a branch or agency, contained in section 10.

[7] See *Singer v. Williams* [1921] 1 AC 41.

[8] The statement in the text is implicit in the language of the subsection. Take the example, "Ludwig Wittgenstein paid the Germans a lot of money to have his sisters in Vienna treated as non-Jewish". One thing that statement tells us is that they were not actually non-Jewish, for if they had been, their brother would not have needed to pay the money. In abstract terms, "If X is to be treated as having quality Y, X does not actually have quality Y." In the context of section 69(2), the statement that the trustee is to be *treated* as non-resident, predicates that the trustee is not actually non-resident.

[9] The point is explored more fully by the author in a forthcoming issue of the *Offshore and International Taxation Review* (Keyhaven).

[10] The argument follows that outlined above in relation to section 69(2). The UK trust company is *treated* as non-resident as regards the trust income, just as it is as regards the trust capital gains, but it is nevertheless a "resident of the United Kingdom" for the purposes of a tax treaty. It is also "a company of a Member State" for the purposes of the EU Parent/Subsidiary Directive.

[11] e*.g.* in Article 11 of the treaty with Barbados.

[12] See Income and Corporation Taxes Act 1988, s.537 and *Simon's Taxes* B.819.

[13] Income and Corporation Taxes Act 1992, s.349.

[14] See GITC Review Vol I No 2 at page 23.

[15] Income and Corporation Taxes Act 1992, Part XVIII Ch II.

JUST SUPPOSING …

Hugh McKay

Introduction

By now, everyone knows that the House of Lords devised and applied a judicial anti-tax avoidance doctrine in a line of cases which started with *W. T. Ramsay v. IRC*[1] and ended with *Macniven v. Westmorland Investments Limited*.[2] However, practically each time they have had a chance to tackle this doctrine, they have gone about it in a different way, so that *Westmoreland* just happens to be the most recent and radical variation on this theme. However, even after 20 years of development, the exact shape of the concept remains elusive. One only need have regard to the difficulties expressed by the Court of Appeal in *Barclays Mercantile Business Finance v. Mawson*[3] to see that the dichotomy between legal concepts and commercial concepts explained in *Westmoreland* seems to raise as many problems as it solves, so that it is not surprising that the House of Lords will be hearing *Barclays Mercantile Business Finance* next year.

However, whatever the exact scope of this doctrine, it does not apply to all taxes. VAT is one notable exception (which also rather contradicts the notion of the doctrine being a rule of statutory construction): see further Lord Hoffmann, *C&E v. Thorn*

Materials Supply Limited[4]. This has lead to the first signs of a different approach to issues of VAT avoidance in the VAT and Duties Tribunal, based on concepts of European Law. I believe that these concepts will ultimately supplant *Ramsay/Westmoreland* as the judicial approach in the United Kingdom in direct tax cases, as well as VAT.

The European Court of Justice is due to hear three landmark VAT avoidance cases next year. Two of those case have been joined - *Halifax plc*[5] and *BUPA Hospitals Limited ("BUPA")*[6]; the other is *University of Huddersfield.*[7] Together those cases provide that Court with an opportunity to begin the development of the general principle of "abuse of rights" as a judicial anti-tax avoidance tool. It is true that Customs and Excise are putting forward two principal arguments, but one of those is limited in its application to VAT (or at least for now).[8]

Development and Integration of European General Legal Principles

In developing European law, the European Court extrapolates various general principles of law which it finds in the laws of the Member States and uses those principles to supplement the Treaties and other European instruments. In this way, principles like *legitimate expectation* and *proportionality* have been taken by the Court from their French and German origins and incorporated, as fundamental principles, into European law. Fundamental principles of European law then tend to be “imported” into our law and take on a role that can be somewhat separate from their European origins. There are several examples of this, and – referring to the two principles I have already mentioned – legitimate expectation has slowly grown in importance in English administrative law. In 1989, it was merely a “valuable developing doctrine”;[9] by only 2000, it had become a rule of English law capable of giving protection to an expectation of substantive benefits.[10] Similarly, the doctrine of proportionality has moved from a mere mention in *Council of Civil Service Unions v. Minister for the Civil Service*[11] to a firm part of English Law, admittedly by way of the incorporation of the European Convention on Human Rights into our law.

Whilst the notion of “abuse of rights” is a slightly difficult one for common lawyers (since the common law permits everything that it does not strictly prohibit, whereas civil law systems take the opposite approach), the fact that it is an unfamiliar and continental rule is not of itself a bar to its ultimate incorporation into United Kingdom tax law. Nor is the fact that it has not (yet) expressly been elevated into a general principle of EC law; it has been applied by the Court on several occasions and most Member States have such a principle as part of their law. *Halifax* will, I believe, be the case that promotes abuse of rights into such a principle, and, even if it does not, such a principle will incontrovertibly become part of United Kingdom VAT law.[12]

The fact that *Halifax* will be a decision in relation to VAT will not prevent abuse of rights from being of wider application. Principles of Community law are capable of application in all areas of Community law, and there are already a number of European-based rules in direct taxation. This being so, it is entirely possible that future questions on direct tax avoidance – and not necessarily United Kingdom questions – could come before the European court and follow a similar pattern to that illustrated by what I suggest will happen in *Halifax*.

Indeed, having regard to the pattern of incorporation of EC principles into our law, and the very relevant fact that the people who hear VAT appeals are also Special Commissioners, the question to be asked is not whether abuse of rights will become part of direct tax law, but rather, *when* will abuse of rights be the judicial anti-avoidance rule applied generally in all taxes.

Meaning of "Abuse of Rights"

According to the VAT Tribunal in *BUPA*[13] there is no generally accepted definition of "abuse of rights" in European law. In fact, in some of the earlier cases it is not even described in those terms. For example in *van Binsbergen*[14] the Court treated it as self evident that the Netherlands could take measures to prevent a Dutch lawyer resident in Belgium from using Article 59 of the Treaty of Rome[15] and they did not mention abuse of rights in terms.

It appears that the European concept of abuse of rights has developed in three particular sorts of circumstances.[16]

The first is where there has been an abusive use of Community law to circumvent provisions of national law. For instance, in *R v. Customs & Excise Commissioners, ex parte EMU Tabac and Others*[17] where there was an attempt to use an Excise Duty Directive[18] in a scheme to supply tobacco from Luxembourg to individuals in the United Kingdom via an agency arrangement without the payment of UK duty. The Advocate General (but not the Court) referred to "abuse of rights" –

> "…if it were necessary to do so as a last resort, the national court could decline to apply the rule contended for by the appellants … on the basis that to apply it to the present case would clearly run counter to the spirit and purpose of the directive and would be inimical to the effectiveness of other provisions of it. By so doing it would merely be applying the general legal principle prohibiting acts in fraud of the law"[19]

Stripped down, it can be seen that this is simply an expression of the purposive rule of interpretation.[20] This, of course, makes it very similar (in one sense) to the *Ramsay/Westmoreland* doctrine, which further suggests that it will not be too difficult replacing (refining even) *Ramsay* with the European concept. Furthermore, this first set of circumstances is the one most likely to give rise to an application of abuse of rights in direct tax. If one thinks of the variety of European Directives applying to the direct taxes (say, the Parent/Subsidiary Directive[21]) or even the Treaty of Rome, it is fairly easy to think of occasions when the Inland Revenue might think of putting the argument to counteract a taxpayer's arrangements. In *BUPA*, the Tribunal suggested that the principle as manifested in this first area seemed to have two forms – the purposive interpretation rule and a rule which disqualifies claims which amount to the abusive use of EC law to circumvent national law. I am not sure that I agree, since the former is an expression of what the rule is, and the latter is an expression of what its application means: that does not seem like two manifestations of a rule. However, it probably does not matter very much, since a quibble like this would not stand in the away of its importation into United Kingdom tax law.

The second instance where abuse of rights has been applied by the European Court is where there is an "abusive" use of Community law to gain a financial advantage from Community funds.[22] In a tax matter this is unlikely to arise. But since this second instance has produced the recent and influential case of *Emsland-Stärke GmbH v. Oberfinanzantduektion München*[23] ("*Emsland-Stärke*"), it merits mention. This is because *Emsland-Stärke* elevates abuse of rights from merely an aid to interpretation to a separate free-standing principle of Community law. In *Emsland-Stärke*, a German exporter exported goods outside the Community (to Switzerland). Immediately after the goods had been released for home use in Switzerland, they were transported back into the Community (Germany and Italy) and were there released for home use on payment of import duties. The German company had sought and obtained export refunds[24] based on the Swiss Customs' papers and freight documents.[25]

According to the European Court in *Emsland-Stärke* there are two conditions which must be satisfied to establish a finding of abuse of rights: the first is objective; the second subjective.

The first requirement is at paragraph 52 of the Court's judgment:

> "A finding of an abuse requires, first, a combination of objective circumstances in which, despite formal observance of those conditions laid down by the Community rules, the purpose of those rules has not been achieved."

The analysis here begins by examining the purpose of relevant provisions (which, is nothing more than another expression of the purposive rule of interpretation) and determining that that purpose has not been complied with. However, it is not clear how one makes this determination at the first stage: it seems to me that one may only do this by incorporating the second test or making some sort of value judgment at this stage. This is supported by the Commission, who had submitted that this first element required "evidence that the conditions for the grant of a benefit were created artificially, that is to say, that a commercial operation was not carried out for an economic purpose but solely to obtain from the Community the financial aid that accompanies the operation". They elaborated that this meant that one must undertake an analysis, on a case-by-case basis, of both the meaning of the provision and the conduct of a prudent trader who manages his affairs in accordance with the applicable rules of law and with current commercial and economic practices in the sector in question.[26] This approach, though not taken up by the Court itself, seems eminently sensible: judges are lawyers, not economists or business-people. To incorporate an evidential requirement so that they can hear what the prudent business-person would do according to expert evidence witnesses must be far more satisfactory that the hazarding of an uninformed guess – which is the *Ramsay/Westmoreland* position.[27]

And the second condition is at paragraph 53, it is that there is

> "… the intention to obtain an advantage from the Community rules by creating artificially the conditions for obtaining it".

This is more difficult, since the one must see into the minds of the parties to a transaction and determine that they have a particular intention at a particular point, which causes them to do something "artificial". In some cases this will not be too difficult: a case where a lorry load of goods takes a trip to a non-EC country and returns without anything happening, except certain customs formalities are complied with is such a case. But greater difficulties will be experienced in more complicated commercial transactions. It should be remembered that as a rule of common sense, if not law, "no commercial man in his senses is going to carry out a commercial transaction except on the footing of paying the smallest amount of tax he can".[28] And in such cases there will be difficult commercial issues for the Court to grapple with. The EC Commission's approach would be useful in such matters in respect of this second element, as well as the first. I hope that either a United Kingdom Court or the European Court sees the value of a requirement for expert witnesses, so that the abuse of rights doctrine can, even from its early days, incorporate valuable, additional evidential requirements: after all, we do not expect judges to decide, without expert help, what reasonable doctors do; but we have allowed them to say, unguided, what reasonable businessmen do.

Consequences

In the United Kingdom we have a very thick body of tax legislation. Much of it is anti-avoidance legislation. And whenever a new relief is introduced, the substantive provisions are often quite short, compared to the thicket of anti-avoidance provisions that accompany them. I believe if "abuse of rights" were part of the United Kingdom's general tax law, we could have new legislation with that thicket cut away. It could even render large parts of the existing legislation redundant: for example, imagine the Group Relief rules without

Schedule 18 of the 1988 Act, as well as much of Chapter IV, Part X.

However, the price of such a development will probably be a loss of certainty as to how the rest of the tax law would apply. The two *Emsland-Stärke* conditions are a little opaque and will need further development, and, as I have suggested, that should come with carefully elaborated requirements about evidence – especially expert evidence – so that the matter does not become one of judges guessing at what a reasonable business-person would do.

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[1](1981) 54 TC 101.
[2][2001] STC 237.
[3][2002] STC 66, 86-7 & 92-3.
[4][1998] STC 725, 739h-j.
[5][2002] STC 402 and [2001] V & DR 73.
[6][2002] V&DR 428.
[7]Decision Number 17,854.
[8]Apart from "abuse of rights", Customs are arguing that where something is undertaken wholly for the purposes of VAT avoidance, it is not a true "business" or "economic activity" within the meaning of Value Added Tax Act 1994 or the 6th EC VAT Directive. Since those arguments are peculiar to VAT law, I say nothing further about them.
[9]See *R v. IRC ex parte MFK* [1989] STC 873, 892j (Bingham LJ).
[10]See *R v. North & East Devon Health Authority ex parte Coughlan* [2001] QB 213, where the very severely disabled applicant had been told by the health authority, on moving from a hospital being closed by the authority to an NHS facility, that the facility would be her home for life. The authority later sought to close the facility. The Court said that it could not, because to do so would be so unfair that it would be an abuse of power to frustrate the applicant's legitimate expectation that the authority would not resile from its promise.

[11][1985] AC 374, 410E (Lord Diplock).
[12]At the moment, differently constituted VAT & Duties Tribunals have taken different views as to whether abuse of rights could or should be part of our VAT law: compare *Blackqueen* (17,680) with *RBS Property Developments Limited* (17,789).
[13][2002] V&DR 428, 468.
[14][1974] ECR 1299, 1309, paragraph 13.
[15]which provides for the progressive removal of restrictions on the freedom to provide services by a person established within one Member State in other Member States.
[16]The third situation, which is not relevant in the United Kingdom, is where Community law has been used in a manner which is alleged to be contrary to a national abuse of rights provision.
[17][1998] ECR I-1605, known as the "Man in Black" or "Death Cigarettes" case.
[18]92/12/EEC.
[19][1998] ECR I-1605, 1627-8 (paragraph 89).
[20]See also, *Centros Ltd. v. Ehrvorvs-og Selskabsseyrel-sem* [1999] ECR I-1459, 1476 where the Advocate General said that to determine whether or not a right is actually being exercised in an abusive manner is simply to define the material scope of the right in question.
[21]4325/90/EEC.
[22]The basis for this appears to be Article 4(3) of Council Regulation 2988/95, concerning the protection of the Community's financial interests – according to which acts which are established to have as their purpose the obtaining of an advantage contrary to the objectives of Community law applicable in that case, by artificially creating the conditions required to obtain that advantage, shall result in the advantage being withdraw or withheld.
[23][2000] ECR I-11579.
[24]Such refunds are designed to compensate for the difference between commodity prices within the Community and international market prices – so as to make Community products competitive on the world market. In this way, their sale outside the Community becomes commercially viable, and effect is given to one of the intentions of the common agricultural policy: see further the second recital in the preamble to Council Regulation 800/99.

[25]Thus apparently satisfying the *formal* requirements for export refunds under Articles 9(1), 10(1) and 20(2-6) of Regulation 2730/79.

[26]See paragraph 39 of the Court's judgment.

[27]The Commission also asserted that there was a third – procedural law pre-condition – but the Court did not accept this.

[28]Lord Upjohn, *IRC v. Brebner* [1967] 2 AC 18, 30F-G and see also *Craven v. White* (1988) 62 TC 1, 171 A-B.

MARD

Issues Arising from the Mutual Assistance in the Recovery of Debts Directive

Aparna Nathan

Introduction

The general principle governing the cross border recovery of tax debts has, generally, been the rule set out in *Government of India v Taylor* [1955] AC 491: one territory will not help in the recovery of a tax debt due to another territory.

European incursions into this principle began in 1976 (76/308/EEC) which dealt with the recovery of claims forming part of the system of financing the European Agricultural Guidance and Guarantee Fund and of agricultural levies and customs duties. The 1976 Directive was extended in 1979 to cover the recovery of VAT (79/1071/EEC).

Directive 76/308/EEC was once again amended in 2001 so that claims relating to taxes on income and capital and insurance premium tax were included within the scope of the directive (2001/44/EEC). The Directive on mutual assistance on recovery of tax debts ("MARD") as amended was enacted into UK law by Finance Act 2002 ("FA 2002").

Given the extensive nature of the taxes covered by MARD, as well as the manner in which it has been enacted into UK law, it is increasingly likely that tax practitioners will come across recovery proceedings under MARD / FA 2002 in practice. The author seeks to draw on the experience gleaned from a recent MARD /FA 2002 recovery case in which the author was involved in order to highlight some of the interesting issues of principle and practice that arise in such proceedings.

Principles of MARD

MARD provides, broadly, that the competent authority in the territory in which the tax debt arises (“the Applicant Authority”) can request the relevant authority in another territory to which a request for assistance is made (“the Requested Authority”) to provide any information which would be useful to the Applicant Authority in the recovery of its claim (Art 4) or to enforce the tax debt (Art 6). The Requested Authority is usually situated in the territory in which the taxpayer is resident or holds assets or where the source of the income is situated.

In complying with the request for assistance under MARD, the Requested Authority makes use of the powers provided under the laws, regulations or administrative provisions in the Requested Authority’s territory which apply to the recovery of similar claims arising in that territory.

Article 7 (as amended) sets out the procedural rules governing the Applicant Authority’s request for enforcement of a claim. Of note is the rule that, except in circumstances falling within the second sub-paragraph of Art 12(2), an Applicant Authority may not make a request for recovery if the claim and/or instrument permitting recovery are contested in the Applicant Authority's territory.

The second sub-paragraph of Art 12(2) provides that the Applicant Authority may make a request for recovery of a claim that is contested in so far as the relevant laws, regulations and administrative practices in force in the territory in which the Requested Authority is situated allow such action.

UK Enactment

MARD was enacted into UK legislation in FA 2002 s134 and Sch 39. Para 2 Sch 39 FA 2002 provides that the UK authority (e.g. the Inland Revenue or the Commissioners of Customs & Excise) may take such proceedings to enforce the foreign claim by way of legal process, distress, diligence or otherwise, as might be taken to enforce a corresponding UK claim.

A "corresponding UK claim" is a claim in the UK corresponding to the foreign claim. Sub-paras 3(1) and (2) Sch 39 FA 2002 provide that the Treasury may, inter alia, provide by regulations what is a corresponding UK claim in relation to any type of foreign claim.

Para 3(4) Sch 39 FA 2002 empowers the relevant UK authority (i.e. the Inland Revenue or the Commissioners of Customs &Excise) to make provisions by regulations as to the application, non-application or adaptation in relation to foreign claims of any enactment or rule of law applicable to corresponding UK claims. However, this is without prejudice to the application of any such enactment or rule in relation to foreign claims in circumstances not dealt with by regulations under para 3(4) Sch 39 FA 2002.

Para 4 Sch 39 FA 2002 enacts the requirement set out in Art 7 MARD that no proceedings under Sch 39 FA 2002 shall be taken against a person if he shows that proceedings relevant to his liability on the foreign claim are pending, or are about to be instituted, before a court, tribunal or other competent body in the foreign territory in question.

Proceedings are "pending" so long as an appeal may be brought against any decision in the proceedings. It must be noted that proceedings under Sch 39 FA 2002 may be taken if the proceedings in the foreign territory are not prosecuted or instituted with reasonable expedition.

Para 5 Sch 39 FA 2002 provides that no proceedings can be instituted under Sch 39 FA 2002 if a final decision on a foreign claim has been given in the taxpayer's favour by a court, tribunal or other body in the foreign territory in question. A final decision is one against which no appeal lies or against which an appeal does lie but the period for making the appeal has expired without an appeal being made.

Para 6 Sch 39 FA 2002 stipulates that for the purposes of proceedings under Sch 39 FA 2002, a request made by an authority of a foreign territory shall be taken to be duly made in accordance with the MARD unless the contrary is proved and, except as mentioned in para 5 Sch 39 FA 2002, no question may be raised as to the person's liability on the foreign claim.

Issues of Principle Arising from UK Enactment

Sch 39 FA 2002 raises at least three controversial issues: first, it is not possible to contest the foreign claim in proceedings brought under Sch 39 FA 2002; second, Sch 39 FA 2002 is potentially retrospective because it can, in theory, apply to claims which arose before the MARD and Sch 39 FA 2002 were enacted; and, third, the Applicant Authority can request assistance in recovery under MARD even where the foreign claim is contested.

First Issue

There is arguably some sense in limiting the right to contest a foreign claim to the territory in which the claim arose on the basis that the tax laws that give rise to the foreign claim will be better understood in that foreign territory than in the territory in which recovery is sought. For instance if the UK tax authorities institute recovery proceedings under Sch 39 FA 2002, and the taxpayer seeks to contest the claim in the recovery proceedings, the UK tax authorities may not know the relevant foreign tax laws and may well be unable to accurately assess the legitimacy of the foreign claim or the legitimacy of the appeal.

The main exception to the principle that the foreign claim cannot be contested in the recovery proceedings is where the foreign claim has already been decided in the taxpayer's favour. Such an exception is clearly fair in principle. After all, it should not be possible to enforce a foreign claim if it has been decided that that foreign claim does not exist.

Further, the exception in para 5 Sch 39 FA 2002 to the rule that the foreign claim cannot be contested in the recovery proceedings has the additional merit of practical efficacy because it should be fairly easy for the taxpayer to demonstrate that the relevant court in the foreign territory has decided the contested tax claim in the taxpayer's favour.

Second Issue

The potential retrospectivity of the legislation is less defensible. Neither MARD nor Sch 39 FA 2002 limit the application of the recovery proceedings to claims that arose after the coming into effect of MARD or FA 2002.

However, it must be noted that Art 14(b) MARD does state that the Requested Authority (in our case, the UK tax authorities) is not obliged to assist in recovery of a foreign claim if the first request for assistance in recovery is made more than five years after the foreign claim arose. The five year time limit runs from the date that the claim is established under the laws of the foreign territory and ends with the date that the request for assistance is made. If the foreign claim is contested, the five years run from the time when the foreign claim can no longer be contested.

Consequently, it is possible for recovery proceedings to be instituted in respect of a foreign claim that arose prior to the enactment of MARD and FA 2002.

Third Issue

Art 12(2) MARD permits an Applicant Authority to make a request for assistance even if the foreign claim is being contested provided that the laws, regulations and administrative practices of the territory of the Requested Authority allow such action. This provision is potentially inequitable because recovery is possible in respect of a contested tax claim even before that contested tax claim has been established by an independent court, tribunal or other body.

In the UK, the potential unfairness of Art 12(2) MARD has been reduced by para 4(1) Sch 39 FA 2002. This provides, subject to one exception, that no proceedings can be instituted under Sch 39 FA 2002 in respect of a foreign claim that is contested. The exception is that recovery under Sch 39 FA 2002 is possible in respect of contested foreign claims where regulations under para 3(4) Sch 39 FA 2002 apply an enactment that permits such proceedings in the case of a corresponding UK claim.

At present, no regulations have been made under para 3(4) Sch 39 FA 2002. Consequently, the UK tax authorities cannot seek to enforce a foreign claim that is contested. Further, and more importantly, it follows that no valid request for assistance can be made by an Applicant Authority to a UK tax authority in respect of a contested foreign claim because the requirements of the second sub-paragraph of Art 12(2) MARD are not satisfied.

Practical Issues Arising from the UK Enactment

It should be safe to assume that, where a taxpayer has a foreign tax claim and is contesting it in the foreign territory, no proceedings for recovery in respect of that foreign claim will be instituted under Sch 39 FA 2002.

Sadly, this is not necessarily true. Experience has shown that, despite the words of the legislation, recovery proceedings may be instituted under Sch 39 FA 2002 even in respect of a contested claim. The situation arises as follows:

(1) MARD permits an Applicant Authority to request assistance in recovery where the claim is contested provided that recovery of a corresponding claim is possible under the laws etc of the territory of the Requested Authority (Art 7 and 12(2) MARD).

- The flaw with the proviso in Art 12(2) is that the Applicant Authority is required to be sufficiently conversant with the laws of the territory in which the

Requested Authority is situated in order to determine whether it, i.e. the Applicant Authority, is permitted to rely on the proviso in Art 12(2) and make a request for assistance. In the author's view, this, perhaps, places too great a burden on the tax authorities of our European neighbours. It is by no means certain that these foreign tax authorities enter into an assessment of the laws of the territory in which the Requested Authority is situated in order to determine whether the foreign tax authorities can rely on the second sub-paragraph pf Art 12(2) MARD. It is, therefore, possible, as happened in a recent matter in which I was involved, that the Applicant Authority will make the request for assistance in any event.

(2) The Applicant Authority makes the request for assistance to the Requested Authority.

- Given the fact that the UK laws do not permit UK tax authorities to enforce contested foreign claims, such a request is invalid under Art 12(2) MARD;

(3) In accordance with para 6(a) Sch 39 FA 2002 the UK tax authorities treat the request for assistance a being validly made under the provisions of MARD *unless the contrary is proved*.

- In other words, the UK tax authorities must comply with the request for assistance in recovery if such a request is made. It is not clear who is required to prove that the request made by the Applicant Authority has not been made in accordance with MARD. It is unlikely, given the paucity of government resources, to be the UK tax authorities. In fact, the words of para 6(a) Sch 39 FA 2002 appear to prevent the UK authorities from checking the validity of the request for assistance. It seems probable, therefore, that the first point at which the validity of the request will be impugned will be when the taxpayer, against whom enforcement is sought, raises the point. This seems to place an unnecessary burden on the taxpayer who is already contesting the foreign claim in the territory in which the Applicant Authority is situated. The taxpayer, therefore, has to bear the time and expense of two separate actions in two different territories relating to the same contested claim. This seems somewhat iniquitous.

(4) The taxpayer against whom recovery of the foreign claim is sought is not permitted to contest his liability except where he can show that the foreign claim has already been determined in his favour by the courts of the foreign territory.

In the light of the foregoing, and entirely inconsistent with the words of the Sch 39 FA 2002, it is possible for recovery proceedings to be instituted under FA 2002 in circumstances where the foreign claim is contested.

Quite apart from seeking recovery in respect of contested foreign claims is the situation where the foreign claim in respect of which assistance is sought by the Applicant Authority is not the tax liability itself (contested or otherwise) but, as happened in the case with which I was involved, is security for a contested tax liability.

It is not clear whether a claim for security in relation to a contested tax liability is the type of foreign claim that is meant to be covered by MARD. The opening words of Art 2 MARD speaks of "all claims relating to". This phrase is arguably broad enough to cover established tax debts, contested tax debts as well as interlocutory measures such as security for the tax debts (contested or otherwise). That contested tax debts are not meant to be recoverable (except in certain circumstances) under MARD is evidenced by Art 7 and 12 MARD.

However, the matter of interlocutory measures is not expressly dealt with by MARD. Arguably, the aim of MARD, as gleaned from the words of the Directive, is to enforce established tax debts i.e. tax liabilities that are final and conclusive and not subject to further appeal (see Arts 7 and 12 MARD). Other language versions of the Directive (French, Finnish and Swedish) seem to support this view: the opening words of Art 2 MARD in these foreign language versions use words that mean "claims *or debts* relating to". The implication of the reference to "debts" suggests that there should be an established final tax liability. As a result, it is arguable that MARD should not be used to enforce interlocutory measures, such as security, for an unestablished tax liability.

Issues Arising From the Mechanics of Recovery Proceedings

The UK tax authorities, when complying with a request under MARD, rely on the Civil Procedure Rules ("CPR") mechanisms to enforce the tax debt i.e. they seek third party debt orders and charging orders (CPR Parts 72 and 73).

The applications for such orders are made either in the County Court or in the High Court. Initially, interim orders are sought without notice to the taxpayer / debtor and are granted without a hearing. These interim orders are made final after a hearing at which both the Revenue and the taxpayer/debtor are present.

The procedure for obtaining these orders appears to place the taxpayer/debtor at a disadvantage: he is not told about the UK tax authority's application for an interim third party order or charging order, and has an order made against his assets as a result of which he is no longer free to deal with those assets.

Further, although the Court has discretion whether to grant the interim orders, it does so on the basis of the papers. The Court may refuse to make an interim charging order if the result would be oppressive – perhaps because the amount of the debt is too small to warrant a charge on the assets. Of importance is the fact that this procedure does not permit the Court, when exercising its discretion to grant the interim order, to determine whether the application by the UK tax authorities is validly made i.e. effectively, whether the request under MARD was validly made by the Applicant Authority. It is, therefore, possible for the taxpayer /debtor to be subject to an interim order even though the request for assisntace under MARD was invalidly made by the Applicant Authority.

Interim orders, once granted, continue until they are made final. The Court has discretion in deciding whether to make the interim orders final. The burden of showing why an interim order should not be made final is on the taxpayer/ debtor. This is the taxpayer/ debtor's first opportunity to object to the UK tax authorities' enforcement actions, for instance, on the grounds that the Applicant Authority has no right to make a request for assistance under MARD because the foreign claim is being contested.

It is the author's view that the opportunity to impugn the validity of the Applicant Authority's request under MARD comes too late – the taxpayer/ debtor has already been prejudiced by the grant of the interim third party and / or charging orders.

An added concern relating to the CPR recovery procedures is that the proceedings are generally heard in the County Court by a District Judge. It is the author's view that this forum may be inappropriate to deal with the important issue of the UK tax authorities' jurisdiction to bring recovery proceedings. This is based on two factors: first, the time allotted to such hearings tends to be wholly inadequate- matters are initially set down for 5 minutes unless representations are made to the court clerk that important issues and significant sums are involved, in which case the time allocated to the hearing may be slightly extended.

Secondly, there is some concern that the subject matter of MARD / FA 2002 hearings, involving matters of law and principle, are outwith the general run of matters dealt with by County Courts. District Judges (for it is they who usually deal with third party debt orders and charging orders) are more used to dealing with small claims actions and matters generally turning on factual issues and so may not, perhaps, be the most appropriate persons to deal with MARD / FA 2002 jurisdiction issues.

The UK tax authorities, in the recent case in which I was involved, withdrew the case after the first (five minute) hearing before the District Judge, when it became apparent from the Appellant's skeleton argument that the Applicant Authority had not made a valid request for assistance under MARD: the foreign claim was being contested in the foreign territory, and the UK tax authorities were not permitted by the laws of the UK (para 4(1) Sch 39 FA 2002) to enforce a claim that was being contested. The interim orders were, therefore, discharged.

The net result of this exercise was that the taxpayer/debtor had to expend time and money in order to show that the UK tax authorities had no jurisdiction to enforce the foreign claim in the first place. In our case, the UK tax authorities agreed to pay the costs of the action. However, it is arguable that payment of costs alone does not adequately recompense the taxpayer/debtor for the anxiety pending the hearing nor for the taxpayer/debtor's inability to deal with the assets subject to the interim orders.

Conclusion

From the foregoing, it is clear that MARD and its UK enactment in FA 2002 raise several issues of principle and practice. One of the difficult issues relates to the commencement, by the UK tax authorities in compliance with MARD, of enforcement proceedings in respect of contested claims.

Given the fact that a number of taxpayers now resident in the UK were recently resident in an EU country, it seems likely that the UK tax authorities will face a high volume of requests for assistance under MARD. Further, given the apparent inability on the part of the UK authorities to check the validity of the requests made under MARD by the Applicant Authorities, it seems increasingly likely that FA 2002 proceedings will be brought which may, where the taxpayers/debtors resist such proceedings, eventually be abandoned by the UK tax authorities.

It is, therefore, in the interest of taxpayers/debtors to ascertain whether the UK tax authorities have the jurisdiction to bring such recovery proceedings. Although this course of action could be expensive, at least initially, it may well be rewarded with a withdrawal of the recovery proceedings by the UK tax authorities.

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