Hide and seek

Unpublished Special Commissioners' decisions must stay hidden to maintain justice and fairness. **OLIVER MARRE** explains the recent decision of the First-tier Tribunal in *Ardmore v HMRC*.

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The recent First-tier Tribunal (FTT) judgment in *Ardmore Construction Ltd v HMRC* TC/2011/07724 concerns two issues, one procedural and the other substantive, and each in its own way is of great importance to taxpayers. The procedural issue relates to whether a party in tribunal proceedings can cite an unpublished Special Commissioners' decision. The FTT held that it cannot. The substantive issue is the correct test for identifying the location of the source of interest income. The FTT held that the right approach is to apply a multi-factorial test.

Unpublished decisions

HMRC have access to a large number of judgments that, generally, taxpayers cannot know about. These are the decisions of the Special Commissioners which, before 1994, were unpublished and unreported. HMRC would naturally have been a party, but the judgments, being unpublished, were not available to other taxpayers or their advisers.

When an unpublished Special Commissioners' decision is favourable to the case HMRC wishes to present to the FTT, they will seek to rely on it. However, when an unpublished decision favours the taxpayer's argument before the FTT, the taxpayer – being ignorant of the decision – would not be able to cite it.

In *Ardmore*, HMRC sought to rely on the unpublished decision in *Poldi (UK) Limited v CIR* (1993). Counsel for Ardmore argued that they should not be permitted to do so for three reasons: first, to ensure a fair trial; second, because the rule of law dictates that the law should be known and not hidden from the populace at large; and third, because of the practice of the courts.

For the taxpayer in *Ardmore*, the situation was further complicated by the fact that HMRC had, just weeks earlier, cited the unpublished decision in *Poldi* to another FTT, which then published its own judgment, relying on *Poldi* in coming to its decision. Therefore, Ardmore had to argue not only that the FTT should disregard *Poldi*, but also that the tribunal must ignore the earlier published FTT decision because it was reliant on *Poldi*.

The FTT in *Ardmore* first considered the question of the usual practice of the courts in relation to unpublished decisions. Counsel for Ardmore drew the tribunal's attention to HMRC's Revenue Interpretation 125 (19 October 1995), which was published a few months after Special Commissioners' decisions began to be published. In this document, HMRC noted:

> "The Special Commissioners have indicated that they will expect, in future, to have their attention drawn in appropriate cases to any of their previous published decisions which are relevant (but not to unpublished decisions)…"

Ardmore then relied on the decision of the Special Commissioner in *TSB Bank Plc (Antrobus Deceased) v CIR* [2002] SSCD 468, who expressly disregarded an earlier, unpublished Special Commissioners' decision, saying:

> "Because this decision was unpublished, and so cannot be identified in this decision, I have not relied upon it in reaching my decision."

KEY POINTS

- Historically, HMRC have sought to rely on unpublished Special Commissioners' decisions.
- Decisions unfavourable to HMRC may be ignored and taxpayers are unaware of these.
- The First-tier Tribunal holds that unpublished decisions must be ignored to ensure a fair trial.
- The tax significance of sources of interest.
- The source of interest must be determined using a multi-factorial approach.

Fairness and justice

The same approach was followed in *Henke v HMRC* [2006] SSCD 561. Although there are a few reported cases where HMRC have cited unpublished decisions, and the FTT (or even the Upper Tribunal) has relied on them in reaching a judgment, counsel for Ardmore submitted that the propriety of citing an unpublished case had not been considered in those instances.

The FTT then considered the question of fairness and the rule of law. In doing so, it considered its own responsibility to apply the overriding objective under Rule 2 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules SI 2009/273, to "deal with cases fairly and justly", in ways that are "proportionate" to the "resources of the parties". The tribunal also considered the importance of the rule of law and relied on the statement of Lord Diplock in *Fothergill v Monarch Airlines Limited* [1981] AC 251 at 279 that "elementary justice" or the "need for legal certainty" requires a taxpayer to know the law by means of ascertainable and publicly published sources. The FTT concluded:

> "There must be thousands of unpublished decisions known by and available only to HMRC. In our view, given that a persuasive authority, unless considered to be wrong, will as a matter of judicial comity be followed by the FTT, it cannot be right or just for HMRC to have such an advantage over a taxpayer."

Having reached this decision, the FTT went on to state, briefly, that a recently published FTT decision, which had not applied this law but had taken into account an unpublished Special Commissioners' decision, must also be disregarded.

This decision is to be welcomed. It is also interesting to consider the extent to which the same arguments for legal certainty and a fair trial should apply to Special Commissioners' and FTT decisions that have been published, but which are not reported, because it is not always possible to locate these judgments. (The FTT decision in *Ardmore*, by way of example, is not yet available.)

Source of interest

The FTT went on to consider the question of the source of interest income in the absence of the authority of either the Special Commissioners' decision or the earlier FTT ruling. The facts of the case, which are set out in the judgment, were agreed between the parties.

The dispute was in respect of interest paid by Ardmore to offshore trusts and companies. If the interest was interest "arising in the United Kingdom", then Ardmore was liable to withhold income tax on the payments, under ITA 2007, s 874, by deducting and accounting to HMRC at a rate of 20%. If, on the other hand, it was non-UK source income, there was no outstanding charge to tax.

The result of the agreed facts was that, if the FTT agreed with HMRC and decided that the correct test for the source of income is to balance various factors including the residence of the debtor, the substantive origin of funds out of which the interest was paid, the situs or location of the debt and the jurisdiction in which proceedings might be brought to enforce the interest obligation, the source of interest would be the UK. If, on the other hand, the FTT agreed with Ardmore that the source of interest is not multi-factorial, but is located in the place where credit is provided, the source of interest would be outside the UK.

The source of interest income is, of course, relevant not only for withholding tax under s 874, but also for the remittance basis for non-UK domiciliaries (income must have a source outside the UK to qualify as relevant foreign income and so to qualify for the remittance basis) and the territorial scope of the taxation of the income of non-UK residents under ITTOIA 2005, s 368 (which states that savings and investment income arising to a non-UK resident is chargeable to tax under ITTOIA 2005, Part 4 only if it is from a source in the UK).

Arguments for and against

HMRC relied on the House of Lords in *Westminster Bank Executor and Trustee Co (Channel Islands) Limited v National Bank of Greece SA* (1970) 46 TC 472. In this case, the National Bank of Greece issued bearer bonds but, when it defaulted, a guarantor paid the interest. Initially, the original debtor and the guarantor both had no connection to the UK. But, over time, the guarantor (who originally had no branch in the UK) acquired a branch in the UK and the bonds (which were originally enforceable in Greece) became enforceable in the UK. The question before the court was therefore whether the location of a source of interest is fixed, or whether it moves with changes of circumstances. However, HMRC relied on it as authority for the proposition that, in order to ascertain the source of interest, all features of the loan are relevant and, if different features point in different ways, determining the source of interest is a matter of carrying out a balancing exercise. I cannot find this in the *Bank of Greece* judgment, but the FTT agreed with HMRC.

In support of the taxpayer, it was argued that *Bank of Greece* could not be relied on as authority for a multi-factorial approach, whereas there was authority from commonwealth jurisdictions that the correct test was the one for place of credit. In several of these cases, the courts have held that the place of credit test would give the source of interest. However, in its judgment, the FTT decided that, in at least one of these commonwealth cases, the court had looked at various factors before deciding that it would give most weight to the place of credit. The FTT also expressed doubt as to the strength of the authority of the commonwealth decisions.

Subject to appeal?

HMRC will, therefore, continue to apply a multi-factorial approach for now. However, Ardmore is understood to be appealing and the state of the law on the source of interest is not, to my mind, any more certain after the FTT decision than it was before. The commonwealth authorities may fare better before a higher court and the *Bank of Greece* case should be confined to authority for the point it actually decides.

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