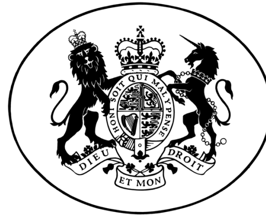

TC02194

Appeal number: TC/2010/2769

Income tax – claim for relief for interest paid under s 353 ICTA – whether payment of net present value of interest to accrue was "interest" eligible for relief – whether interest paid in excess of a reasonable commercial rate – whether interest relief was sole or main benefit expected to accrue to taxpayer from the transaction under which the interest was paid – s 787 ICTA

Settlement agreement – s 54 TMA, s 5 CRCA – whether ultra vires as a forward tax agreement – whether voidable for material non-disclosure – whether applicable for periods after disposal by taxpayer of relevant investments

FIRST-TIER TRIBUNAL
TAX CHAMBER

GARRETT PAUL CURRAN **Appellant**

- and -

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

TRIBUNAL: JUDGE ROGER BERNER
NIGEL COLLARD

Sitting in public at Victoria House, Bloomsbury Place, London WC1A 2EB on 13 – 22 June 2012

Malcolm Gammie QC, instructed by Herbert Smith LLP, for the Appellant

Jonathan Fisher QC and Hui Ling McCarthy, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

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DECISION

1. Mr Curran's appeals relate to three payments made by him in respect of three loans used to finance the acquisition of loan notes in two close companies carrying on property investment business. The loans were made in 2002, 2003 and 2007, and the payments in dispute were also made in the corresponding years. In each case the payments satisfied in full Mr Curran's obligation to pay interest under the relevant loan. Tax relief was claimed under s 353 of the Income and Corporation Taxes Act 1988 ("ICTA").

2. The appeals are against the following decisions made by HMRC:

(1) A closure notice issued on 31 October 2008 in respect of Mr Curran's self assessment for the year ended 5 April 2007 the conclusion of which was that Mr Curran was not due a deduction or relief for the following amounts:

(a) £40,000 (in respect of the 2002 Loan for £1,000,000);

(b) £32,938 (in respect of the 2003 Loan for £850,000);

(c) £2,594,028 (in respect of the 2007 Loan).

As a result of the consequential amendments to Mr Curran's self assessment, there was an increase in tax due of £1,049, 340.55. Mr Curran appealed against the closure notice on 10 November 2008.

(2) Notices of assessment ("discovery assessments") issued by HMRC under s 36 of the Taxes Management Act 1970 ("TMA"). Under those assessments Mr Curran was charged to tax:

(a) £29,174.40 for the tax year ended 5 April 2006;

(b) £29,950.70 for the tax year ended 5 April 2005;

(c) £29,176.00 for the tax year ended 5 April 2004;

(d) £167,157.59 for the tax year ended 5 April 2003; and

(e) £177,999.90 for the tax year ended 5 April 2002.

Mr Curran appealed against the discovery assessments on 27 January 2009.

The issues

3. Put shortly, the issues between the parties are as follows:

(1) *The Interest issue*. Whether the three payments ("the Payments") made by Mr Curran of:

(a) £899,995 on 5 April 2002 ("the 2002 Payment");

(b) £755,788 on 28 March 2003 ("the 2003 Payment") and

(c) £2,594,028.69 on 4 April 2007 ("the 2007 Payment")

are payments of interest eligible for relief under s 353 ICTA.

(2) *The Settlement Agreement issue.* Whether there is a valid agreement between the parties which precludes HMRC from raising the discovery assessments and making the amendments under appeal, or any of them.

The Interest issue - summary

4. As regards the Interest issue, HMRC say that the Payments are not payments of interest eligible for relief because, firstly, properly understood the Payments are capital payments being either (a) payments in lieu of the interest which would otherwise have become payable under the relevant loan agreements, the effect of the present value discount applied to each purported interest payment being to capitalise the future income stream and extinguish the relevant lenders' rights to receive all future interest payments, or (b) repayments of loan principal.

5. HMRC also argue that, even if the Payments are found to be of interest, relief is denied either (a) in respect of interest paid at a rate in excess of a reasonable commercial rate, the argument here being that the relevant interest rate is to be determined by reference to the short period of the loans that had elapsed at the time of payment, and not by reference to the balance of the 30-year term of each loan, or alternatively that it should be calculated on the reduced value of the outstanding principal amount, or (b) by virtue of the anti-avoidance provisions of s 787 ICTA, on the basis that the sole or main benefit that might be expected to accrue to Mr Curran from the transaction under which the interest was paid was the obtaining of a reduction in tax liability by means of the s 353 relief.

6. Against this, Mr Curran's case is that the Payments were interest. The argument is that a lender and a borrower are free to agree that the consideration for a loan of money is to be paid in advance or in arrear and in a single amount or in several amounts at different intervals over time. It is the character of the payment and receipt as consideration or compensation for the use or deprivation of money over time that matters, not the timing or frequency of payment. Interest was initially agreed to be paid over the term of the loan, and it was later agreed that the interest would be paid in advance in a single sum. The parties re-calculated the amount of each of the Payments to reflect the time value of the use of the money obtained by the lender and foregone by Mr Curran, and made provision for an adjustment if the loans were repaid early. The Payments remained payment for the provision of loan finance and thus interest.

7. Mr Curran says that the interest paid was at a commercial rate, which is to be calculated by reference to the 30-year period of the loans and not the period of time that had elapsed when he made the Payments. In relation to s 787, Mr Curran argues that the transactions entered into by him were genuine, and involved real commercial risk and real commercial rewards, such that the sole or main benefit was not the obtaining of interest relief.

The Settlement Agreement issue – summary

8. The Settlement Agreement is an agreement that was entered into between Mr Curran and HMRC in settlement of Mr Curran's income tax position in respect of the tax years 2001/02 and 2002/03. It relates specifically to the tax treatment of the Payments made by Mr Curran in respect of the relevant loans made to him in 2002 and 2003. A number of disputes arise in this connection:

(1) HMRC say that the Settlement Agreement was concluded on 1 November 2007, the date on which HMRC formally accepted Mr Curran's letter of offer and accompanying side letter of 2 December 2005. Mr Curran argues that the Settlement Agreement was a binding contract by 2 December 2005.

(2) HMRC submit that the Settlement Agreement was voidable in respect of the 2002 and 2003 payments as a result of material non-disclosure by Mr Curran to HMRC. On the discovery of the material non-disclosure, it is said, HMRC avoided the Settlement Agreement by raising the discovery assessments and making the amendments. Mr Curran disputes that there was any non-disclosure, and says that even if there were such non-disclosure it would not have been reasonable for HMRC to have relied upon it.

(3) If the Settlement Agreement is not voidable, HMRC submit that its effect for the relevant tax years is constrained by reason of the following:

(a) Section 54 TMA cannot apply to the Settlement Agreement for the tax year 2002/03 because there was no open appeal (indeed the enquiry for that year had not even been closed). In relation to 2001/02, the terms of the Settlement Agreement are limited to the year under assessment (2001/02 only) because s 54 gives the agreement the like effect as a decision of the (then) General or Special Commissioners. Mr Curran argues that since he appealed HMRC's original decision to refuse interest relief, s 54 can cover the appeal in relation to 2001/02 and 2002/03, but that in any event HMRC had a general power to enter into the Settlement Agreement and are therefore bound by it.

(b) Clause 6 of the Settlement Agreement (which relates to tax years after those of each Payment) comprises a forward tax agreement in respect of which HMRC has no capacity to enter into. Mr Curran says that it is not an *ultra vires* forward tax agreement and it is binding for future years on HMRC.

(c) If HMRC is bound by clause 6 of the Settlement Agreement, they say that interest relief ceased to be available from the date (3 April 2006) on which Mr Curran disposed of the loan notes acquired with the 2002 and 2003 Loans ("the 2002 Notes" and "the 2003 Notes"). Mr Curran argues that clause 6 does not operate subject to any such condition, and that the relief provided by clause 6 continues to apply notwithstanding the disposal of the 2002 and 2003 Notes.

(4) HMRC submit that the Settlement Agreement does not on any view apply to the 2007 Payment. Mr Curran says that the 2007 Payment was materially identical to the 2002 and 2003 Payments, and when it was paid there had been

no material change in the law. Accordingly, argues Mr Curran, HMRC should be held to its position in the Settlement Agreement in determining the tax treatment of the 2007 Payment.

Our jurisdiction

9. Each of these issues falls to be determined by us. Although the Settlement Agreement issue might in certain respects fall away depending on how we decide the Interest issue, we shall, subject to what we say in the following paragraph, give our decision and our reasoning on all issues, in case this matter goes further and we are found to have gone wrong in any respect.

10. We should add that Mr Curran has also issued judicial review proceedings in respect of the closure notice and the discovery assessments seeking declaratory relief that HMRC's refusal to grant a deduction for interest relief for all the tax years in question was unlawful and seeking a quashing order in respect of the closure notice and the assessments. Each of the parties' counsel made reference in their skeleton arguments to the issue whether public law principles of legitimate expectation, unfairness and inconsistency are within this Tribunal's jurisdiction, but we heard no oral argument in these respects at the hearing. On the basis that the question of this Tribunal's jurisdiction to consider certain public law arguments is to come before the Upper Tribunal in other appeal proceedings, and that the judicial review proceedings in this case are stayed pending the determination of this appeal, we have not addressed the public law issues in this decision. We have confined ourselves to making what we hope are comprehensive material findings of fact for the assistance of the Upper Tribunal, to which jurisdiction in the judicial review proceedings has, we understand, been transferred by the Administrative Court.

Statement of Agreed Facts

11. We were provided with a helpful statement of agreed facts, which we reproduce here:

This Statement of Agreed Facts comprises two parts. Part A contains a statement of agreed facts relevant to the consolidated statutory appeals with case references TC/2010/02781 and TC/2010/02769 (the "Statutory Appeals"). Part B contains a summary chronology, based on the facts set out in Part A.

A. STATEMENT OF FACTS

1. THE APPELLANT

1.1 The Appellant is a Managing Director in the Investment Banking division of Credit Suisse Group. The Appellant was employed by Dresdner Kleinwort Wasserstein from 16 November 1998 to 31 August 2007.

2. COMPANIES OWNED BY MR BYRNE: 2002 AND 2003 TRANSACTIONS

2.1 Embryo Property Trading Limited ("Embryo") was incorporated in the UK on 13 February 2001. It was registered as a PLC in November 2001 and re-registered as a private limited company in February 2005. At all material times, Embryo was wholly owned by Mr Andy Byrne ("Mr Byrne") and a member of his close family, Mr Rory Byrne.

2.2 Embryo was formed with the object of carrying on business as a trader in property.

2.3 Stratford Opportunities PLC ("SOP") was incorporated in the UK on 22 January 2002. The authorised share capital of SOP at the date of adoption of its articles of association was £100,000,000 divided into 1,000,000,000 ordinary shares of 10p each, of which 1,001,000 were issued (with 99% of those issued shares owned by Mr Byrne).

2.4 SOP was formed with the objects (among others) of carrying on property development and a property investment business.

2.5 Tailored Loans Limited ("TLL") was incorporated in the UK on 14 February 2001. At all material times, TLL was wholly owned by Mr Byrne and Mr Rory Byrne.

2.6 TLL was formed with the object of carrying on business as a lender of money to individuals and companies.

2.7 Opes Finance Limited ("OFL") was incorporated in the UK on 4 February 2003. At all material times, OFL was wholly owned by Mr Byrne and Mr Rory Byrne.

2.8 OFL was formed with the object (among others) of carrying on a money lending business.

2.9 Embryo Investment Trust Limited was incorporated in the UK on 30 March 2000. Initially, it was owned 50:50 by Mr Byrne and Mr Anand Haridh and was formed with the object of carrying on business as an investment trust.

2.10 On 12 April 2001, Mr Haridh transferred his entire shareholding to Mr Rory Byrne.

2.11 On 30 January 2002, Embryo Investment Trust Limited changed its name to The Opes Group Limited ("Opes").

2.12 On 12 June 2002, the shareholders of Opes (at that time, Mr Byrne and Mr Rory Byrne) resolved to delete the company's memorandum and articles of association and replace them in their entirety. One of the changes was to change the company's object to (among others) carrying on *"a business of arranging transactions in investments for individuals, companies, partnerships, trusts and any other persons."*

2.13 On the same day, Mr Rory Byrne transferred his entire shareholding to Mr Byrne (resulting in Mr Byrne owning 100% of the issued share capital of Opes). Thereafter (save for a short period in 2004/05 when some of the issued share capital was held by Embryo), Opes was wholly owned by Mr Byrne.

5 2.14 On 7 January 2003, Opes received authorisation from the FSA to carry on the regulated activities of advising on investments, agreeing to carry on a regulated activity, arranging deals in investments, and making arrangements with a view to transactions in investments.

3. THE 2002 TRANSACTIONS

10 *Letter from Embryo*

3.1 By a letter dated 20 December 2001, Embryo offered the Appellant the opportunity to invest in a Jersey incorporated company (The Real Estate Holding Company Limited, referred to in the letter as "HoldCo"). The letter stated that *"We have incorporated [HoldCo] specifically to hold the Stratford*
15 *property portfolio. HoldCo is a Jersey incorporated company which is currently 100% owned by Embryo"* and anticipated that the properties in Stratford ("7 to 8 houses with a value of approximately £1,300,000") would be acquired by "mid February 2002".

3.2 The investments offered by Embryo in HoldCo were:

20 3.2.1 equity investments (by way of Class B ordinary shares); and

3.2.2 debt investments (by way of unsecured loan notes with a 30 year term, paying monthly interest at 8.50 per cent per annum).

3.3 By a letter dated 21 December 2001, TLL offered to lend the Appellant money to be used to fund any purchase by the Appellant of loan notes in *"a company*
25 *that will be incorporated by Embryo Property Trading PLC to invest in properties located in Stratford".* Any monies advanced by TLL were stated to be for 30 years (charging monthly interest at 8.00% per annum) and secured on the loan notes with an equivalent notional value as the loan advanced by TLL.

3.4 In the event, the Appellant did not make any investment in a company called
30 "The Real Estate Holding Company Limited".

3.5 On 6 February 2002, the Appellant lent £200,000 to Mr Byrne.

Letter from SOP

3.6 On 22 February 2002, SOP wrote to the Appellant stating that "later today we will be completing the acquisition of the first properties in the 'Stratford
35 Portfolio'… [consisting] of 5 freehold houses and 3 leasehold apartments

located in Stratford and its surrounding areas." The purchase price of the properties was stated to be "approximately £1,316,000."

3.7 By the same letter, the Appellant was invited to subscribe for 1,000,000 preference shares in SOP to be issued at par (0.10p). The letter stated that the offer to subscribe for preference shares was only available if the Appellant agreed to subscribe for a loan note in SOP with a minimum principal amount of £1,000,000. The authorised share capital of SOP did not include any preference shares at this date: the preference shares were created on 25 February 2002.

3.8 On 22 February 2002, TLL wrote to the Appellant stating that it was "pleased to formally confirm Tailored Loans' approval to support the financing of the [£1,000,000 Loan Note issued by SOP]".

3.9 On the same day, the Appellant borrowed £1,000,000 from TLL (the "2002 Loan") and subscribed for a £1,000,000 loan note in SOP (the "2002 Note") and charged the same as security for the 2002 Loan.

3.10 A resolution of a meeting of the directors of SOP held on 22 February 2002 records that the monies invested by the Appellant were to be used to pay part of the completion amounts relating to the acquisition of 5 freehold and 3 leasehold properties in Stratford and Shoreditch on and around 22 and 25 February 2002. The Respondent wishes to note that the extract does not contain a statement of (i) who was present at the meeting other than Mr Byrne; or (ii) the time at which the meeting took place on 22 February 2002. The Respondent also wishes to note that it has no evidence of whether the monies invested by the Appellant were in fact used to pay the various completion amounts (but see paragraph 0 below).

3.11 On 26 February 2002, the Appellant subscribed for 1,500,000 preference shares in SOP at par (10p per share). The Respondent wishes to note that it does not know when the offer to the Appellant was increased from 1,000,000 to 1,500,000 preference shares.

3.12 The Appellant subscribed for a further 350,000 preference shares in SOP at par on 23 September 2002.

Early payment

3.13 On 25 March 2002, TLL wrote to the Appellant offering him "the opportunity to pay the present value of some or all of [his] future interest obligations arising from [the 2002 Loan]" at a discount rate of 8.25 per cent per annum.

3.14 TLL's offer letter did not contain any statement as to the tax effects (for the Appellant) of the payment proposal. However, the Appellant and Mr Byrne met on 2 April 2002 to discuss the proposal. The Respondent wishes to note that there is no written record of what was discussed at that meeting and in particular whether, or the extent to which, the tax effects for the Appellant were so discussed.

3.15 On 5 April 2002, the Appellant entered into an agreement with TLL which stated that:

3.15.1 *"[the Appellant] may make a prepayment... of all interest payable for... the Interest Periods ending on 21st April 2002 and 21st February 2032... and each other Interest Period expiring between those periods"* (the "Relevant Interest periods") to TLL in the amount of £889,995.36 (which was described as *"representing the amount of interest payable by [the Appellant] for the Relevant Interest Periods discounted at a discount rate of 8.25%"*) provided that it was paid no later than 5 April 2002; and

3.15.2 the *"full amount"* of the 2002 Loan would remain payable unless the whole or any part of it was repaid before the contractual maturity date; and

3.15.3 if the whole or any part of the 2002 Loan were repaid before the contractual maturity date, a reduced amount would be payable in accordance with an algebraic formula set out in clause 4(b) of the agreement.

3.16 The Appellant paid the £899,995.36 to TLL on 5 April 2002. The Appellant contends that the payments were funded out of a deposit account which contained his bonus (of £674,851.08 which he had received from his then employer, Dresdner Kleinwort Benson, on 27 February 2002) and an overdraft from Barclays Bank. The Respondent requires the Appellant to prove this.

3.17 In his tax return for the year ended 5 April 2002, the Appellant claimed interest relief in respect of the £899,995.36 paid to TLL. This (together with, among other things, relief for investments in Venture Capital Trust shares and the Enterprise Investment Scheme) enabled the Appellant to seek to claim a tax repayment of £394,397.34 for that tax year.

3.18 The Respondent accepts that the relevant conditions (for statutory relief) in sections 360(1) and (2) of the Income and Corporation Taxes Act 1988 were satisfied at the date on which the early payment of interest was made (ie, 5 April 2002).

4. THE 2003 TRANSACTIONS

Opes' proposal

4.1 In or around February 2003, Opes offered the Appellant the opportunity to make a further debt investment in SOP by way of a subscription for further unsecured loan notes (with a term of 30 years and paying interest at 8.25 per cent per annum). The purpose of this further fundraising was stated to be to raise capital for the purchase of 8 apartments in the Q Building, Stratford for approximately £1.72m.

4.2 By a letter dated 6 February 2003, Opes stated that it had made arrangements with an associated company – OFL – for the Appellant to fund any debt investment he chose to make in SOP with monies borrowed from OFL.

Investment in SOP

5 4.3 On 10 February, the Appellant borrowed £850,000 from OFL (for a term of 30 years, paying interest at 7.75 per cent per annum, and to be secured by loan notes issued by SOP with an equivalent notional value) (the "2003 Loan").

4.4 On the same day, the Appellant used those monies to subscribe for a £850,000 unsecured loan note in SOP (the "2003 Note", with a 30 year term and paying
10 interest at 8.25 per cent per annum) and charged the same as security for the 2003 Loan.

Early payment

4.5 On 16 March 2003, Opes wrote to the Appellant offering to arrange for him *"to pay the present value of some or all of [his] future interest obligations arising*
15 *from [the 2003 Loan]"* at a discount rate of 8.00 per cent per annum.

4.6 The Appellant accepted Opes's offer and, on 26 March 2003, entered into an agreement with OFL which was materially identical to that described in paragraph 0 above (save that the relevant periods were those from 9 April 2003 to 9 February 2033, and the sum to be paid by the Appellant was £755,788).

20 4.7 The Appellant paid the £755,788 to OFL on 28 March 2003. Similarly to the payment made to TLL in April 2002, the Appellant contends that the payment was part funded by monies received as a bonus from his then employer, Dresdner Kleinwort Wasserstein. The Respondent requires the Appellant to prove this.

25 4.8 In his tax return for the year ended 5 April 2003, the Appellant claimed interest relief in respect of £755,788 paid to OFL.

4.9 The Respondent accepts that the relevant conditions (for statutory relief) in sections 360(1) and (2) of the Income and Corporation Taxes Act 1988 were satisfied at the date on which the early payment of interest was made (ie, 28
30 March 2003).

5. THE 2005 TRANSACTION

5.1 During the period 24 May 2002 to 4 April 2005, the Appellant borrowed further monies from TLL (totalling £756,000) as follows:

5.1.1 24 May 2002: £200,000 (7.75 per cent per annum; repayable on
35 demand);

5.1.2 30 September 2002: £200,000 (7.75 per cent per annum; repayable on demand);

5.1.3 13 January 2003: £150,000 (7.75 per cent per annum; repayable on demand);

5.1.4 12 August 2003: £83,500 (7.75 per cent per annum; repayable on demand);

5.1.5 4 September 2003: £100,000 (7.75 per cent per annum; repayable on demand); and

5.1.6 15 January 2004: £22,500 (7.75 per cent per annum; repayable on demand).

5.2 In addition, the Appellant borrowed a further £100,000 (7.75 per cent per annum; repayable on demand) from OFL on 4 April 2005. (This loan and the loans described at paragraph 5.1 are hereafter referred to as the "Interim Loans".) During this period, the Appellant invested in Swiss and Portuguese properties.

5.3 On 18 June 2005, Opes wrote to the Appellant outlining a potential restructuring of the Interim Loans. Paragraph 5 of that letter stated that the restructuring would not involve the repayment of the 2002 and 2003 Loans.

5.4 On 7 August 2005, Opes wrote to the Appellant confirming the restructuring proposal in respect of the Interim Loans:

5.4.1 TLL would make a new loan facility available in the amount of £1,179,566.87 (hereafter, the "2005 Loan");

5.4.2 £1,014,630.82 of the 2005 Loan was to be drawn down and used to repay the Interim Loans (including accrued interest thereon);

5.4.3 interest would be payable at 7.60 per cent per annum on the 2005 Loan (0.15 per cent per annum less that in respect of the Interim Loans); and

5.4.4 the Appellant would be offered the opportunity to invest the balance of the 2005 Loan in another venture – the Gable House Investment (though this would be by way of a payment made to the Appellant in lieu of drawdown).

5.5 On 16 August 2005, the Appellant accepted Opes' proposal and entered into the 2005 Loan.

5.6 On the same day:

5.6.1 the Interim Loans were discharged;

5.6.2 the charges over the 2002 and 2003 Notes were released;

5.6.3 new charges were put in place over the 2002 and 2003 Notes, securing the 2002 and 2005 Loans (leaving the 2003 Loan unsecured); and

5 5.6.4 the balance of the 2005 Loan was left undrawn (in exchange for an investment position in the Gable House Investment).

6. DISPUTE IN RELATION TO THE 2002 AND 2003 TRANSACTIONS

Investigations

6.1 The Respondent disputed the claims for relief described at paragraphs 3.17 and 10 4.8 above and opened enquiries (pursuant to section 9A of the Taxes Management Act 1970 ("TMA")) into the Appellant's tax returns for the years ended 5 April 2002 and 5 April 2003 under Code of Practice 8 (the "Investigations").

6.2 In relation to the 2001/02 Investigation, the Respondent issued a closure notice 15 on 3 December 2004 pursuant to section 28A TMA denying the interest relief claimed by the Appellant. No closure notice was issued in relation to the 2002/03 Investigation.

6.3 On 15 December 2004, the Appellant appealed pursuant to section 31 TMA against the amendment to his 2001/02 tax return.

20 6.4 The Appellant became a client of Herbert Smith LLP ("Herbert Smith") on 30 September 2005, appointing Herbert Smith to represent him in relation to the Investigations.

The Settlement Meeting

6.5 On 17 October 2005, Herbert Smith wrote to the Respondent, setting out the 25 basis on which the Appellant claimed relief for interest in the 2001/02 and 2002/03 tax years and inviting the Respondent to meet with them and the Appellant to discuss the possibility of a negotiated settlement in relation to (i) the Appellant's appeal against the amendment to his 2001/02 tax return; and (ii) the 2002/03 Investigation.

30 6.6 A settlement meeting was held on 3 November 2005 (the "Settlement Meeting") at the Respondent's offices in Euston Tower, London NW1 3TY.

6.7 The Settlement Meeting was attended by:

6.7.1 the Appellant;

6.7.2 the Appellant's accountant (David Ritzema of the Briars Group);

6.7.3 Heather Gething and Mark Feldman of Herbert Smith; and

6.7.4 Patricia Feighan (a Grade 7 Officer of the Respondent) and Andrew Hewitt (an Officer of the Respondent).

6.8 At the Settlement Meeting, Ms Feighan (among other things) proposed that relief for the payment of interest in respect of the 2002 and 2003 Loans be given (i) as to 50% in the tax year in which the payment was actually made; and (ii) as to 50% over the remaining life of the 2002 and 2003 Loans.

6.9 Ms Feighan had discussed this proposal prior to the Settlement Meeting with (i) a technical specialist – Mr Richard Rogers, a Grade 6 Officer of the Respondent; and (ii) the Group Leader for Special Civil Investigations Manchester – Mrs Catherine Gregory, a substantive Band B2 Officer of the Respondent (promoted to Band B1). Further, Ms Feighan telephoned Mrs Gregory on two occasions during the course of the Settlement Meeting to check that she was content with the settlement proposals made by Ms Feighan during the Settlement Meeting (and Mrs Gregory agreed the basis of the settlement).

6.10 Manuscript notes of the Settlement Meeting were taken by Ms Gething, Mr Feldman, Ms Feighan and Mr Hewitt. None of those notes record any discussions:

6.10.1 as to whether the Appellant should be required to retain the 2002 and 2003 Notes (in order to obtain relief for interest paid early in respect of the 2002 and 2003 Loans); or

6.10.2 regarding the charges in place over the 2002 and 2003 Notes (securing the 2002 and 2003 Loans).

The Settlement Agreement

6.11 On 14 November 2005 (following the Settlement Meeting), Mr Ritzema sent a letter to Ms Feighan setting out an initial calculation of the tax relief due in accordance with what he described in that letter as *"the basis agreed"*. That letter also recorded what Mr Ritzema described as *"the remaining part of the settlement agreement"*.

6.12 Ms Ellams, an officer of the Respondent, responded on behalf of Ms Feighan (by email to Herbert Smith) on 23 November 2005 with a draft settlement agreement (the "Settlement Agreement"), in the form of a letter from the Appellant to the Respondent, recording the settlement terms.

6.13 On 29 November 2005, Mr Feldman sent a mark up of the Settlement Agreement (by email) to Ms Feighan. Ms Feighan responded with a further mark up of the Settlement Agreement (by email) on 2 December 2005.

6.14 Further amendments to the draft Settlement Agreement were agreed (by telephone) between Ms Feighan and Mr Feldman on 2 December 2005.

6.15 The Appellant signed a final version of the Settlement Agreement on 2 December 2005 and sent a copy to the Respondent on the same day (by fax and by courier).

6.16 On 22 December 2005, the Respondent acknowledged receipt of the signed version of the Settlement Agreement and stated that a *"letter of acceptance [would] be issued early in [2006]"*.

Subsequent events

6.17 On 8 December 2005, the Respondent paid £404,258.34 into the Appellant's bank account (number 70441066).

6.18 On 12 April 2006, the Respondent paid a further £30,664.42 to the Appellant's bank account (number 70441066).

6.19 A further £14,825.68 was met by an overpayment on account which had been paid into the Appellant's bank account (number 70441066) by the Respondent on 11 July 2006.

6.20 The Respondent issued a coding notice for the tax year 2005/06 on 8 December 2005. The Respondent issued further coding notices for the tax years 2006/07 and 2007/08 on 15 January 2006 and 3 July 2007 respectively.

6.21 On 2 October 2007, the Respondent wrote to the Appellant stating "*It has come to [the Respondent's] attention that the Letter of Offer signed by you on 2nd December 2005 was never formally accepted... In order however that a formal response may now be issued to the offer letter could you please confirm in writing that you wish the offer, un-amended in any respect, to go forward for consideration.*"

6.22 On 22 October 2007, the Appellant wrote to the Respondent stating "*I confirm that I would like the offer of 2nd December 2005 signed by me (and unamended since that date in any respect) to go forward for consideration as agreed at the time.*"

6.23 On 1 November 2007, the Respondent wrote to the Appellant stating that it "*hereby accept[s] the offer made in your letter dated 2 December 2005... whereby you offer to pay the sum of £313,156.40. I can confirm that you have already paid £313,156.40.*"

7. THE 2006 AND 2007 LOAN TRANSACTIONS

Sale of equity investments in SOP

7.1 On 22 February 2006, Opes wrote to the Appellant with an offer to purchase his entire shareholding in SOP (which had been purchased for £185,000 – see paragraphs 3.11 and 3.12 above) for £259,000.

7.2 The Appellant accepted Opes' offer on the same day, receiving payment on 24 March 2006.

Sale of the 2002 and 2003 Notes

7.3 On 2 April 2006, Opes wrote to the Appellant with the following proposal:

5 7.3.1 TLL would purchase the 2002 and 2003 Notes for £1,999,780.48 (being the face value of those securities plus accrued interest in respect thereof);

7.3.2 the Appellant would use £1,063,221.91 of the proceeds to repay the 2005 Loan (plus accrued interest); and

10 7.3.3 the Appellant would use the remaining sale proceeds (£936,558.57) to make an unsecured loan to Mr Andy Byrne in his personal capacity (at 11.89 per cent per annum; repayable on 1 month's notice).

7.4 The Appellant accepted Opes' proposal and the following took place on 3 April 2006:

15 7.4.1 TLL released the charges over the 2002 and 2003 Notes;

7.4.2 the Appellant sold the 2002 and 2003 Notes to TLL for £1,999,780.48;

7.4.3 the Appellant repaid the 2005 Loan (plus accrued interest);

7.4.4 the Appellant advanced an unsecured loan to Mr Byrne in the sum of
20 £936,558.57 (the "First Personal Loan"); and

7.4.5 the 2002 and 2003 Loans became unsecured.

Further investments

[The Respondent does not agree the following paragraphs 7.5 to 7.8 inclusive. In particular and for the avoidance of doubt, the Respondent notes that it is in no position
25 to agree to whether this is an exhaustive list of the personal loans made by the Appellant to Mr Byrne. However, the Appellant wishes them to be included and is content to be put to proof on their content.]

7.5 In October 2006, the Appellant advanced a further loan of £2,000,000 to Mr Byrne (at 15 per cent per annum) (the "Second Personal Loan").

30 7.6 The Second Personal Loan was drawn down in three tranches:

7.6.1 £1,000,000 on 11 October 2006;

7.6.2 £500,000 on 30 October 2006; and

7.6.3 £500,000 on 10 November 2006.

7.7 The principal on the Second Personal Loan was repaid in full by Mr Byrne on 28 March 2007.

7.8 On the same day, Mr Byrne repaid £400,000 of the principal on the First Personal Loan. The remaining principal on the First Personal Loan was repaid in instalments in May, July and October 2007.

7.9 On 7 October 2007, the Appellant agreed to lend £2,000,000 to "Courtyard Property Group Limited" (which company was previously known as Opes Group Holdings Limited (see paragraph 8.4 below). On 17 October 2007 this was replaced with a formal agreement between the Appellant and "The Courtyard Property Group Limited" for £2,000,000 (the "OGH Loan"). The term of the OGH Loan was 180 days and interest was due at 30 per cent per annum for the first three months and 25 per cent per annum thereafter.

8. COMPANIES OWNED BY MR BYRNE: 2007 TRANSACTION

8.1 Opes Group Holdings Limited ("OGH") was incorporated in the UK on 21 March 2003. At all material times, OGH was wholly owned by Mr Byrne

8.2 OGH was formed with the object of carrying on business as a general commercial company.

8.3 During 2007 (and at all material times after), OGH was the sole shareholder of a number of property development/investment companies, including EC Development Fund Ltd, EC Sandringham Ltd, Weybridge Property Ltd, EC Woking Ltd, and – as described in more detail below – English Courtyard Developments Ltd.

8.4 On 19 June 2007, OGH changed its name to the "Courtyard Property Group Limited".

8.5 Wimbledon Property Ventures ("WPV") was incorporated in the UK as a private limited company on 20 September 2006. On incorporation, WPV was wholly owned by Mr Byrne.

8.6 WPV was formed with the object (among others) of carrying on property development and investments activities.

8.7 Wimbledon Property Investments Limited ("WPI") was incorporated in the UK as a private limited company on 6 January 2006. On incorporation, WPI was wholly owned by Mr Byrne. On 13 March 2007, Mr Byrne transferred his shareholding to WPV.

8.8 WPI was formed with the object (among others) of carrying on property development and investments activities.

9. THE 2007 TRANSACTIONS

9.1 On 24 August 2006, OGH acquired English Courtyard Developments Limited – a company carrying on a business of property development and sales. (In a letter to the Appellant dated 10 March 2007 (see 9.3 below), Opes records the purchase price for English Courtyard Developments as having been £11,000,000 (with £4,750,000 of the purchase price left outstanding, accruing interest at 18 per cent per annum).)

9.2 On 7 March 2007, Opes approached the Appellant with the opportunity to make an equity investment of £3,700,000 in English Courtyard Developments Limited. Opes offered to fully fund the investment with a loan of £3,700,000 (charging interest at 7 per cent per annum) from English Courtyard Developments Limited. The offer was subsequently withdrawn shortly after – possibly on the same day.

9.3 On 10 March 2007, Opes approached the Appellant with another investment proposal. That proposal comprised two limbs:

9.3.1 First, the Appellant was offered the opportunity to make an equity investment in WPV.

9.3.2 Second, the Appellant was offered the opportunity to make a debt investment in OGH.

Investment in WPV

9.4 WPV and its subsidiary – WPI – owned two out of three sites required to assemble a redevelopment site in Wimbledon. The middle site was owned by the YMCA. It was intended that Mr Byrne's companies would acquire the third site and then develop a mixed-used scheme across the three sites.

9.5 The terms of Opes' investment offer in relation to WPV was as follows:

9.5.1 Opes offered the Appellant the opportunity to purchase a 46.2 per cent equity stake in WPV at a cost of £2,500,000 (the "WPV Shares").

9.5.2 The Appellant would have the right to sell the WPV shares to Mr Byrne in five years for £6,200,800 (generating a return of 20 per cent per annum over 5 years).

9.5.3 Further, Mr Byrne would have the right to purchase that equity stake from the Appellant in three years for £4,882,812.50 (generating a return of 25 per cent per annum over 3 years).

Investment in OGH

9.6 At the time of Opes' offer, OGH still owed the vendor of the English Courtyard group £4,100,000 of the purchase price (accruing at 18 per cent per annum).

9.7 In order to assist OGH in making payment to the vendor, Opes offered the Appellant the opportunity to make a debt investment in OGH by way on an unsecured loan note with a 30 year terms, paying interest at (i) 22 per cent per annum for ten years; and (ii) 2 per cent per annum for the following twenty years (the "OGH Note").

Funding from TLL

9.8 On 11 March 2007, following a meeting and subsequent discussions between the Appellant and Mr Byrne, TLL wrote to the Appellant confirming that it would be willing to advance a loan of £3,500,000 to the Appellant in order to finance the purchase of the WPV Shares and the OGH Note.

9.9 The terms offered by TLL were 30 year funding (at 8.00 per cent per annum) secured by the WPV Shares and OGH Note.

Acceptance of Opes' proposal

9.10 The Appellant agreed TLL's terms and entered into a loan agreement (reflecting the terms set out at paragraphs 9.8 and 9.9 above) on 13 March 2007 (the "2007 Loan").

9.11 The Appellant used the proceeds of the 2007 Loan to purchase the WPV Shares on 13 March 2007 and to purchase the OGH Note on 16 March 2007 (both of which investments were charged on the same day as security for the 2007 Loan).

Early payment

9.12 On Wednesday 28 March 2007, Mr Byrne transferred £2,400,000 to the Appellant's account with Barclays Bank. In this regard, the Appellant refers to paragraphs 7.7 and 7.8 above.

9.13 On Thursday 29 March 2007, TLL wrote to the Appellant offering him "*the opportunity to reduce your interest bill [on the 2007Loan] significantly by paying a portion of this interest in advance". The letter went on to state that "[i]n principle, [TLL] are prepared to offer you the opportunity to reduce the cost of your interest payments by a discount of 8.25% (compounded) for each year in the future that the interest payment is due"*.

9.14 On Monday 2 April 2007, Mr Byrne discussed the offer with the Appellant and (on behalf of TLL) wrote to him, confirming the offer of 29 March 2007 (allowing the Appellant to pay £2,594,028.69 being an amount equal to the present value of his future interest obligations arising from the 2007 Loan in the interest periods from 12 March 2010 to 12 March 2037).

9.15 The Appellant accepted TLL's offer and, on 4 April 2007, entered into an agreement with TLL which stated that:

9.15.1 *"[the Appellant] may make a prepayment... of all interest payable for... the Interest Periods endings on 12th March 2010... and 12th March 2037... and each other Interest Period expiring between those dates, together the 'Relevant Interest Periods'"* to TLL in the amount of £2,594,028.69 (which was described as *"representing the amount of interest payable by [the Appellant] for the Relevant Interest Periods discounted at a discount rate of approximately 8.25%"*) provided that it was paid no later than 4 April 2007; and

9.15.2 the *"full amount"* of the 2007 Loan would remain payable unless the whole or any part of it was repaid before the contractual maturity date.

9.16 The Appellant paid £2,594,028.69 to TLL on 4 April 2007. The Appellant contends that he funded the payment out of a deposit account into which his then employer (Dresdner Kleinwort Benson) had paid his bonus (of £1,004,994.71) on 29 March 2007, and into which Mr Byrne had made the repayment described at paragraph 9.12 above.

9.17 In his tax return for the year ended 5 April 2007, the Appellant claimed interest relief in respect of the payment which, according to the Appellant, resulted in a repayment of tax of £1,028,602.76 for the year 2006/07.

9.18 The Respondent accepts that the relevant conditions (for statutory relief) in sections 360(1) and (2) of the Income and Corporation Taxes Act 1988 were satisfied at the date on which the early payment of interest was made (ie, 4 April 2007).

10. DISPUTE IN RELATION TO THE 2007 TRANSACTION AND DECISION TO RESILE FROM SETTLEMENT AGREEMENT

10.1 The Respondent disputed the claims for relief described at paragraph 9.17 above and opened an enquiry (pursuant to section 9A TMA) into the Appellant's tax return for the year ended 5 April 2007 under Code of Practice 8 (the "2007 Investigation").

10.2 In relation to the 2007 Investigation, the Respondent issued a closure notice on 31 October 2008 pursuant to section 28A TMA denying the interest relief claimed by the Appellant (the "Closure Notice").

10.3 On 10 November 2008, the Appellant appealed against the Closure Notice pursuant to section 31 TMA.

10.4 On 16 January 2009, the Respondent issued five discovery assessments for the 2001/02, 2002/03, 2003/04, 2004/05 and 2005/06 tax years, the effect of which was for the Respondent to resile from the Settlement Agreement (denying the Appellant interest relief in respect of the interest treated as having been paid in respect of the 2002 and 2003 Loans in those year by the Settlement Agreement) (the "Discovery Assessments").

10.5 On 27 January 2009, the Appellant:

10.5.1 made protective appeals against the Discovery Assessments pursuant to section 31 TMA; and

5 10.5.2 issued judicial review proceedings in respect of the Respondent's decision to resile from the Settlement Agreement.

B. Summary chronology

The following summary chronology is based on the facts set out in Section A above.

Date	**Event**
February 2002	• Appellant borrowed £1,000,000 from TLL (ie, the 2002 Loan) • Appellant purchased 2002 Note from SOP and charged the same as security for the 2002 Loan • Appellant subscribed for 1,500,000 preference shares in SOP
April 2002	Appellant paid £899,995.36 to TLL in respect of the 2002 Loan
September 2002	Appellant subscribed for 350,000 preference shares in SOP
February 2003	• Appellant borrowed £850,000 from OFL (ie, the 2003 Loan) • Appellant purchased 2003 Note from SOP and charged the same as security for the 2003 Loan
April 2003	Appellant paid £755,788 to OFL in respect of the 2003 Loan
August 2005	• Appellant consolidated the Interim Loans into the 2005 Loan • TLL and OFL released the charges over the 2002 and 2003 Notes

	(which had secured the 2002 and 2003 Loans) • Appellant charged the 2002 and 2003 Notes as security for the 2002 and 2005 Loans
November 2005	Settlement Meeting between the Appellant and the Respondent took place
December 2005	• Appellant sent signed record of the settlement reached at the Settlement Meeting to the Respondent • Respondent made repayment of tax to Appellant
January 2006	Respondent issued coding notice in relation to the 2005/06 tax year and also issued a coding notice in relation to the 2006/07 tax year
April 2006	Appellant sold 2002 and 2003 Notes to TLL
August 2006	OGH acquired the English Courtyard property group
March 2007	• Appellant borrowed £3,500,000 from TLL (ie, the 2007 Loan) • Appellant purchased the WPV Shares and the OGH Note and charges the same as security for the 2007 Loan
April 2007	Appellant paid £2,594,028.69 to TLL in respect of the 2007 Loan
October 2007	Appellant lent £2,000,000 to OGH (ie, the OGH Loan)

Table of abbreviations

12. The statement of agreed facts contains a number of matters to which, for convenience, abbreviations or defined terms have been assigned. It may be helpful to
5 the reader therefore to have those summarised in tabular form. For the avoidance of

doubt, nothing in this table should be regarded as itself constituting any finding of fact by the Tribunal.

Term or Abbreviation	Definition
Amendment	Closure notice and amendment to the Appellant's 2007 Tax Return (dated 31 October 2008)
Assessments	Assessments raised by HMRC on the Appellant for the 5 years to 5 April 2006
Mr Byrne	Mr Andy Byrne, the owner and controller of companies concerned in the relevant transactions
Byrne group	The group of companies owned and controlled by Mr Byrne, including: - Embryo - OFL - OGH - SOP - TLL - WPI - WOV
COP 8	Code of Practice 8: HMRC's Code of Practice pursuant to which the Special Compliance Office (now Specialist Investigations) carried out investigations into serious losses of tax, not concerning fraud
2002 Deed of Charge	Deed of Charge of 22 February 2002 pursuant to which the Appellant charged to TLL the 2002 Note as a continuing security for the payment and discharge of the 2002 Loan
2003 Deed of Charge	Deed of Charge of 10 February 2003 pursuant to which the Appellant charged to OFL the 2003 Note as a continuing

	security for the payment and discharge of the 2003 Loan
2007 Deeds of Charge	Deeds of Charge of 13 March 2007 pursuant to which the Appellant charged to OFL the 2007 Shares and the 2007 Note as a continuing security for the payment and discharge of the 2007 Loan
Embryo	Embryo Property Trading plc (a company owned and controlled by Mr Byrne)
Ms Feighan	Ms Patricia Ann Feighan, an HMRC Investigator currently working in the Manchester Fraud and Avoidance Team which is part of the Specialist Investigations directorate of HMRC. In 2003, that team worked under the title of the Special Compliance Office, Manchester
Herbert Smith	The firm Herbert Smith LLP which was engaged by the Appellant in September 2005
Interest relief	Relief from income tax pursuant to s.353 of the Income and Corporation Taxes Act 1988
Letter of Offer	Letter of offer from the Appellant to HMRC of 2 December 2005
2002 Loan	£1,000,000 lent by TLL to the Appellant under the 2002 Loan Agreement on 22 February 2002
2003 Loan	£850,000 lent by OFL to the Appellant under the 2003 Loan Agreement on 10 February 2003
2007 Loan	£3,500,000 lent by TLL to the Appellant under the 2007 Loan Agreement on 13 March 2007
2002 Loan Agreement	Term Loan Facility Agreement between TLL and the Appellant

	dated 22 February 2002
2003 Loan Agreement	Term Loan Facility Agreement between OFL and the Appellant dated 10 February 2003
2007 Loan Agreement	Term Loan Facility Agreement between TLL and the Appellant dated 13 March 2007
2002 Note	£1,000,000 loan note issued by SOP to the Appellant on 22 February 2002 with a 30-year term and 8.50% interest rate (interest to accrue daily and be payable on the 21st day of each month)
2003 Note	£850,000 loan note issued by SOP to the Appellant on 10 February 2003 with a 30-year term and 8.25% interest rate (interest to accrue daily and be payable on the 9th day of each month)
2007 Note	£1,000,000 loan note issued by OGH to the Appellant on 16 March 2007 with a 30-year term and 22.0% interest rate until 15 March 2017, 2.0% interest rate thereafter (interest to accrue daily; the date on which interest was to be payable in each month was left blank)
OFL	Opes Finance Limited (a company owned and controlled by Mr Byrne)
OGH	Opes Group Holdings Limited (a company owned and controlled by Mr Byrne); renamed the Courtyard Property Group in June 2007
2002 Payment	The payment of £889,995 by the Appellant to TLL on 5 April 2002 pursuant to the 2002 Payment Agreement

2003 Payment	The payment of £755,788 by the Appellant to OFL on 5 April 2002 pursuant to the 2003 Payment Agreement
2007 Payment	The payment of £2,594,028.69 by the Appellant to TLL on 4 April 2007 pursuant to the 2007 Payment Agreement
2002 Payment Agreement	Agreement under which the Appellant made a payment of £889,995.36, purportedly of interest in respect of the 2002 Loan, to TLL [The nature of this payment is in dispute.]
2003 Payment Agreement	Agreement under which the Appellant made a payment of £755,788, purportedly of interest in respect of the 2003 Loan, to OFL [The nature of this payment is in dispute.]
2007 Payment Agreement	Agreement under which the Appellant made a payment of £2,594,028.69, purportedly of interest in respect of the 2007 Loan, to TLL [The nature of this payment is in dispute.]
Mr Ronan Curran	The Appellant's brother
SCO	The Special Compliance Office of HMRC
SCO Manual	The version of the SCO Manual understood to have been circulated internally in draft form to SCO investigators and relied on by them during the periods under review.
Settlement Agreement	The agreement between the Appellant and HMRC in purported settlement of the Appellant's income tax position in respect of 2001/02 and 2002/03. [The circumstances of this agreement are subject to dispute

	between the parties.]
Settlement Meeting	Meeting on 3 November 2005 attended by the Appellant, Ms Heather Gething and Mr. Mark Feldman of Herbert Smith, Mr. David Ritzema of Briars Consulting, and Ms. Patricia Feighan and Mr. Andrew Hewitt of HMRC.
2007 Shares	Six ordinary £1 shares in WPV issued to the Appellant on 13 March 2007 for £2.5m
Side Letter	Letter from the Appellant to HMRC accompanying the Appellant's Letter of Offer of 2 December 2005
SOP	Stratford Opportunities plc (a company owned and controlled by Mr Byrne)
TLL	Tailored Loans Limited (a company owned and controlled by Mr Byrne)
WPI	Wimbledon Property Investments Limited (a company owned and controlled by Mr Byrne)
WPV	Wimbledon Property Ventures Limited (a company owned and controlled by Mr Byrne)

The law

13. To be eligible for income tax relief, interest paid by an individual must satisfy certain conditions. For the periods under appeal, the relevant law was contained in ss 353 to 379 ICTA. In broad terms, relief from income tax is granted under s 353 for interest payments made in certain circumstances. Relief is given against income for the tax year in which an individual pays interest. The relief consist of a deduction or set-off of the amount of the interest from the individual's income in that year (s 353(1B)). But relief will not be given for any interest in excess of a commercial rate (s 353(3)).

14. Eligibility for relief depends on the use to which the monies borrowed are put. Where the loan is used to acquire ordinary share capital of a company, or in lending

money to a company (in each case the company must be a close company), both the company and the individual must meet certain conditions at the time each payment of interest is made, if those payments are to qualify for relief. One such condition is that the individual must not have recovered any amount of capital from the company without using that recovered capital in repayment of the loan, and an individual is treated as having recovered an amount of capital if he receives (or in a non-arm's length transaction, is deemed to have received) consideration for assigning any debt due to him from the company (ss 360 and 363).

15. So far as material, we set out below the relevant parts of this legislation. The provisions were materially the same for periods 2001/02 and 2002/03, and 2006/07 respectively, save only for an amendment made to s 353(1) by the Income Tax (Trading and Other Income) Act 2005 for tax year 2005/06 onwards which we have included in square brackets (and which is not material to these appeals):

> **353 General provision**
>
> (1) Where a person pays interest in any year of assessment, that person, if he makes a claim to the relief, shall for that year of assessment be entitled (subject to sections 359 to 368 [of this Act and section 52 of ITTOIA 2005]) to relief in accordance with this section in respect of so much (if any) of the amount of that interest as is eligible for relief under this section by virtue of sections 359 to 365.
>
> ...
>
> (1B) Where a person is entitled for any year of assessment to relief under this section in respect of any amount of interest which—
>
> … is eligible for that relief otherwise than by virtue of section 365,
>
> that relief shall consist (subject to section 237(5)(b)) in a deduction or set-off of that amount from or against that person's income for that year.
>
> …
>
> (3) Relief under this section shall not be given in respect of—
>
> …
>
> (b) where interest is paid at a rate in excess of a reasonable commercial rate, so much of the interest as represents the excess.

16. Interest is defined by s 832(1) ICTA as meaning "both annual or yearly interest and interest other than annual or yearly interest".

17. Section 360 set out a number of conditions which must be satisfied in respect of loans used to acquire an interest in a close company:

> **360 Loan to buy interest in close company**
>
> (1) Subject to the following provisions of this section and sections 361 to 364, interest is eligible for relief under section 353 if it is interest on a loan to an individual to defray money applied—

(a) in acquiring any part of the ordinary share capital of a close company complying with section 13A(2); or

(b) in lending money to such a close company which is used wholly and exclusively for the purposes of the business of the company or of any associated company of it which is a close company satisfying any of those conditions; or

…

and either the conditions stated in subsection (2) below or those stated in subsection (3) below are satisfied.

(2) The conditions first referred to in subsection (1) above are—

(a) that, when the interest is paid, the company continues to comply with section 13A(2) and the individual has a material interest in the company; and

(b) that he shows that in the period from the application of the proceeds of the loan to the payment of the interest he has not recovered any capital from the company, apart from any amount taken into account under section 363(1); and

(c) that, if the company exists wholly or mainly for the purpose of holding investments or other property, no property held by the company is used as a residence by the individual;

but the condition in paragraph (c) above shall not apply in a case where the individual has worked for the greater part of his time in the actual management or conduct of the business of the company, or of an associated company of the company.

…

18. Section 363 set out supplementary provisions restricting interest relief in certain circumstances. So far as material it provided as follows:

363 Provisions supplementary to sections 360 to 362

(1) If at any time after the application of the proceeds of the loan the individual has recovered any amount of capital from the close company, co-operative, employee-controlled company or partnership without using that amount in repayment of the loan, he shall be treated for the purposes of sections 353, 360, 361 and 362 as if he had at that time repaid that amount out of the loan, so that out of the interest otherwise eligible for relief (or, where section 367(4) applies, out of the proportion so eligible) and payable for any period after that time there shall be deducted an amount equal to interest on the amount of capital so recovered.

(2) The individual shall be treated as having recovered an amount of capital from the close company, co-operative, employee-controlled company or partnership if—

…

(c) he receives consideration of that amount or value for assigning any debt due to him from the close company, co-operative, employee-controlled company or partnership;

and where a sale or assignment is not a bargain made at arm's length, the sale or assignment shall be deemed to be for a consideration of an amount equal to the market value of what is disposed of.

19. Even if the various statutory conditions for relief are satisfied, relief will not be given if the provisions of s 787 ICTA apply. Section 787 relevantly provided as follows:

787 Restriction of relief for payments of interest

(1) Relief shall not be given to any person under any provision of the Tax Acts in respect of any payment of interest if a scheme has been effected or arrangements have been made (whether before or after the time when the payment is made) such that the sole or main benefit that might be expected to accrue to that person from the transaction under which the interest is paid was the obtaining of a reduction in tax liability by means of any such relief.

…

(2) In this section "relief" means relief by way of deduction in computing profits or gains or deduction or set off against income or total profits.

The evidence

20. We had witness statements for Mr Curran from Mr Curran himself, David Ritzema, tax director of the Briars Group Limited, and Heather Gething, a Solicitor Advocate and Head of Tax Planning and Tax Disputes at Herbert Smith LLP, and for HMRC from Patricia Feighan, an investigator currently working in the Manchester Fraud and Avoidance team which is part of the Specialist Investigations directorate of HMRC. All gave oral evidence subject to cross-examination.

21. In addition we had experts' reports from experts appointed by each of the parties. Mr Curran's expert was Professor Jeremy Dent, professor in accounting at the London Business School, and HMRC's expert was Marcus Stanton, a banking consultant and non-executive director of a number of quoted companies. As well as their individual reports, the experts produced a joint report and each gave oral evidence subject to cross-examination.

22. It is convenient at this stage to set out the experts' joint report as it forms part of the agreed factual matrix, and it also serves to highlight certain areas where the experts disagreed and in respect of which we will be required to make a determination.

1. Introduction

1.1. This is a Joint Expert Report in connection with [these appeals].

1.2. The issue in dispute between Mr Curran and HMRC is Mr Curran's claim for tax relief on three payments made on 4 April 2002, 28 March 2003 and 4 April 2007.

1.3. *Transaction Background*

1.4. On 22 February 2002, 19 February 2003 and 13 March 2007, Mr Curran borrowed sums from finance companies in Mr Byrne's control on 30 year terms. These sums he invested in property development companies, also in Mr Byrne's control, which we understand to be close companies. Shortly after borrowing each sum, Mr Curran made payments to Mr Byrne's finance companies equivalent to the present value of the future interest obligations arising on each loan to its maturity date, and claimed tax relief on these payments. Consistent with our earlier reports, we refer to these payments as "Early Interest Payments" and/or "Prepayments".

1.5. The finance companies from which Mr Curran borrowed were Tailored Loans Limited ("TLL") and Opes Finance Limited ("OFL"). The property development companies in which Mr Curran invested were Stratford Opportunities Plc ("SOP"), Wimbledon Property Ventures Limited ("WPV") and Opes Group Holdings Limited ("OGH"), later renamed Courtyard Property Group Limited ("CPG").

1.6. *Expert Reports*

1.7. We each prepared Amended Expert Reports on the above transactions, both dated 14th February 2011. The purpose of this Joint Report is to identify points of agreement, points of disagreement and, where possible, reasons for any disagreement.

1.8. As instructed by the Tribunal we met on 6 April 2011, at the offices of Herbert Smith, solicitors for Mr Curran. The agenda for the meeting was arranged beforehand through a telephone conversation and a series of emails/draft agendas exchanged between us. The format of this joint report tracks the items listed in the agenda, which is attached as Appendix 1 [*not reproduced*].

2. The Nature of the Arrangements

2.1. *The Nature of the Equity Investments*

2.2. We agree that Mr Curran's investments in Mr Byrne's property development companies comprised equity subscriptions (in SOP and WPV) and investments in unsecured loan notes (in SOP and OGH).

2.3. We also agree that against a backcloth of a rising property market, the potential upside return on Mr Curran's equity investments in SOP and WPV was high and that his investments were at risk in the event of a falling property market.

2.4. *The Effect of the Reduced Principal Payment Amount Formula*

2.5. The three Loan Amendment Agreements, which each provided for Mr Curran to make a defined Early Interest Prepayment, also included a Reduced Principal Payment Amount ("RPPA") formula. We agree that the formula determined the amount payable by Mr Curran to the lenders (TLL and OFL) in the event of the loans being repaid before their maturity dates. We also agree that its effect was to reduce the amount otherwise payable by a sum

equivalent to the present value of the interest relating to the period after the early redemption date.

2.6. *The Commonality of the Early Interest Payments*

2.7. The distinctive characteristic of the Prepayments was that the interest on the loans was paid to maturity but the loan principal remained outstanding. Professor Dent has not had experience of such transactions before, at least in relation to personal and/or corporate transactions. Mr Stanton has not had any significant working experience of this either, although he has seen interest prepayments in certain film financing arrangements.

2.8. *The Zero Coupon Cash Flows*

2.9. We agree that the economic profile of Mr Curran's loans, taken together with the Early Interest Payments, was similar to those of a zero coupon bond. We also agree that Mr Curran did not, in fact, issue zero coupon bonds.

3. **The Sequential or Combined Nature of the Arrangements**

3.1. The common pattern in Mr Curran's investment transactions with Mr Byrne's companies was as follows:

a) Mr Curran borrowed from Mr Byrne's finance companies,

b) Mr Curran invested in Mr Byrne's property development companies, and

c) Mr Curran made Early Interest Payments on the sums borrowed.

3.2. We disagree as to whether each set of the above transactions can be seen as a series of sequential and separate transactions, or as a combined transaction to be considered as a whole. In Professor Dent's view, the Early Interest Payments were separate and sequential to the borrowing and investment. In Mr Stanton's view the arrangements can be viewed as a combined transaction.

In forming our views we have taken the following factors into account.

3.3. *Long Term Funding to Mr Curran and TLL*

3.4. We were both surprised by the 30 year term of the loans made by Mr Byrne's finance companies to Mr Curran. Further, it seems clear to both of us that this was not matched by 30 year funding obtained by Mr Byrne's finance companies (TLL and OFL).

3.5. In Professor Dent's view the lack of long term funding to Mr Byrne's finance companies was unremarkable, for borrowing short and lending long was a feature of corporate finance at that time. In Mr Stanton's view it is difficult to see the 30 year term loans made to Mr Curran as other than a prelude to making the Prepayments.

3.6. *Risk Transfer*

3.7. We agree that an effect of Mr Curran borrowing from Mr Byrne's finance companies and investing the proceeds into Mr Byrne's property development companies was to transfer to Mr Curran the risk of those property development companies failing, at least to the extent of his investments in them. We also agree that the interest rates receivable on Mr Curran's loan

note investments in Mr Byrne's property development companies were (for the most part) higher than those payable on his loans from Mr Byrne's finance companies.

3.8. In Professor Dent's view the interest rate differential (or spread) was rational compensation to Mr Curran for assuming that risk. In Mr Stanton's view, although there was 5 a transfer of risk, these funding arrangements were predicated on 30 year unsecured terms, which in his experience is unusual and, as stated above, are difficult to envisage other than as a prelude to making the interest prepayments.

3.9. *Were the Early Interest Payments Inevitable?*

3.10. We disagree on whether the Prepayments were inevitable. Professor Dent's view is that 10 they were not, in that (i) it was not a condition precedent of making the loans that the interest would be prepaid and (ii) Mr Byrne's property ventures seem to have been financed independently of the Early Interest Prepayments.

3.11. Mr Stanton's view is that whilst it was not a formal condition precedent to make the Prepayments, it seems likely that they would always follow on from the loans. In his view the 15 absence of documentation does not preclude an understanding to this effect and instances of Mr Curran and Mr Byrne conducting business on an undocumented basis are cited in his report. Further, given the many intercompany transactions between Mr Byrne's companies, and his personal loans, it is difficult to discern how Mr Byrne's property ventures were financed.

20 4. **The Economics of the Arrangements**

4.1. *The Rationality of the Investments in SOP, WPV and OGH*

4.2. We agree that the effect of Mr Curran's investments in SOP, WPV and OGH was to give him exposure to profits and losses on Mr Byrne's property development ventures.

4.3. *The Rationality of the Early Interest Payments*

25 4.4. We disagree as to the extent of the economic rationality of the Early Interest Payments. In Professor Dent's view the payments were rational in that they produced pre tax gains to Mr Curran. In Mr Stanton's view, and on the assumption that the Prepayments could be viewed as a separate leg of the arrangements, then once liquidity costs are taken into account these gains would be reduced, possibly into a loss.

30 5. **The Economic Benefits of the Transactions to Mr Curran**

5.1. We agree that Mr Curran made a profit on his equity investment in SOP when it was sold in March 2006 and that his loan notes in that company were redeemed at par (or nominal value) with interest paid in full. We also agree that Mr Curran seems to have incurred substantial losses on his investments in WPV and OGH.

35 5.2. Focusing more specifically on the tax benefits flowing from the early payment of interest, Professor Dent's view is that these are largely to do with timing and naturally reverse through time. That is to say, any relief Mr Curran is successful in claiming for the early payments of interest will be compensated by lower claims for relief in the future. Mr Stanton's view is that a reversal, over the following 30 years, is based upon a number of assumptions. By way of

example, these include Mr Curran remaining liable to UK tax (for instance by not leaving the UK).

6. The Sale of the SOP Loan Notes in 2006

6.1. We agree that in April 2006, when Mr Curran sold his loan notes in SOP, the loans advanced to him by TLL and OFL ceased to finance an interest in a close company. The sale proceeds plus accumulated interest were approximately £2m.

6.2. We also agree that in October 2007 Mr Curran made a loan of £2m to CPG, a company managed and controlled by Mr Byrne.

6.3. In Professor Dent's view it would be reasonable for Mr Curran to argue that the sale proceeds of the SOP loan notes were later reinvested in CPG. In Mr Stanton's view money is a fungible commodity, and it is not possible to track individual amounts once they are mixed up in a bank account. Accordingly, it would be very unlikely that one particular inflow of funds could be paired up with another particular outflow, some 18 months later.

7. The Disposal of the Appellant's Loans from TLL and OFL

7.1. In July 2008 Mr Byrne sold the loans that his companies had earlier advanced to Mr Curran in 2002, 2003 and 2007. The acquirer was Mr Ronan Curran, Mr Curran's brother. The consideration was £15,000.

7.2. At the time of writing our Amended Expert Reports, we both understood that one remaining interest payment on the 2007 loan was due in March 2009 in the sum of £280,000. Professor Dent has since been advised by Herbert Smith that this payment was made in advance, at a discount of £40,000, shortly before the loans were sold to Mr Ronan Curran.

7.3. On the assumption that all interest on the loans was prepaid and in the absence of events of default (see below), we agree that Mr Ronan Curran was buying claims to the repayment of the principal loan amounts at maturity (due in 2032, 2033 and 2037). At a price of £15,000, this would imply a 25% discount rate. We also agree that putting a value on these claims is difficult. In Professor Dent's view a 25% discount rate would not be unreasonable. In Mr Stanton's view, given the duration to maturity, it is difficult to know what level of discount would be appropriate.

7.4. We agree that if any loan was in default, the lender could call for repayment in line with the RPPA formula. We also agree that as of July 2008 the amounts payable under the RPPA formula were approximately £141,000 in respect of the 2002 loan, £111,000 in respect of the 2003 loan and £354,000 in respect of the 2007 loan.

7.5. We agree that the 2007 Loan was in default at the date of its sale, by virtue of Mr Curran putting CPG into receivership, at least to the extent that that loan was secured over the OGH Note. In Mr Stanton's opinion, it is also possible that the 2002 and 2003 Loans were in default, by virtue of the disposal of the security of the SOP Loan Notes.

7.6. We disagree as to the practical effect of default on the value of the loans. In Mr Stanton's view, default has a material bearing on the valuation of the loans and the value of the loan portfolio was substantially in excess of the £15,000 paid by Mr Ronan Curran (see Appendix 2). In Professor Dent's view, given the economic circumstances of the time, the practical effect of default on the value of the loans is questionable.

8. **Capital Market Transactions**

8.1. We agree that the discounting techniques applied in the early interest payment calculations and in the RPPA formulae are straightforward and would be well understood in banking and financial circles.

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Appendix 1 [*not reproduced*]

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Appendix 2

Revisions to Loan Valuations in Mr Stanton's Amended Expert Report

10 1. At the time of writing our Amended Expert Reports, we both understood that one remaining interest payment on the 2007 loan was due in March 2009 in the sum of £280,000. Professor Dent has since been advised by Herbert Smith that this payment was made in advance, at a discount of £40,000, shortly before the loans were sold to Mr Ronan Curran.

2. Mr Stanton wishes to inform the Tribunal that had he been aware of this, the combined 15 valuation of the three loans transferred to Mr Ronan Curran, as summarised at paragraph 127 of Mr Stanton's earlier report, would have been as follows:

a) £376,000 if the liquidation of SOP could not be anticipated as at July 2008[1], and

b) £606,000 if the liquidation of SOP could be anticipated as at July 2008[2].

3. Mr Stanton's conclusion, that the value of the loan portfolio was substantially in excess of 20 £15,000 paid by Mr Curran, remains the same.

………………………

Additional findings of fact

23. As well as the witness evidence and the experts' reports, we also had a number of bundles of documentation. From all this evidence we find the following additional 25 facts.

24. Mr Curran is an investment banker working in financial services. He has since 1994 worked in financial services in a variety of roles including financial product structuring, debt capital markets origination and debt principal finance. He told us,

[1] Being £13,000 for the 2002 TLL Loan (not in default), £9,000 for the 2003 OFL Loan (not in default) and £354,000 for the 2007 TLL Loan (in default)

[2] Being £141,000 for the 2002 TLL Loan (in default), £111,000 for the 2003 OFL Loan (in default) and £354,000 for the 2007 TLL Loan (in default)

and we accept, that he is a sophisticated investor, with a high appetite for risk. He has invested in a number of venture capital projects involving private companies.

25. Mr Curran first came into contact with Mr Byrne when Mr Byrne was working as an analyst for Merrill Lynch. Mr Curran's brother was also an analyst there and he and a Mr Gerza, whom Mr Curran had recruited to work for him at Dresdner Kleinwort Benson, had spoken highly of Mr Byrne as an original thinker and highly-motivated entrepreneur.

26. In or around 2001 Mr Byrne sought Mr Curran's advice (as a senior and more experienced individual with a history of investing in entrepreneurial activities) in relation to starting his own business. Mr Byrne wanted to (and in fact did) leave employment with Merrill Lynch in order to develop a property-led investment group. Mr Byrne wanted to bring to private individuals the techniques and service standards that large investment banks provide to their corporate and institutional clients.

27. In addition to seeking out Mr Curran's advice, Mr Byrne wanted to secure him as a client for his property investment business. Mr Curran's evidence, which we accept, was that he was the perfect client for Mr Byrne: financially sophisticated, with significant financial resources and an appetite for high risk-adjusted returns, but with very little time to consider the making and management of investments in the property market by himself. We accept also that having Mr Curran as a client would add weight to Mr Byrne's business proposal and help him to attract other sophisticated investors.

28. At the time of its letter to Mr Curran of 20 December 2001 offering Mr Curran the opportunity to invest in the Jersey HoldCo, Embryo was looking to gain exposure to the property market in Stratford. Even at a time long before any talk about London hosting the 2012 Olympics or Stratford becoming the location for the Olympic village, Embryo had identified Stratford as an area in transition. It was becoming one of the UK's major transportation hubs, and was seeing a marked increase in residential interest. Embryo's strategy was to purchase a portfolio of freehold residential property in central Stratford which had the potential for Embryo to add value (that is to say, Embryo was not interested in purchasing recently built or recently refurbished properties unless there was a compelling reason to do so). The properties would be indirectly purchased by Embryo through HoldCo.

29. In relation to the proposed investment in HoldCo, TLL offered financing to Mr Curran in order that he could purchase loan notes in the investing vehicle. That financing was offered by way of a 30-year term loan charging monthly interest at an annual rate of 8%, with the loan being secured on the loan notes. In the event, Mr Curran did not make an investment in HoldCo.

The February 2002 transaction

30. By the letter from SOP dated 22 February 2002, Mr Curran was invited to subscribe for 1,000,000 preference shares of 10p each in SOP. (The total number subscribed was 1,850,000 shares.) This offer to subscribe was conditional on Mr

Curran agreeing to subscribe in addition for a loan note in SOP with a minimum principal amount of £1,000,000. To finance his investment in the loan notes, Mr Curran borrowed £1,000,000 from TLL for a term of 30 years with interest at 8% per annum payable monthly on the last day of each calendar month.

31. The facility agreement for the 2002 Loan was dated 22 February 2002. The purpose of the loan was expressed to be the application by or on behalf of Mr Curran in financing the subscription for the loan note in SOP. Material features of this 2002 Loan Agreement are:

(1) The 2002 Loan was secured by means of a charge over the 2002 Note. The Deed of Charge was entered into on 22 February 2002.

(2) Mr Curran had no right voluntarily to prepay the 2002 Loan without the consent of TLL prior to 22 February 2004. From that date Mr Curran could prepay all (but not part of) the 2002 Loan, subject to payment of a prepayment fee of "up to" 2% on the principal amount prepaid.

(3) In certain circumstances Mr Curran was obliged to prepay the 2002 Loan, subject to the same prepayment fee. These were:

(a) If he became entitled to receive redemption proceeds in respect of all or any part of the 2002 Note, a prepayment was required of the amount of the redemption proceeds;

(b) If he sold or otherwise disposed of all or any part of the 2002 Note provided that the 2002 Note was subject to the Deed of Charge at the relevant time.

32. Asked by Mr Gammie what he understood by this requirement that the 2002 Note be subject to the Deed of Charge, Mr Curran said, and we agree, that if the Loan Notes were not charged at the relevant time, there would be no obligation to prepay the 2002 Loan.

33. TLL itself financed the 2002 Loan to Mr Curran by borrowing, directly and indirectly, from third party banks. The accounts of SOP for its first accounting period from incorporation on 22 January 2002 to 28 February 2003 show that SOP had guaranteed and secured by way of charge over its freehold properties and other assets a loan from Bristol & West plc to Tailored Loans BW Limited of £788,200 and a loan from Allied Irish Bank of £271,088 to TLL. TLL's accounts to the end of February 2002 show as creditors Tailored Loans BW Limited (£921,200) and bank loans payable after 5 years of £463,260. The notes to those accounts show that the loan of £921,200 from Bristol & West to Tailored Loans BW Limited was on-lent to TLL "for the purpose of funding" the 2002 Loan.

34. The 2002 Note was likewise issued on 22 February 2002 for a term of 30 years in the principal sum of £1,000,000 at an interest rate of 8.5%, payable on the 21st day of each month. Provision was made for early redemption in the case of certain defaults and on a winding-up of SOP other than a members' voluntary winding-up. In addition, Mr Curran had the right, following the second anniversary of the issue of the

2002 Note, to redeem the whole of the 2002 Note early at par on giving not less than 60 days' notice.

35. Professor Dent and Mr Stanton agree that this funding was not long-term funding matching the 30-year term of the 2002 Loan. Mr Stanton's view is that this demonstrates that the 2002 Loan was merely a prelude to the 2002 Payment, a subject we shall return to later. Professor Dent, on the other hand, regards this financing structure as unremarkable for the time in question; his evidence is that borrowing short and lending long was standard practice at the relevant time, and that it would have been expected that TLL would have been able to roll its own borrowings over into new borrowings at the terms expired. We prefer Professor Dent's evidence in this regard. We do not consider that, in the context of the market at the material time, the practice of borrowing short and lending long would have been considered as extraordinary.

The commercial rationale for the February 2002 transaction

36. Mr Curran was offered the opportunity to invest in the equity of a property investment business to be established by SOP. As a condition of that investment, Mr Curran would be required to provide debt funding for a 30-year term. Mr Curran did not regard this as an onerous requirement, as TLL at the same time offered equivalent 30-year loan finance.

37. Mr Curran's evidence, which we accept, was that he was attracted by the February 2002 investment proposal. As an investor with an appetite for risk, he was attracted to the rewards that could arise from an equity investment in real estate. He was himself a busy man, and Mr Byrne was offering to do all the work in researching properties, conducting due diligence, negotiating, managing the investments, finding tenants, collecting rent and dealing with all the problems associated with the renting of houses and apartments. Mr Curran would thus be given the opportunity to "piggy-back" on the efforts of Mr Byrne and, without paying any management fee, would gain upside exposure to property investments in Stratford.

38. Mr Curran told us that Mr Byrne is a man of great energy, and some eccentricity, with an insatiable appetite for investment. He carried out a great deal of work on the Stratford property investments, including "pounding the pavements" in order to spot investment opportunities.

39. Mr Curran was cross-examined on the level of due diligence that he had undertaken in relation to the SOP investment. We were shown a copy of a presentation prepared in February 2001 by an unrelated company called Chelsfield plc examining proposals for development of the Stratford Rail Lands from Chelsfield and its development partner, Stanhope. Although this was not original research, we accept that this was relevant information as to the attractiveness of the Stratford area as a development opportunity. The accessing of this material, and its analysis, which took place at a meeting between Mr Curran and Mr Byrne at Mr Byrne's Fleet Street offices, is of itself in the nature of due diligence. As Mr Curran put it: there was no need for either Mr Curran or Mr Byrne to have attempted to replicate such research,

and as effectively a one-man band it would not have been possible for Mr Byrne to have done so.

40. We accept that the level of due diligence required in the case of an investment in real property at the time in question would have been less extensive that that in relation to, for example, a technology company. The UK was at the beginning of a major real estate bubble. The proposed investment was in existing residential property, and not in property development. We find that the due diligence undertaken cannot be described as inadequate in its context.

41. We accept in this respect the view expressed by Professor Dent that Mr Curran undertook the sort of due diligence that Professor Dent would have expected him to have undertaken in relation to the February 2002 transaction, and Professor's Dent's opinion that it was reasonable for Mr Curran to have left Mr Byrne to pull together the due diligence and do all necessary research.

42. Mr Curran accepted that the tax consequences of making an investment were something that had to be taken into account. At the Settlement Meeting Mr Curran had sought to explain that the transactions, ignoring the 0.5% interest rate differential, were tax neutral. The evidence from Professor Dent confirmed what we would in any event regard as self-evident, particularly for an investor of the sophistication of Mr Curran, namely that the tax implications of any financial scheme have to be taken into account in assessing it.

43. Nonetheless, we also accept Mr Curran's evidence that the obtaining of tax relief was not Mr Curran's main reason for making the investments, in respect of both shares and the 2002 Notes, into SOP. First and foremost he was looking to the economic risk; secondarily he had regard to tax, the after-tax returns or the after-tax risk-adjusted returns. We do not accept that the motivation for the 2002 Loan was tax considerations, or, as it was put to Mr Curran in cross-examination, "tax-driven". In particular, we consider that Mr Curran's decision not to repay the 2002 and 2003 Loans, although based in large part on a desire on his part, in terms of economic value, not to forfeit tax relief due to him under the Settlement Agreement, is not in any way indicative of tax being the reason, or the principal reason, for Mr Curran having entered into the February 2002 transactions.

The economics of the February 2002 transaction

44. There were two elements to the investment by Mr Curran in SOP. The first was the equity investment. But that was conditional on Mr Curran agreeing to provide debt finance to SOP in the form of the 2002 Notes, funded by the 2002 Loan.

45. Mr Curran's evidence was that the funding structure of SOP, under which 70% to 85% of the purchase price of the Stratford properties would be funded by debt, had the effect of leveraging the equity investment. For equity investors other than Mr Curran, this leverage would operate at the level of SOP itself. Any increase in value overall (after taking account of financing costs) would provide an enhanced rate of return on the equity after repaying the debt; correspondingly, any losses would give

rise to an increased risk of loss of the equity. For Mr Curran, the position was effectively the same, as confirmed by Professor Dent's evidence. Mr Curran did not finance the 2002 Note from his own resources, but by means of a loan from TLL. His investment was therefore leveraged, albeit outside SOP, in the same way as if he had invested only in equity. Mr Curran's own potential return was furthermore enhanced by the differential interest rate (of 0.5%) which he was to receive on the 2002 Notes compared with the rate on the 2002 Loan.

46. The 2002 Loan not only provided leverage for Mr Curran's own equity investment in SOP. It also had the effect of shifting risk from Mr Byrne's companies to Mr Curran. According to Mr Curran, and we accept this, he was being paid the interest differential to credit enhance the effective financing of SOP by TLL. This credit enhancement was supported by the security package around the 2002 Loan, namely the charge over the 2002 Note. As Mr Curran described it, and again we accept, this level of fee for credit enhancement was not untypical of such credit wrap arrangements in the market up to 2006 that could be made with monoline insurers.

47. Because SOP's properties were charged to secure the loan by Bristol & West to Tailored Loans (BW) Limited and the loan by Allied Irish Bank to TLL, and Mr Curran's investment in the 2002 notes was unsecured, Mr Curran was not only accepting risk of default by SOP, but also risk of default by those other companies in the Byrne group. Although this was not a risk specifically referred to by Mr Curran in his evidence, we can infer, and we so find, that it was a risk that, with his knowledge of financial structures, Mr Curran would have taken into account.

48. At the material time, the risk of loss in an investment of the nature of SOP would have been perceived to be low. As Professor Dent described the position, there had at the material times been rampant price inflation in the property market. Mr Curran was a sophisticated investor who understood the cash flows and the risks and returns.

The 2002 Payment

49. The timing of the offer by TLL to Mr Curran of the opportunity to pay the present value of some or all of the future interest arising on the 2002 Loan, discounted at a rate of 8.25% to reflect early payment, coincided with Mr Curran having received or being about to receive a substantial bonus from his employer. Mr Curran's understanding of the proposal was that it would provide not only an opportunity for value to be created for him, but that from Mr Byrne's perspective it would also enable him to raise money for the expansion of his property investment group. This understanding was confirmed by the evidence of Professor Dent whose view, based on an analysis of TLL's audited accounts, was that TLL did not use the funds raised through the 2002 Payment either to repay the Bristol & West loan or to finance the purchase by SOP of the properties purchased in February 2002.

50. At a meeting on 2 April 2002 Mr Curran met Mr Byrne to discuss the pre-payment proposal in more detail. Mr Curran decided to accept TLL's offer and Mr Byrne wrote to Mr Curran on 3 April 2002 attaching a spreadsheet calculating the

present value of the interest payments at 4 Aril 2002 at a discount rate of 8.25%. This gave a total prepayment amount of £889,794.97.

51. Later the same day, Mr Byrne again wrote to Mr Curran regarding a loan facility that Mr Curran was looking to obtain from Barclays Bank (with whom Mr Curran had an established relationship). The concern was over what Mr Byrne regarded as a penal charge for the facility of £5,000. Mr Byrne proposed that he should effectively bear this cost. Alternatively, it was suggested that Mr Curran could use his own resources as to £400,000, and pay the balance of approximately £490,000 with the help of funding by Mr Byrne, by means of his repaying a loan of £200,000 plus interest and arranging a loan of £290,000. In this email Mr Byrne comments: "This would look quite circular but it can be done."

52. In the same email, commenting on the Barclays proposal, Mr Byrne makes the point that there could be other opportunities to use the Barclays loan if it was sensibly priced. He suggests a loan by Mr Curran to Mr Byrne for a year or more at an interest rate of 10% - 12% to be used to purchase further property. He discusses the possible interest spread, referring to a pre-tax spread of £30,000, and suggests also – without going into any detail - that it might be possible for the interest to be received by Mr Curran free from UK tax.

53. The 2002 Payment Agreement was entered into on 5 April 2002. Its terms were as described in the statement of agreed facts. As regards the reduced amount (the Reduced Principal Payment Amount or RPPA) payable if the whole or part of the 2002 Loan were to be repaid before the expiry of its 30-year term, the provisions of clause 4(b) were as follows:

> "If the whole or any part of the Loan (a "Principal Payment Amount") is repaid before the Repayment Date pursuant to Clause 14 (Events of Default) or Clause 5 (prepayment and Cancellation), the Reduced Principal Payment Amount shall be payable instead of the Principal Payment amount which would otherwise be required to be repaid. The Reduced principal repayment amount in relation to a Principal Payment Amount shall be equal to:
>
> A + B[c][3] x D, where,
>
> A = the amount of the Loan as at the date of [the 2002 Payment Agreement];
>
> B = 1 + (W ÷ 12) where W is the interest rate payable on the Loan as set out in the Specific Terms divided by 100 (for example where the interest rate payable on the Loan is 8%, W will be 0.08);
>
> C = (Y ÷ 365) x 12 where Y is the number of days between the Reference Date (excluding the Repayment Date but including the Reference Date;

[3] The formula is expressed as B to the power of C

D = the Principal Payment Amount (before any reduction pursuant to this paragraph 4(b)) divided by the amount of the Loan as at the date of [the 2002 Payment Agreement]; and

The relevant Reference Date is:

5 (i) in the case of a repayment of the whole or part of the Loan pursuant to a demand under Clause 14 (Events of Default) of the General Terms, the date of such demand;

(ii) in the case of a prepayment pursuant to a request delivered pursuant to Clause 5.1 (Prepayment and cancellation) of the General 10 Terms, the date of such request

(iii) in the case of a prepayment becoming due pursuant to Clause 5.2 or Clause 5.3 (Prepayment and cancellation) of the General terms, the date on which such prepayment becomes due."

54. Clause 5 of the 2002 Payment Agreement provides that there is no release from 15 any obligation to make a prepayment or repayment of the Loan under the 2002 Loan agreement, and that the 2002 Payment Agreement did not constitute an amendment or variation of any term of that agreement "save as specifically provided for in this letter".

55. There is a difference of view between the experts as to the economic effect of 20 the RPPA formula. Professor Dent's view is that the RPPA formula does not reduce the principal to be repaid. Instead it provides for a rebate to compensate for the early payment of interest to the maturity date of the loan. The principal is a fixed amount. The rebate depends on the redemption date. In his report, Mr Stanton appears to endorse this view. He says there that the RPPA formula provides something of a 25 financial short cut, in that in the event of an early repayment only one payment needs to be made, by the borrower to the lender. This he contrasts with the making of two payments, the first being the whole repayment of principal by borrower to lender, and in the opposite direction an amount in repayment of part of the earlier prepayment. But Mr Stanton in his evidence to us objected to the characterisation of the formula as 30 providing for a rebate of interest. He did so because his analysis is that the 2002 Payment cannot at the outset be characterised at all either as wholly interest or as wholly capital; it is an amalgam of the two and the precise composition of the payment cannot be ascertained until the interest accrues or there is a prepayment of principal.

35 56. It is evident that the resolution of this dispute between the experts will not determine the issue we have to decide, namely the nature of the 2002 Payment. Rather it is that determination which, at least in legal terms, will help to resolve the question whether the reduction by the RPPA formula in what would otherwise be payable on redemption of the 2002 Loan should properly be described as a rebate of 40 interest or as something else.

57. The experts also differed on whether or not it was inevitable that, having entered into the February 2002 transactions, and having borrowed on the terms of the 2002 Loan, Mr Curran would be offered the opportunity to make the 2002 Payment. Mr Stanton takes the view that it was always intended that the 2002 Loan would be

amended, and that Mr Curran would pay in advance the present value of some or all of his interest obligations due to arise from the 2002 Loan. His analysis is that what Mr Curran was being offered was a combined transaction, being the combination of (i) borrowing £1,000,000 from TLL, (ii) subscribing £1,000,000 for the 2002 Note, and (iii) prepaying approximately £900,000 to TLL.

58. On that basis, Mr Stanton's view is that the choice offered to Mr Curran was not independent and sequential, in economic terms. In terms of the Byrne group obtaining new funding, Mr Stanton does not regard this as having come into effect until the 2002 Payment was made.

59. In support of his analysis, Mr Stanton makes the point that, in his view, it would have been highly challenging for a start-up financial company, such as TLL, to raise 30-year funding. He rightly says, by reference to the relevant accounts of the Byrne group, that TLL did not have any such funding. He concludes on this basis that it was the 2002 Payment that provided the funding for TLL. He then goes on to present a hypothetical summary of how the transaction could be analysed. Its starting point is that TLL would lend £1,000,000 to Mr Curran, who would lend to SOP which would, in one way or another, through an intercompany account process, lend £1,000,000 to TLL. At this point, Mr Stanton, concludes, no net new funds would have been raised by the Byrne group. His analysis then continues to include the 2002 Payment. He says that, shortly afterwards, Mr Curran would agree to pay £900,000 to TLL. As a result £900,000 of new funds would flow from Mr Curran to TLL, which TLL would use to repay £900,000 of the intercompany loan from SOP, which would then, at that stage, be new funds for SOP, available for use in its property business.

60. We find this analysis of no assistance. It is a hypothetical construct which bears no relationship to the facts. It is clear that TLL did not raise 30-year funding; it had no need to do so. It did have funding, as we have described, both directly and indirectly, from third party lending institutions. That much is clear from the accounts of both TLL and SOP. We have, in this connection, accepted Professor Stanton's evidence that these funding arrangements were unremarkable. It is also clear from those accounts that the 2002 Note subscribed by Mr Curran did provide funding for the purchase of the Stratford properties, and that there was no £1,000,000 loan from SOP to TLL through any intercompany account.

61. Mr Stanton goes on to make the point that, looking at the transaction as a whole, if it had not been intended at the outset that Mr Curran would make the 2002 Payment, then TLL would be lending £1,000,000 to Mr Curran at 8% and Mr Curran would be lending £1,000,000 to SOP at 8.5%. He says that this would have resulted in a 0.5% external payment by the Byrne group, which could very simply have been avoided by TLL lending directly to SOP. He goes on then to say that at this point, given that there is no new funding into the Byrne group, he cannot see an economic reason for doing this. Whilst Mr Stanton acknowledges that there was a risk transfer to Mr Curran from TLL, he says that at that point none of the funds would have been invested in property.

62. This analysis is again of no value in these proceedings. It is a fact that the funds generated from Mr Curran's subscription for the 2002 Note were invested in acquiring the Stratford properties. Nor do we accept that there was no economic reason for the 2002 Loan; there was an economic reason both as regards the Byrne group, which shifted risk and obtained credit enhancement, and for Mr Curran who obtained a 0.5% interest differential for accepting that risk, and was thereby enabled to obtain a leveraged equity investment in a real estate venture. It is not any part of HMRC's case that any of the transactions in question did not take place or are otherwise to be disregarded as a sham. The tax position must be determined on the basis of what happened, and not on the basis of an economic recharacterisation of events.

63. Apart from one reference, in a note of a meeting on 26 February 2004 between Ms Feighan and a colleague, Mr Preshaw, and Mr Curran and his advisers, including Mr Ritzema, there is nothing in the agreements or in the other documentation we have seen that lends support to a conclusion that the 2002 Loan and the 2002 Payment were anything other than separate transactions. At that meeting Mr Curran confirmed that he had discussed the rolling up of interest with Mr Byrne around Christmas 2001, but it had not been included in the original deal. We do not consider that these discussions show that the 2002 Payment was part of the same transaction as the 2002 Loan. We find that they were separate.

Investment rationale of the 2002 Payment

64. For the Byrne group, there was a commercial cash flow benefit in obtaining further funds by means of the receipt of the 2002 Payment.

65. As Mr Curran described it, the opportunity to prepay the interest on the 2002 Loan by means of the 2002 Payment was itself a compelling investment opportunity for him. It was put to him in cross-examination by Mr Fisher that this amounted to a recognition on the part of Mr Curran that the real investment in the Byrne group was the early payment of interest. Mr Curran explained that he was here referring to the compelling nature of the pre-payment opportunity, but he was not singling that out; there were, as he put it, many compelling investment opportunities that Mr Curran entered into with the Byrne group. We accept Mr Curran's evidence on this point. It is clear to us that his reference to the pre-payment proposal being a compelling investment opportunity does not carry with it any acknowledgement or indeed implication that the 2002 Payment was the real investment in the Byrne group. For the reasons we have explained, we do not accept that, viewed objectively, this was the case.

66. There were a number of benefits to Mr Curran in pre-paying the interest. First, a higher discount rate was applied in calculating the amount of the 2002 Payment than the interest rate on the 2002 Loan. This had the effect in present value terms of enabling Mr Curran to eliminate a liability to make future interest payments with a net present value of around £911,000 (discounting at the actual interest rate of 8%) in return for a payment of about £890,000. We accept the evidence of Professor Dent in this respect that Mr Curran's wealth can be regarded as at the date of payment as having increased by £21,000 as a consequence. This is a benefit that can be

calculated in net present value terms, even though it would in fact be realised in money terms over the period of the 2002 Loan.

67. Secondly, from the perspective of Mr Curran, whose analysis was essentially confirmed by Professor Dent, the pre-payment of interest on the 2002 Loan amounted to a risk-free investment. The analysis is that the elimination of a liability is equivalent to the acquisition of an asset. An actual asset would have an element of risk attached to it, which would impact on the return an investor would expect on that asset. But where a liability is eliminated there is no actual asset, and accordingly no risk. The comparison can therefore only be with a risk-free asset, and an appropriate proxy for such an asset is UK government bonds. Mr Curran's evidence was that the appropriate benchmark rate for government bonds at the relevant time was between 4% and 5%, and Professor Dent used a rate of 5%. On this basis, Professor Dent calculated the value of the benefit to Mr Curran of making the 2002 Payment at £350,000.

68. The experts differed on the impact of the loss of liquidity inherent in Mr Curran making the 2002 Payment, when compared with the proxy of UK government bonds. Whilst accepting that Mr Curran would show a net present value gain by making the 2002 Payment, Mr Stanton focuses on the fact that by doing so Mr Curran would have been tying up what would otherwise be available cash for a period of 30 years. He calculates the liquidity cost of this by reference to the cost of borrowing replacement funds. His analysis, based on an assumed borrowing cost of 20% per annum on a 30-year loan, is that the annual cost to Mr Curran of borrowing £890,000 on those terms would have been £176,000, which, says Mr Stanton, would more than have eliminated the benefit of savings Mr Curran would have achieved by making the 2002 Payment (annual interest saved of £80,000). In Mr Stanton's view, therefore, the appropriate discount rate on an investment basis would not be 5%, but 20%.

69. Professor Dent disagreed with Mr Stanton's approach. His first point was that it would not be a correct approach to deal with a liquidity issue of this nature by altering the discount rate. The question was whether Mr Curran had the cash to make the 2002 Payment, or whether he could borrow at reasonable rates. Secondly, Professor Dent considers it wrong to use a 30-year unsecured loan as the comparison. The correct comparison, in Professor Dent's view, was with the actual unsecured financing, over say a five-year term, Mr Curran could have obtained at the relevant time, which, according to the evidence, was between 4% and 6%. In his view, the comparison with a 30-year term loan at an assumed rate of 20% was hypothetical, and not the correct approach to an issue of liquidity.

70. Professor Dent's view is that the economics of the 2002 Payment, and its investment return, is a separate issue from the affordability of the investment. However, he accepted that, in relation to the comparison with government bonds, those bonds would have liquidity, whereas the 2002 Payment would not. On this basis he would accept a marginal uplift in the assumed discount rate (from 5% to 5.5%); he would not accept that loss of liquidity could result in a discount rate of 20%, as propounded by Mr Stanton.

71. Mr Curran's evidence was that he saw the differential of between 3.25% and 4.25% between the discount rate (8.25%) applied to calculate the 2002 Payment and the assumed rate on government bonds of 4% to 5% as more than enough to compensate for the liquidity risk. He compared the position with a private placement under which investors would demand a better yield for the surrender of liquidity, but this would not generally be more than 1%, and significantly less than that in almost all cases.

72. In this regard we accept the evidence of Mr Curran and, to a large extent, that of Professor Dent. We consider that liquidity is a factor that impacts on yields, and that this should therefore be reflected in a discount rate. But we do not accept Mr Stanton's view as to the appropriate discount rate in these circumstances. It seems to us that a discount rate is reflective of yields, and not of the costs of borrowing to replace liquidity. Even if this were a valid factor, we consider Mr Stanton's view of the appropriate rate is nothing more than a hypothetical example, which is unsupported by any evidence of applicable rates and fails to take account of the real circumstances of Mr Curran's case.

73. We should at this stage consider a related submission made by HMRC as to the investment rationale of Mr Curran in making the 2002 Payment. It is convenient to do so here, because it impacts on the argument put by HMRC that Mr Curran's motive for making that payment was driven by the availability of tax relief. In his evidence, Mr Curran referred to the benefit of being able to mobilise the cash realised by obtaining the relief by investing at an IRR (internal rate of return) of between 15% and 20%. Even though this would have been at a cost of making the 2002 Payment, Mr Curran's evidence was that, depending on the performance of the amount released by way of tax relief, at the end of the 30-year term the aim was for him to have increased his net wealth. The original rationale for pre-paying the interest was based on Mr Curran's ability to deploy the funds released in respect of the interest relief at a superior return to the discounting effect.

74. HMRC point to this and argue that the discount rate of 5% used by Mr Curran and Professor Dent to calculate the investment benefit of making the 2002 Payment at £350,000 must be based on a false hypothesis that tying up the sum in question in government bonds was a realistic choice for Mr Curran. It is argued that Mr Curran's own evidence of his return expectations point to the contrary. If, instead of Professor Dent's 5% figure, the 20% rate of return referred to by Mr Curran were to be substituted as the relevant discount rate, it is submitted that it is self-evident that Mr Curran would have made significant losses by choosing to make the 2002 Payment, but for the availability of interest relief.

75. We do not accept these arguments. The comparison we are invited by HMRC to make is between apples and pears. The reason a 5% (or 5.5%) discount rate was applicable to the 2002 Payment was because it was equivalent to a risk-free investment, and government bonds were an appropriate proxy. Hypothetical investments with an IRR of 20% would not be risk-free, and so would not represent a proper proxy. As Professor Dent explained in evidence, the key issue for Mr Curran was not the absolute amount of return, but the return relative to the risk. It is not

therefore appropriate to value an investment with one risk profile that was actually made by Mr Curran by reference to an investment with a completely different risk profile. The fact that Mr Curran might invest at the riskier end of the market is nothing to the point; it cannot affect the valuation of an investment opportunity that does not fit that risk profile.

Was the 2002 Payment tax-motivated?

76. The evidence of Mr Curran, which we accept, was that, prior to the making of the 2002 Payment, Mr Byrne had explained to him that the interest he would be paying on the 2002 Loan by virtue of the 2002 Payment would be tax-deductible. Mr Byrne had also cautioned that by paying only the net present value of the interest Mr Curran would be receiving interest relief only on the discounted amount. Mr Byrne had further explained that in the future this could result in Mr Curran receiving interest on the 2002 Note but without the offset of interest expense, leaving Mr Curran in a net taxable position.

77. The effect of the 2002 Payment having been calculated on a net present value basis was that, in arithmetical terms, the amount of the payment was £890,000 as against aggregate interest over the remainder of the 30-year term of the 2002 Loan of approaching £2,400,000. Thus, in actual money terms, the amount of interest relief on the 2002 Payment would have been very much less than the relief, assuming the 2002 Loan went to term and was not repaid early, and that relief continued to be available, on the total interest payable under the 2002 Loan absent the 2002 Payment Agreement.

78. The effect of the 2002 Payment, therefore, was that Mr Curran obtained a lower amount of tax relief on interest than he would have done, on the assumptions we have referred to, by paying interest over the term of the 2002 Loan. On the other hand, he obtained the interest relief more quickly than if the interest had simply been left to accrue, and he eliminated the risk that relief would subsequently cease to be available for any reason. But in present value terms also, there was less tax relief on the interest paid by virtue of the 2002 Payment than on the interest on the 2002 Loan itself. The additional discount on which the 2002 Payment was calculated resulted in the amount of the 2002 payment being less than the net present value of the interest obligation. Relief would thereby be foregone on the difference.

79. We accept that Mr Curran considered the tax consequences, as it is evident he would have done in the case of any investment, but tax was only one of his considerations. We accept that he made his overall decision to make the payment on investment grounds, whilst appreciating that tax is an element in calculating the value of any investment decision.

80. It was submitted for HMRC that it is inconceivable that Mr Curran would have transacted in the way that he did, but for the perceived availability of interest relief. In making this submission, which requires us to make a finding of fact in this respect, HMRC rely on a number of factors.

81. The first is that Mr Curran's dealings with Mr Byrne were informal, flexible, undocumented in large part and do not have the appearance of commercial parties dealing at arm's length. HMRC point to Mr Byrne having liaised with Barclays Bank on behalf of Mr Curran and with Mr Curran's accountant regarding the filing of Mr Curran's tax return for 2001/02. It is submitted that this is a strange thing for an arm's length moneylender to do. It is said that it is equally strange for an arm's length moneylender to suggest paying bank fees incurred by his borrower so that the borrower could make what became the 2002 Payment.

82. We see nothing in this submission. The relevant transactions were fully documented. The way in which Mr Curran and Mr Byrne conducted their business, in particular its relative informality and flexibility, tells us nothing about whether the transactions can be said to have been tax-motivated. Furthermore, we do not recognise the description of Mr Byrne as a moneylender. He was an entrepreneur, with an investment opportunity that he wanted to sell, both for the benefit of Mr Curran and his own benefit, and he was prepared to finance that investment. His contacts with Mr Curran's bank and accountant were wholly unexceptional. Nor is there any evidence that the dealings between Mr Curran and Mr Byrne were anything other than on arm's length terms. The evidence of the financial engineering and fine-tuning of the investments and their financing points in the opposite direction.

83. Nor do we regard the fact that Mr Curran was required to take quick decisions on the investment opportunities he was offered as anything to the point. Mr Curran was an investment banker and a sophisticated private investor. He was well-used to rapid financial decisions having to be taken. Furthermore, for the reasons we have indicated earlier, we do not consider that the due diligence, in the context of the opportunity on offer, can be characterised as inadequate, or in any way suggesting that the investment was uncommercial and merely a means to obtain interest relief.

84. The timing of the 2002 Payment was just before the end of the tax year 2001/02. Mr Curran explained that he accepted the offer to make the 2002 Payment as soon as possible after it was made in order to put his money to work as quickly as possible. His evidence was that he would have taken this course of action even if the end of the tax year had not been imminent. Whilst we accept that Mr Curran had an investment imperative to act on an opportunity that he had evaluated as beneficial to him, it is not credible that the opportunity to obtain tax relief one year earlier by making the 2002 Payment just before, rather than just after, the end of the tax year did not play a part in his thinking. We find that it did. We also find that Mr Byrne was just as aware of the tax implications, and that he would have been concerned that there was nothing in the investment structure that would deny Mr Curran interest relief that would otherwise be expected. This explains Mr Byrne's reference, in his email of 3 April 2002, to circularity. However, taking tax into account, and structuring a transaction so as not to fail to obtain tax relief, amounts to no more than an element of sensible investment planning, and did not in this case render the transaction as a whole tax-motivated.

The February 2003 transaction

85. The offer by Opes to Mr Curran in February 2003 to make a further debt investment in SOP by way of the 2003 Notes was in order that further capital could be raised for the purchase of further properties in Stratford. This was not accompanied by any further requirement to introduce equity in the form of preference shares. But the 2002 Notes, as well as providing their own investment return to Mr Curran, would also add leverage to the existing equity investment in the way we described earlier.

86. We accept that the investment rationale for the February 2003 transaction was the same as that for the February 2003 transaction. We note that the accounts of SOP for the period ended 28 February 2003 show an accounting loss (interest costs exceeding rental income and other profits). Professor Dent explained that those accounts in any event would not have shown any unrealised gains on SOP's investment properties, since the accounts would, in accordance with accounting convention, have continued to record the investment properties at historic cost. The accounts in fact state that the investment properties are valued at cost as, in the directors' opinion, this is not materially different from their value to the company at 28 February 2003. On this basis, and in the absence of any other evidence of value, we find that there was no material unrealised gain at the material time. On the other hand, on disposals of £193,442, an actual profit of £11,558 had been realised. SOP was in a start-up phase, and nothing in the accounts would, in our view, have affected the investment rationale.

87. The 2003 Loan and the 2003 Note had the same interest differential (0.5%) as the corresponding 2002 Loan and 2002 Note. This was a benefit to Mr Curran, in the same way as it was for the February 2002 transaction.

88. The terms of the 2003 Loan, the 2003 Note, the 2003 Deed of Charge and other ancillary documents were materially identical to their 2002 counterparts. Our findings therefore in relation to the February 2002 transaction apply equally therefore to the February 2003 transaction.

The 2003 Payment

89. A little more than one month after Mr Curran borrowed the 2003 Loan, he was offered the opportunity to prepay the interest on it. This followed the pattern of the 2002 Loan and the 2002 Payment, and we consider that it is reasonable to infer that, by the time of the 2003 Loan it was expected (though not certain) that the opportunity to pre-pay would likewise be offered. Such a transaction had, as we have described in relation to the 2002 transactions, commercial advantages both for Mr Curran and the Byrne group. But although this was likely to have been an expected outcome, it lacked any degree of certainty that would enable the 2003 Loan and the 2003 Payment to be regarded as a combined transaction. We apply in this regard the same analysis that we adopted in relation to the 2002 transactions.

90. Our findings in relation to the 2003 Payment are the same as those for the 2002 Payment.

The 2005 transactions

91. The statement of agreed facts sets out the details of the Interim Loans. In evidence before us it was confirmed that these loans were used to make investments in London (two properties), Verbier, Switzerland (one property) and Portugal (four properties). Mr Curran resides in one of the London properties, the other was a basement in the same building, which has since been sold. The Verbier property was purchased with monies borrowed from UBS, but part of the monies borrowed under the Interim Loans was used to make staged payments throughout construction of that property. The Portugal properties were purchased with the assistance of finance from Barclays Bank.

The 2005 Restructuring

92. The 2005 Restructuring amounted to no more than the rationalisation of the Interim Loans that existed between Mr Curran and the Byrne group. Although these loans carried a lower interest rate (7.75%) than the 2002 Loan (8%), which along with the 2003 Loan (also 7.75%) was not to be refinanced, it is understandable commercially that the refinancing was of the short-term Interim Loans, rather than the 30-year term loans.

93. The effect of the 2005 Restructuring was to consolidate the numerous Interim Loans (with their associated documentation and differing cash flows), which simplified the arrangements between Mr Curran, TLL and OFL. At the same time, Mr Curran was being offered a lower interest rate (7.6%) than that applicable on the Interim Loans.

94. The offer of the 2005 Restructuring also provided Mr Curran with the opportunity to participate in a further investment (the Gable House investment) that Mr Byrne had executed some six months earlier. Gable House was a property on Stratford High Street in respect of which there was an opportunity for significant capital growth depending upon a successful renegotiation of the lease with the tenant.

95. As regards Mr Byrne's rationale for requiring Mr Curran to charge the 2002 Notes and the 2003 Notes as security for the 2002 and 2005 Loans (rather than the 2002 and 2003 Loan) Mr Curran's evidence, which we accept, was that Mr Byrne had explained to him that it made sense to concentrate the security held by his lending companies on the loans with the highest present value. The present value of the 2003 Loan (which became unsecured) was low – having regard to the fact that it was payable over 28 years, and the interest had been pre-paid – whereas the value of the 2005 Loan (which was payable on demand) was many times higher.

96. Following the restructuring the 2002 and 2003 Notes remained charged, but under new deeds of charge dated respectively 16 August 2005, and not under either the 2002 Deed of Charge or the 2003 Deed of Charge. The 2002 and 2003 Notes were each released from the 2002 Deed of Charge and the 2003 Deed of Charge respectively by deeds of release executed by TLL and OFL respectively on that date. The consequence was that a disposal of the 2002 Notes would no longer give rise to a

requirement that Mr Curran repay the 2002 Loan, and a disposal of the 2003 Notes would no longer result in repayment of the 2003 Loan.

Dispute in relation to the 2002 and 2003 transactions

97. The enquiry into Mr Curran's 2001/02 tax return was initially handled by Mr Baird of the Complex Personal Returns ("CPR") team in Manchester. Following consultation with Mr Preshaw (at that time the Group Director of the Manchester Special Compliance Office ("SCO")), an investigation under Code of Practice 8 ("COP 8") was commenced, headed by Ms Feighan. COP 8 was used rather than COP 9, because HMRC did not consider that the case involved fraud.

98. The investigation into Mr Curran's 2002/03 tax return was not commenced until 25 January 2005, at which point Ms Feighan wrote to Mr Curran to inform him that the investigation would proceed under COP 8.

99. In evidence Ms Feighan confirmed, and we accept, that the guidance she followed in her investigation was that in the SCO Manual. The Enquiry Manual was used for general procedure, such as assessment, but if there was any conflict between the two, the SCO Manual would prevail. Based on the SCO Manual, Ms Feighan's evidence as to the practice she adopted was that any offer made by a taxpayer must be made formally to the Commissioners for HMRC, and the decision on whether to accept or reject an offer is therefore the prerogative of the Commissioners, with that authority being in most cases delegated to Group Director level. At Ms Feighan's level, accordingly, she would not have delegated authority to make a formal acceptance of an offer of settlement.

100. Ms Feighan explained the usual process adopted in a negotiated settlement. The first step would be the authorisation to proceed along a contract settlement route. An offer from the taxpayer would be invited. That offer would be received in the SCO office. The officer, such as Ms Feighan, would submit the offer, along with the officer's settlement report to the Group Director who had authority to accept or reject the offer. The settlement report would include a detailed history of the case, notes of meetings, technical advice received from head office specialists and any compromises reached. If the offer was accepted the file would be passed to a settlement officer (not the original officer) who would issue the letter of acceptance.

Meeting of 26 February 2004

101. This meeting was held to discuss Mr Curran's 2001/02 claim for interest relief. We referred to it previously in the context of whether the 2002 payment was a combined transaction with the 2002 Loan. It was attended by Mr Curran and his advisers Mr Ritzema and Ms Kate Brierley, and from HMRC by Ms Feighan and Mr Preshaw.

102. The meeting discussed the 2002 transactions in some detail, and towards the end Ms Feighan outlined HMRC's then current concerns:

(1) There was a concern over the effect of the RPPA formula in the 2002 Payment Agreement. As Ms Feighan outlined it, the concern was that the formula would reduce the capital outstanding on an early repayment of principal, in particular if this took place soon after the 2002 Payment. Effectively, therefore, paying interest reduces capital, and the concern was that this was driven by tax considerations. Mr Curran had considered the tax consequences of the 2002 Payment, but it had not occurred to him that there might be beneficial tax consequences to repaying the 2002 Loan early, after having made the 2002 Payment. He had not considered repaying the principal of the 2002 Loan; the prepayment provision in the 2002 Loan Agreement had been inserted by Mr Byrne to cater for an eventuality such as the sale of the entire enterprise (which we take to mean the Byrne group) or if Mr Byrne were to cease to be associated with the group. It was not a matter that concerned Mr Curran.

In her evidence to us, Ms Feighan accepted that her concern regarding the operation of the RPPA formula would not arise if the 2002 Loan were not repaid early.

(2) Ms Feighan also referred to her concern that the 2002 transactions exploited a mismatch between the treatment of interest paid by an individual (giving rise to an immediate deduction) and interest to which a corporate lender is entitled (taxable as it accrues for accounting purposes). Ms Feighan summarised her concern in relation to (1) and (2) as being that the amount prepaid by the 2002 Payment might not in fact be correctly characterised as "interest".

(3) Ms Feighan considered it possible that s 787 ICTA might apply to deny relief, and/or that a Ramsay[4] approach was appropriate. Ms Feighan told us that these were routine issues to raise at the outset of an SCO investigation.

103. Following that meeting, Ms Feighan contacted Ms Marrable of HMRC's business tax division, who, prior to registration of the case with SCO, had been advising Mr Baird, and who subsequently provided Ms Feighan with specialist input in relation to the tax mismatch aspects of the case. In due course, as we shall describe, from about January 2005 specialist advice in relation to relief for the 2002 and 2003 Payments as interest would be sought from Mr Rogers, who was HMRC's technical expert on this subject.

104. In an email dated 17 March 2004 Ms Feighan confirmed to Ms Marrable that Mr Curran appeared keen to co-operate with HMRC, and that his agents, the Briar Group, had promptly supplied everything requested. She records that Mr Curran, when questioned about the RPPA formula, had been "completely unfazed" and had explained that discounting the principal if interest was prepaid was a normal formula in commercial use. Whilst this was more common in larger transactions, Mr Curran had made the point that part of the attraction of his dealing with Mr Byrne was that he was using techniques for private investment that were more commonly associated in larger institutional finance.

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[4] *W T Ramsay Ltd v IRC* [1981] STC 174

Progress of investigation and issue of closure notice for 2001/02

105. On 14 June 2004, Ms Feighan sent a notice under s 20 TMA to Bristol & West, seeking documents relating to Tailored BW Loans Limited in connection with Mr Curran's tax affairs. No other s 20 notices were issued; in particular, no notice was sent to Mr Byrne, TLL or SOP. Ms Feighan's enquiries of Bristol & West did not uncover any information of assistance to HMRC's investigation or cast doubt on the information supplied by Mr Curran.

106. Almost seven months passed following the February meeting without Mr Curran or his advisers being given any indication from Ms Feighan of when she anticipated concluding the enquiries. Concerned at the lack of progress being made with the investigation, Mr Curran applied on 21 September 2004 to the General Commissioners for a closure notice for the years ended 5 April 2001 (not material to this appeal) and 5 April 2002. Before the matter came before the General Commissioners Ms Feighan issued a closure notice for 2001/02, which denied the interest relief on the 2002 Payment.

107. During this period SIS itself had chased Ms Feighan for a progress update on 26 August 2004 (but had received no response) and again on 23 November 2004. At that point, on 24 November 2004, Ms Feighan responded, stating that she had not given the case as much time as she would have wanted, and that the case badly needed some close review and refocusing.

108. There followed a number of emails between Ms Feighan and Ms Marrable, which culminated in Mr Rogers becoming involved as the technical adviser. On 19 January 2005 Mr Rogers, having been given little time to respond and therefore having not examined the facts as closely as he would have liked, provided Ms Feighan with a technical note which referred to two possible challenges to Mr Curran's claim for interest relief in respect of the 2002 Payment. The first was on the basis that the amount in question was not "interest". The second was the possible application of s 787. Mr Rogers ended his note with an enigmatic reference to "Ramsay?", indicating that he had been unable fully to consider that issue The note was then converted by Ms Feighan into a letter to the Briars Group, dated 20 January 2005, including a short paragraph, added by Ms Marrable, on *Ramsay*.

109. A letter from Ms Feighan to Mr Ritzema dated 25 January 2005 opened an enquiry into Mr Curran's tax return for 2002/03. No closure notice was ever issued in respect of that return.

110. On 11 April 2005, Mr Ritzema wrote to Ms Feighan with a detailed response to the technical arguments contained in Ms Feighan's letter of 20 January. Ms Feighan did nothing with that letter until 11 May 2005, at which point she referred it to Mr Rogers for advice. Mr Rogers then considered the matter in more depth than he had previously been able, but concluded, in a letter to Ms Feighan of 13 June 2005 that he remained of the view that the payments were not of interest. With additions from Stephen Paulard, a colleague of Mr Rogers, in relation to s 787 and *Ramsay*, this technical note then became the basis for a letter from Ms Feighan to the Briars Group on 21 July 2005.

Herbert Smith's letter of 17 October 2005

111. There was considerable focus on the letter written by Herbert Smith on 17 October 2005, following its appointment by Mr Curran on 30 September 2005, in reply to Ms Feighan's letter of 21 July. It is HMRC's case that this letter, although purporting to disclose all facts and circumstances, failed to do so, with the result that the Settlement Agreement, whenever made, is voidable for material non-disclosure.

112. The opening paragraphs of the Herbert Smith letter are:

> "We set out below all relevant details relating to:
>
> (1) the loan made by Tailored Loans Limited to Mr Curran used to acquire an interest in Stratford Opportunities; and
>
> (2) the prepayment of interest under that loan.
>
> You will be aware of much of this detail but we set it out below so that your decision to allow relief is taken in light of all the facts and circumstances and the proper analysis of the law. We consider Mr Curran's claim for interest relief in his tax returns for 2001-02 and 2002-03 should be allowed for the reasons set out below.
>
> Please note that this letter focuses on the facts in relation to the claim for relief made for the year of assessment 2001-02 but we understand the facts relating to the claim for relief in the year of assessment 2002-03 to be substantially identical except for the amounts claimed. The statements made below should therefore be equally applicable to that claim for relief."

113. At the time of writing this letter, Herbert Smith had seen the documentation relating to the 2002 transactions but had not seen the documents for the 2003 transactions. Ms Feighan, who at that time had not herself seen all the documents relating to the 2003 transactions, understood that the relevant details being provided were those relevant to the claim for relief in 2001/02 and 2002/03.

114. Although the letter refers (in para 1.1.8) to Mr Curran having agreed to grant security over the 2002 Note by way of a Deed of Charge granting a fixed charge to TLL, there is no reference in the letter to the 2005 Restructuring. At the material time, Herbert Smith were not aware of that restructuring, and were not aware that the Deeds of Charge over the 2002 and 2003 Notes had been released or that the 2003 Loan had become unsecured.

115. Ms Gething was the author of the Herbert Smith letter. It was put to her by Mr Fisher in cross-examination that a reasonable reader of para 1.1.8 would assume that the security arrangements remained in place, and that if Ms Gething herself had known of the 2005 Restructuring, she would have made reference to it in her letter.

116. Ms Gething's evidence was that the information being provided to HMRC in the letter was that relevant to the tax years in question. As interest relief was claimed on an annual basis, subsequent events would have no bearing on the claim for a relief for a particular period. As the release of the 2002 Deed of Charge was not pertinent to the relief claimed in the relevant year, Ms Gething expressed the view that, had she

actually been aware of that fact, she did not think that she would necessarily have included it in the letter.

117. The letter goes on to deal with the statutory conditions for relief. It comments:

> "Section 363 has no bearing on the relief as Mr Curran has not 'recovered any amount of capital' from Stratford Opportunities. He still holds the Preference Shares and the Loan Note. Indeed, no dividends have been paid on the Preference Shares and no other benefits or payments have been received by him from Stratford Opportunities other than the interest on the Loan Note."

118. It was further put to Ms Gething that the inclusion of this paragraph, dealing as it did with circumstances outside the relevant tax years, suggested that the letter was not solely directed to those years, and that the 2005 Restructuring, had it been known to Ms Gething, would have been referred to in the letter. Ms Gething thought that her reference to s 363 must have been in response to some specific point raised by HMRC in the letter of 21 July 2005. But that is not the case: that letter expressly did not consider the statutory conditions. Alternatively, Ms Gething said that the charging of the 2002 Note formed no part of the statutory relief.

119. It is difficult, at a distance of some seven years, and with the benefit (or, more pertinently perhaps, the burden) of hindsight for any author of a letter to be certain of what, if known, might have been incorporated into it. We accept Ms Gething's evidence that she would not necessarily have referred to the 2005 Restructuring, for the reasons of relevance that she gave. But, judging from the careful attention to detail apparent from the letter itself, we think it equally likely that she would have done, and would at the same time have explained the irrelevance of it to the claims for relief for the two years in question. But, whether or not it would have been included in the letter, it is a matter for us, and we consider later, the extent to which its omission can be regarded as a material non-disclosure in relation to the Settlement Agreement.

120. Mr Ritzema was also, at the material time, unaware of the 2005 Restructuring. His evidence, which we accept, was that, had he known, he would not have considered it relevant to Mr Curran's claims for relief in respect of the 2002 and 2003 Payments since the existence of charges is no part of the statutory conditions for relief. Ms Feighan also said that she understood that the existence of charges was not a statutory requirement, and further understood that this was the view of the HMRC technical specialists. But again, that does not determine whether the failure to disclose it can be regarded as a material non-disclosure in relation to the Settlement Agreement.

The Settlement Meeting

121. Prior to the Settlement Meeting on 3 November 2005, Ms Feighan, on 28 October 2005, obtained advice from Mr Rogers concerning Herbert Smith's letter of 17 October 2005. Mr Rogers explained, in a written note to Ms Feighan, that it was general policy for technical specialists not to attend meetings when a negotiated

settlement was in prospect. His technical view remained that the 2002 and 2003 Payments were not of interest, and that if agreement could not be reached, HMRC should be prepared to litigate.

122. Mr Rogers also put forward his own view as to what might represent an acceptable settlement. He said that anything less than 50% would be unacceptable. Ms Feighan confirmed that she understood this to mean that no more than half of the payments should be allowed as a deduction. Mr Rogers also expressed the view that the tax at stake in this case was "relatively small" and that the scheme had only been used in this specific case. He counselled that it had to be made clear that any agreement would be conditional on Mr Curran agreeing that he would not repeat the transactions that had given rise to the disputed claims. Mr Rogers said that if Mr Curran intended to do so, it would be better to "lance the boil" at that stage by litigating.

123. Following receipt of Mr Rogers' note, Ms Feighan met him on 2 November 2005 to discuss his technical advice. Ms Feighan's evidence was that at that meeting she had explained to Mr Rogers that it would not necessarily be the case that Mr Curran would accept what was being put forward by HMRC. The evidence of Ms Feighan was that Mr Rogers said that she should aim for 50%. Although Mr Gammie argues that this is contradicted by the Settlement Report, prepared shortly prior to HMRC's formal acceptance of the Letter of Offer in October 2007, where Ms Feighan had recorded that Mr Rogers had concurred in a 50/50 basis of compromise, and to some extent the statement of agreed facts (para 6.9 of which refers to a discussion of the proposal with Mr Rogers), we accept Ms Feighan's oral evidence in this respect. We consider it unlikely that Mr Rogers in fact concurred with the 50/50 proposal before it was put at the Settlement Meeting. We also accept Ms Feighan's evidence that the 50/50 offer was not something that had been formulated before the Settlement Meeting.

124. Ms Feighan also consulted her Group Director, Ms Gregory, and it was agreed that Ms Gregory would attend the Settlement Meeting. Ms Gregory was aware at that time of the contents of Mr Rogers' note. Ms Feighan's evidence was that Ms Gregory was also fully aware of the negotiated settlement which was hoped to be the outcome of the meeting. At that stage, as we find, this was the 50% basis as outlined in Mr Rogers' note.

125. In the event, because of certain travel difficulties, it proved impossible for Ms Gregory to attend the Settlement Meeting. It therefore went ahead with Ms Feighan being accompanied by Mr Hewitt, who had no involvement with or knowledge of the case, as note taker from HMRC.

126. Crucial areas of dispute revolve around the Settlement Meeting. It is argued for Mr Curran that all the fundamental terms of settlement in relation to the claims for interest relief for 2001/02 and 2002/03 were orally accepted by HMRC at the Settlement Meeting, in that all the terms pertaining to the availability of relief were agreed, though some calculations needed to be carried out following the meeting in order to determine the precise quantum of the relief. It is argued by way of analogy

that it is not uncommon in banking transactions for the terms of an agreement to be agreed between the parties with financial calculations to follow. On this basis it is argued that the Settlement Agreement was binding by 2 December 2005, the date on which the final form of the Letter of Offer and Side Letter were sent to HMRC. For HMRC, it is said that the Settlement Agreement was concluded on 1 November 2007, the date on which HMRC formally accepted the Letter of Offer and the Side Letter dated 2 December 2005.

127. The basis of the settlement, leaving aside when the Settlement Agreement was made and a dispute as to the proper interpretation of certain of its terms to which we shall return, was that Mr Curran would be allowed 50% of the relief he had claimed in the tax year in question, and that the remaining 50% would be spread forward to be allowed on an accruals basis over the remaining period of the 2002 and 2003 Loans respectively (we refer to this as the "50/50 settlement"). In fact it was not quite as simple as that. Although the initial 50% relief was to be allowed in relation to 50% of the 2002 and 2003 Payments, which reflected the discounted payments that Mr Curran had made, the remaining 50% was based on actual interest that would have fallen due, in other words not discounted.

128. According to Ms Feighan, and we accept her evidence in this respect, Herbert Smith had argued that a settlement on the basis only of 50% relief, whilst that might be a workable solution on the footing that the loans would immediately be repaid (because going forward it was accepted that no further interest relief would then be available), would not resolve the position if the loans were not repaid. In those circumstances then, as Ms Feighan described it, the argument was that if, by way of compromise, the prepayment was being viewed as deductible in some way, albeit that it was not interest, then if the loan were to be maintained for 30 years, it would be reasonable to give relief for the remaining 50% spread over a period.

129. The basis of settlement was, accordingly, different from that which Mr Rogers' had suggested was the limit of acceptability for HMRC. It arose out of the discussions at the meeting. Ms Feighan had of course explained to Mr Rogers that settlement would depend on negotiation, and although Ms Gregory had been unable to attend the meeting, Ms Feighan telephoned her on two occasions during breaks to check that Ms Gregory was content with the proposals that were to be put on the table, culminating in the 50/50 settlement proposal outlined above, which Ms Gregory agreed.

130. There is a dispute concerning what happened at the meeting regarding disposals of the 2002 and 2003 Notes being restricted. In his evidence, Mr Curran said that, specifically, HMRC (through Ms Feighan) raised at the meeting the issue whether ongoing relief (that is, the 50% relief spread forward) should continue to be available were Mr Curran to dispose of his investments in SOP. Mr Curran said that he would not agree to such a restriction, and that accordingly no such term was included in the Settlement Agreement.

131. It was common ground that there was no such term in the Settlement Agreement. Mr Curran's evidence was that he recalled that, shortly after the

possibility of 50% being allowed on an ongoing basis had been raised, there was a break in the meeting when the HMRC representatives left the room to have a private discussion. When Ms Feighan returned, according to Mr Curran, she suggested that Mr Curran would not be able to sell the 2002 and 2003 Notes. He then replied to the effect: What investor would restrict themselves from selling their investment? What if somebody came in and offered me a ridiculous price tomorrow?

132. Mr Ritzema's evidence also recalled discussion of Mr Curran's insistence that he would not accept any settlement unless it enabled him to dispose of his investments. Mr Ritzema's recollection was that this was a matter discussed during a break in the meeting, which may well have been the break referred to by Mr Curran, and that it was Mr Curran who raised the point. Mr Ritzema was, understandably, unable to recall the precise conversations, but he was clear that this was an important point for Mr Curran.

133. Mr Ritzema said that, following the break in which Mr Curran had raised the issue, Mr Curran explained to Ms Feighan that this was a key point for him and that Ms Feighan eventually understood the point and accepted it. However, confusingly, Mr Ritzema linked this acceptance with the clause in the Side Letter dealing with the consequences of early repayment of the Loans, which disqualified only future interest relief. Ms Gething, the only other meeting participant to give evidence, could not recall discussion of the point.

134. Ms Feighan's evidence is that she gave no consideration to whether the 2002 and 2003 Notes should be retained by Mr Curran, and that she neither discussed this with Ms Gregory during the break in the meeting nor did she raise the point with Mr Curran. Ms Feighan's evidence is supported by the lack of any reference in the notes taken by any of the participants in the meeting to this issue.

135. Mr Gammie sought to explain the absence of a contemporaneous note of this issue by pointing to the fact that the various notes had, by the stage this point was said to have been raised, been largely reduced to figures rather than narrative discussion. However, we find that the fact that the notes do not contain a record of what, from Mr Curran's side certainly, and likely also HMRC's, would have been a material point, a strong indication that the point was not raised. Furthermore, if it had been discussed in the way Mr Curran says it was, we would have expected Mr Curran's advisers to have insisted that it be included as an express term of the Side Letter.

136. We do not consider that Mr Curran was in any way trying to mislead the Tribunal. We believe however that his recollection of events is not accurate in this respect. The most likely explanation is that Mr Curran did raise this point, but only with his own advisers. We accept Ms Feighan's evidence that she did not raise the issue, and that she did not consider it.

137. Furthermore, although Mr Rogers had referred in his note to the need to secure agreement from Mr Curran that he would not repeat the transactions in question, Ms Feighan did not raise this point at the Settlement Meeting.

138. We find that the only condition stipulated by Ms Feighan for the proposed 50/50 settlement was that Mr Curran should not repay the loans before expiry of their 30-year terms.

139. We find that, following the negotiation of the terms of the settlement, Ms Feighan explained the procedure to be adopted. The various notes of the meeting confirm that the next formal step was that Mr Ritzema would prepare the consequential computations, and that there would then be a letter of offer made by Mr Curran to HMRC.

The Settlement Agreement

140. The documented Settlement Agreement took the form of a Letter of Offer, made to HMRC, signed by Mr Curran and dated 2 December 2005. In light of the circumstances, the opening paragraph contained the following statement which, on its face, appears rather incongruous:

> "The tax on the statement below is unpaid, wholly or in part, because of my failure to meet all my obligations under the Taxes Acts. On the basis that no proceedings are taken against me now or at any time in the future for that tax, or for any penalties, surcharge and interest that may be due on it [Mr Curran offered the sum of £313,158.40, all of which had been paid on account]."

141. As was explained in evidence, this form of words is standard procedure in any settlement agreement between a taxpayer and HMRC. We accept it as such. We do not consider that the wording of it is material to our determination of when the Settlement Agreement became binding. It is not evidence that any offer must have come from Mr Curran. Nor, if there was such an agreement reached at the Settlement Meeting, would such an agreement have been undone by the form of the Letter of Offer.

142. The evidence was that, following the Settlement Meeting, there was no substantive negotiation of the basis of settlement, namely the 50/50 proposal, but that the parties were agreeing and computing the quantum of relief and their respective calculations in that regard. As Ms Feighan acknowledged, all the terms that were documented in the Settlement Agreement had been discussed at the Settlement Meeting. No new terms were included, other than purely mechanical terms: see clauses 7 and 8 of the Settlement Agreement below.

143. The Letter of Offer, according to its terms, was subject to the Side Letter, which expressed the "offer" contained in the Letter of Offer as being subject to certain conditions. The terms of this Side Letter are important, and we set almost all of its terms in full:

> "1. The following conditions are accepted by HMRC on the understanding that I [Mr Curran] have made a full and complete disclosure of all relevant facts relating to:

(a) the £1,000,000 loan advanced by me, per the loan agreement dated 22nd February 2002 by Tailored Loans Limited and,

(b) the £850,000 loan advanced to me, per the loan agreement dated 10th February 2003 by Tailored Loans Limited.

5 2. It concludes the enquiries into my personal affairs, all other points having been resolved in correspondence with my advisors, The Briars Group, for the years 2001/2002 and 2002/2003.

3. In each case subject to point 4. below:

(a) I have agreed that I will not repay either of the loans prior to the
10 original loan agreement capital repayment dates i.e. 21st February 2032 and 9th February 2033 respectively.

(b) I undertake to advise HMRC within one month of the relevant date if any capital repayments are made.

(c) Early repayment of either of the loans will disqualify me from
15 the right to the reliefs described at point 6 below but will not disqualify me for those such reliefs that have already accrued prior to such early repayment.

4. The loans may be repaid:

(a) upon my death;

20 (b) in the event of the insolvency of Tailored Loans Limited; or

(c) To the extent that I am obliged to repay the loans as a matter of law

and in such circumstances the other provisions of point 3. above will not apply.

25 5. The terms of the negotiated settlement have included agreement by HMRC to allow 50% of the amounts prepaid as interest to Tailored Loans Limited to be relieved as interest in the respective years of payment i.e. 2001/2002 and 2002/2003.

6. The remaining sums in respect of both loans are to be treated as if
30 half of the loan interest due on each loan were accrued and paid by me over the remaining span of both of the loans. Specifically;

(a) The £1,000,000 loan will give rise to qualifying interest for each year until the end of the period of the loan (30 years) of £40,000 per annum. In the final year, 2031/2032 that figure will be £35,288.

35 (b) The £850,000 loan will give rise to qualifying interest for each year until the end of the period of the loan (30 years) of £32,938 per annum. In the final year 2032/2033 that figure will be £27,975.

(c) To the extent that the qualifying interest is not set against income and gains in the year it is accrued and deemed to arise in (a)
40 and (b) above, it may be carried forward indefinitely and set against income and gains in any subsequent year.

7. HMRC make a repayment of tax (including the repayment supplement and compensation tax credit) in the sum of £449,748.44 to

> be paid by BACS transfer within five days of receipt by HMRC of the signed letter of offer to the account in the name of Garrett Curran …
>
> 8. The relief for the year 05/06 will be given through HMRC authorising my employer to adjust my PAYE coding …"

144. Payments were made by HMRC pursuant to clause 7 on 8 December 2005 and 12 April 2006, and the coding notice for year 2005/06 was issued on 8 December 2005. The arrangements for the initial repayments were made by Ms Feighan in an email to an HMRC officer, Duncan Cameron, at Chapel Wharf, sent on 2 December 2005. The email refers to the "finally agreed letters" and suggests achieving "repayments to match what I have agreed", and issuing manual coding to Mr Curran's employer to reflect further allowances. Following further detailed calculations from Mr Ritzema, Ms Feighan wrote by email on 8 December 2005 to Julie O'Connell, Duncan Cameron and Margaret Morris at Chapel Wharf summarising the repayments being made to settle the enquiries into Mr Curran's claim for loan interest relief in accordance with the Letter of Offer and Side Letter. Ms Feighan says in her email to Ms Morris that the repayments should be authorised on that day, and asks to be contacted if there is any problem with authorisation. It is evident from this, and we so find, that it was not Ms Feighan who authorised the payments, but that they were authorised to be made.

Settlement Agreement – subsequent events

145. At the time the Letter of Offer and Side Letter were submitted by Mr Curran, and HMRC acted upon them by making repayments of tax and issuing PAYE coding notices, there was no formal acceptance by HMRC of Mr Curran's "offer". HMRC realised in October 2007 that the paperwork had not been finalised. Ms Feighan's evidence was that she had made a "complete hash" of the matter. On 1 October 2007, Ms Feighan's team leader (at that time, Ms Mannion) wrote to Ms Feighan suggesting that Ms Feighan write to Mr Curran in fairly low key terms, saying that the issue of a letter of acceptance by HMRC in respect of the Settlement Agreement had been overlooked and asking him to confirm in writing that he was happy for the offer to proceed.

146. On 2 October 2007, HMRC wrote to Mr Curran noting that the letter of 2 December 2005 was never formally accepted by HMRC and asking Mr Curran to confirm that he still wished to make the offer. Ms Feighan's evidence in this regard was that she was not asking Mr Curran to repeat his offer, but merely to confirm that it should go forward un-amended for consideration. Nor did Ms Feighan put Mr Curran on notice that he needed to tell HMRC about anything that had happened since the Letter of Offer and Side Letter were sent by Mr Curran to HMRC.

147. On 22 October 2007 Mr Curran wrote to HMRC confirming that he would like the offer to go forward "as agreed at the time". That was followed, on 1 November 2007, by HMRC writing to Mr Curran formally accepting the offer contained in the Letter of Offer.

The 2006 transactions

148. Mr Curran's sale of his preference shares in SOP, as a consequence of the offer from Opes on 22 February 2006 and Mr Curran's acceptance of it on that date, realised Mr Curran a 40% return on that investment.

5 149. On 2 April 2006, Opes wrote to Mr Curran proposing that:

(1) TLL purchase the 2002 and 2003 Notes for £1,999,780.48;

(2) Mr Curran use £1,063,221.01 of the proceeds to repay the 2005 Loan; and

(3) Mr Curran use the balance to make an unsecured loan to Mr Byrne (at an interest rate of 11.89%, repayable on one month's notice).

10 150. Mr Curran sought advice on this proposal from Herbert Smith. He was concerned whether this would be a breach of the Settlement Agreement. Herbert Smith advised him that it would not. Mr Curran proceeded with the transactions. As a consequence, the 2002 and 2003 Loans became unsecured.

The 2007 transactions

15 151. Between 2003 and 2007, Mr Byrne continued to expand his property investment group, and he took the Byrne group in a new direction by procuring the purchase of English Courtyard Limited by OGH from Chasophie Limited on 24 August 2006 for £11,000,000 (with £4,750,000 of the purchase price left outstanding, accruing interest at 18% per annum). English Courtyard Limited was involved in the residential care
20 home business. In particular, it was a housebuilder and developer operating at the luxury end of the retirement market. It was a long-established company, having operated for about 25 years.

152. In 2007, Mr Byrne moved his offices to a new building – Aria House – where he occupied an entire office floor with around 16 to 20 workstations. Mr Byrne
25 described to Mr Curran that amongst his plans for the new office was an idea to allow clients to work from the office. This would enable Mr Byrne to be in close proximity to his clients and to brainstorm ideas with them.

153. Mr Curran left his job at Dresdner Kleinwort Benson in May 2007, and based himself at Aria House on a part-time basis. He explained in evidence that he was
30 involved in litigation with his former employer and needed a base from which to work. It made sense for Mr Curran to work from Mr Byrne's offices as he had so much invested in Mr Byrne's companies. Mr Curran's wife who, with two employees, was launching a new recruitment consultancy business, also moved into Aria House for a period, before moving to a serviced office.

35 *Investments in WPV and OGH*

154. The opportunity afforded by Opes for Mr Curran to purchase a 46.2% equity stake in WPV, was accompanied by put and call options entitling Mr Curran to sell his shares after five years to Mr Byrne at a pre-determined price (and thus at a pre-determined annual return of 20%), and Mr Byrne to require Mr Curran to sell after

three years with a pre-determined return of 25% per annum. This gave Mr Byrne a potential interest in the equity upside, whilst providing Mr Curran with downside protection. The long term projected upside for the equity investors in the project was £24,000,000, on which basis a 46.2% interest was projected to be worth, potentially, £11,088,000.

155. It was originally intended that the debt owed by OGH to Chasophie Limited as a result of the acquisition of English Courtyard Limited would be repaid by the end of November 2006. The fact that the debt remained outstanding on 10 March 2007 was straining the relationship between Mr Byrne and Chasophie Limited, a company that had been a client of Mr Byrne for some time prior to the sale of the English Courtyard group.

156. It was in order to assist OGH in making payment to Chasophie, that Opes offered Mr Curran the opportunity to make a debt investment in OGH in the form of the 2007 Note.

157. The 2007 Loan was made by TLL to Mr Curran for the purpose of enabling him to finance the purchase of the WPV Shares and the 2007 Note. The 2007 Loan contained no right to pay the principal early (unlike the 2002 and 2003 Loans). The reason was that, in the discussions leading up to the Settlement Agreement, HMRC had objected to the inclusion of such a right in the earlier Loans.

The 2007 Payment

158. Consistent with the pattern adopted in relation to the 2002 and 2003 Loans, Mr Curran was offered the opportunity, prior to the end of tax year 2006/07, to pre-pay the interest on the 2007 Loan at a discounted rate greater than the interest rate on the loan (a discount rate of 8.25%, as opposed to an interest rate of 8%).

159. As the pattern was identical, we apply the same analysis to the 2007 Loan as we did in respect of the 2002 and 2003 Loans. It follows that we consider that, in relation to the 2007 Loan, Mr Curran would have expected to have been offered the ability to pay the interest in advance on similar terms to those offered in relation to the earlier loans. But we find that this was not certain, and that it does not result in the 2007 Loan and the 2007 Payment being capable of being regarded as a combined transaction.

Claim for relief in respect of the 2007 Payment

160. In evidence, Mr Curran explained his understanding that the Settlement Agreement was not limited in its terms to the 2002 and 2003 Payments. He thought that HMRC would apply the terms of the Settlement Agreement to any transaction with materially identical fact patters to those of the 2002 and 2003 Payments. In cross-examination, Mr Curran explained this viewpoint in terms of his own experience of negotiating a complicated transaction, on which consensus is then reached. The fact of that consensus, in Mr Curran's view, would then create an

expectation in future negotiations on something very similar, that there would be less scope for negotiation.

161. After making the 2007 Payment, Mr Curran completed his tax return for 2006/07 with a claim for interest relief on the whole of the 2007 Payment. He did so on the advice of Mr Ritzema, who advised that he should file on the basis of the law (that is to say, his understanding of the law), but with an expectation that, after discussion with HMRC, relief would be allowed on the basis of the Settlement Agreement. It had been expected that the matter would be finalised by the first or second quarter of 2008.

OGH default

162. OGH encountered liquidity difficulties and defaulted on the 2007 Note and the OGH Loan. In consequence, and under the terms of the loans, Mr Curran appointed a receiver to protect his interests.

163. In an attempt to alleviate these liquidity problems, TLL sought to liquidate its loan portfolio. On 29 July 2008, part of the portfolio (the 2002, 2003 and 2007 Loans) was sold to Ronan Curran, Mr Curran's brother, who had also been a client of Mr Byrne. This followed unsuccessful attempts by Mr Byrne to market the loan to sophisticated investors. According to Mr Curran, his understanding was that there were four such investors. We accept that Mr Byrne attempted to market the loans in this way.

164. The loans were sold to Ronan Curran at a price of £15,000, based on a discount rate of 25%, which was in the region of the rates that had been suggested to Mr Byrne by the potential third party investors. Professor Dent's evidence included his view that the loans did not have any appreciable value at the time of their sale to Ronan Curran.

165. Mr Curran was asked in cross-examination why it was that he had not himself bought these loans from TLL. His initial reply was that he had not thought of doing so. He had in mind at the relevant time that the Settlement Agreement precluded a repayment of the 2002 and 2003 Loans. In subsequent evidence, Mr Curran explained that, without doing the calculations at the time, it had been intuitively obvious to him that the present value of the ongoing relief under the Settlement Agreement (which would have been forfeited for the future if the 2002 and 2003 Loans had been repaid) was worth more to him than the present value of his obligation to repay the loans.

166. Mr Curran illustrated this by reference to evidence of the valuation of the 2002 and 2003 Loans contained in Mr Stanton's report. That report assumed that the 2002 and 2003 Loans would have become immediately repayable in the event of a liquidation of TLL. On that basis, Mr Stanton applied the RPPA formula assuming a repayment of the loans at July 2008, giving repayment amounts, for the 2002 and 2003 Loans of £141,000 and £111,000 respectively. Mr Curran's approach was to compare those values with the value of a strip of interest relief running, as it did on

the 2002 and 2003 Payments combined, at the rate of £72,000 per year. Given certain assumptions, such as Mr Curran having taxable income going forward to the future, this strip of income, deriving from the Government, could then be valued by applying a discount rate applicable to gilts of corresponding maturity. This, explained Mr Curran, would give a present value of more than £500,000, which would compare favourably to the benefit, taking the then combined values of the 2002 and 2003 Loans, of monetising £252,000.

167. Mr Curran further explained that, although he did not engage in any detailed thinking at the time (but relied on his financial intuition) a decision in 2008 to repay the 2002 and 2003 Loans would have involved weighing the benefit of certainty in the elimination of his liability to repay the loans against the loss of an asset, namely the right to interest relief against his taxable income. His rationale was that he would rather keep the cash and invest it himself, rather than prepay the loans. This analysis appeared to be based, at least in part, on a misunderstanding that a repayment of the 2002 or 2003 Loans would have resulted in a recapture of relief already given. Nonetheless, we consider that this represented the sort of intuitive evaluation Mr Curran arrived at when considering what he should do at the relevant time in relation to the Loans.

Position of the 2002, 2003 and 2007 Loans

168. We accept the evidence of Mr Curran that all of the 2002, 2003 and 2007 Loans were transferred to Ronan Curran, and that they remain outstanding. There is no documentary evidence to the contrary, and there is nothing to throw any doubt on Mr Curran's evidence in this respect.

Discussion

The Interest issue

A. Were the 2002, 2003 and 2007 Payments of "interest"?

169. Mr Curran's case is simple. He says that, according to the authorities we shall look at in a moment, interest is a charge made for the use or deprivation of a principal sum over a period of time. Mr Gammie submitted that, although interest is usually paid periodically in arrears, there is no requirement that interest be charged in this way. A lender might decide to charge interest monthly in advance, or to charge a single lump sum interest payment. The 2002, 2003 and 2007 Payments (which we shall refer to collectively as "the Payments") were simply payments in advance of interest, discounted to reflect early payment, which fulfilled Mr Curran's interest obligations under the various Loans.

170. HMRC submit that the Payments are not payments of interest at all. Rather they are capital payments, for one of two reasons. First, because they are payments, not of interest itself, but in lieu of interest payable under the Loan Agreements, the effect of the present value discount being to capitalise the future income stream and extinguish

the relevant lenders' rights to receive all future interest payments. Secondly, that the Payments are repayments of the loan principal.

171. We need therefore to look at some well-established authority on the meaning of interest. In doing so we make the initial observation that the classification of the Payments is a matter of law and not of economics, so that we attach no weight to the evidence of either Professor Dent of Mr Stanton in so far as it purported to classify the Payments.

The meaning of interest

172. Our starting point is the legislation under which interest relief is claimed. For the purposes of s 360 ICTA, interest is defined by s 832(1) of that Act as "both annual or yearly interest and interest other than annual interest". There is no further statutory definition of interest.

173. We were referred to a number of well-known cases that have explored the meaning of "interest". The classic formulation is that of Rowlatt J in *Bennett v Ogston* (1930) 15 TC 374 (at p 379) where he described interest as "payment by time for the use of money". Even earlier than that, however, in *Bond v Barrow Haematite Steel* [1902] 1 Ch 353 (at p 363) Farwell J had described interest as "compensation for delay in payment". These cases describe the position by reference to both sides of the interest coin, that of the borrower on the one hand, paying for the use of money, and the lender on the other, being compensated for the deprivation of that use.

174. The meaning of interest from the perspective of the lender was also addressed in *Riches v Westminster Bank Ltd* [1947] AC 390 (HL) where Lord Wright said (at p 400):

> "… the essence of interest is that it is a payment which becomes due because the creditor has not had his money at the due date. It may be regarded either as representing the profit he might have made if he had had the use of the money, or conversely the loss he suffered because he had not that use. The general idea is that he is entitled to compensation for the deprivation."

175. Those cases were among the authorities examined by Megarry J in *Re Euro Hotel (Belgravia) Ltd* [1975] STC 682 where, in the course of finding that amounts described as interest paid in respect of units of calculation under a sub-building agreement were not interest as such because there was no debt due to the recipient of the interest, the learned judge firstly made it clear that the question is one of the true nature of the payment and said (at p691D):

> "It seems to me that running through the cases there is the concept that as a general rule two requirements must be satisfied for a payment to amount to interest, and a fortiori to amount to 'interest of money'. First, there must be a sum of money by reference to which the payment which is said to be interest is to be ascertained. A payment cannot be 'interest of money' unless there is the requisite 'money' for the payment to be said to be 'interest of'. Plainly, there are sums of 'money' in the

> present case. Second, those sums of money must be sums that are due to the person entitled to the alleged interest; and it is this latter requirement that is mainly in issue before me. I do not, of course, say that in every case these two requirements are exhaustive, or that they are inescapable. Thus I do not see why payments should not be 'interest of money' if A lends money to B and stipulates that the interest should be paid not to him but to X: yet for the ordinary case I think that they suffice."

176. There was no disagreement that these authorities establish that the simple test of what constitutes interest is that it is a payment for the use of money, or, taking the other side of the coin, a payment received for the deprivation of money by reference to the period of time of that use or deprivation.

177. Mr Gammie submitted that the Payments satisfied this test. Mr Curran was given the use of the loan principal in respect of each of the Loans for a term of 30 years. He was contractually bound to pay interest on those sums to the lenders, representing a charge for his use of the principal and the lenders' deprivation of the principal. The lenders offered Mr Curran the opportunity to pay the interest under the Loans earlier than originally agreed, at a discount to reflect early payment. Having accepted those offers, Mr Curran made the Payments to the lenders, fulfilling his interest obligations under the relevant loans.

178. Mr Gammie argued that the mere fact that Mr Curran paid the interest on the loans in advance, instead of in arrears, cannot alter the nature of the Payments. That is clearly right, and HMRC did not argue to the contrary. A payment in respect of a sum of money due that is calculated by reference to the time of use of that money, or the time of deprivation of that use, is interest however it is paid, whether periodically, or in a single or multiple lump sum, whether in advance or in arrear. The mechanics of payment do not affect the characterisation of a payment as interest if it satisfies the basic test as set out in the authorities.

179. HMRC put their case in this way. They say that the Payments do not fall within the meaning that has been given to interest. Mr Curran was required to pay an amount equal to the present value of the interest that would otherwise have been due and payable over time. Although interest may be described as "payment by time for use of money", the present value of a future payment, discounted to reflect the time value of money, cannot by definition be "interest", because the effect of the present value calculation is to remove the effect of time.

180. In putting HMRC's case on this issue, Ms McCarthy argued that it was important not only to have regard to the contracts (the Loans and the Payment Agreements) but to analyse the respective rights and obligations of the parties, and in that way to ascertain what the payments were made for. Ms McCarthy referred us to *Lomax v Peter Dixon & Son Ltd* (1943) 25 TC 353, and to the well-known judgment of Lord Greene MR.

181. From *Lomax v Dixon* we can conclude that there are some cases where the nature of a receipt may be determined by the proper interpretation of the contract, and

there are others that are not susceptible to that analysis. An example of the former, given by Lord Greene (at p 362), is that in *Rushkin Investments Ltd v Copeman* (1943) 25 TC 187, where a loan at interest, which was satisfied, as to both principal and interest, by the assignment of certain ground rents. In such a case it could not seriously be suggested that the value of the ground rents ought not to be treated as made up of the principal advanced plus interest. The answer to the question whether the receipt was to be regarded as capital or as income (or which part of the receipt was to be accorded which classification) was to be found in the contract itself.

182. Lord Greene went on to give an illustration of a case in which mere interpretation of the contract would lead nowhere. He said (at p 362):

> "If A lends B £100 on the terms that B will pay him £110 at the expiration of two years, interpretation of the contract tells us that B's obligation is to make this payment; it tells us nothing more. The contract does not explain the nature of the £10. Yet who could doubt that the £10 represented interest for the two years? The justification for reaching this conclusion may well be that, as the transaction is obviously a commercial one, the lender must be presumed to have acted on ordinary commercial lines and to have stipulated for interest on his money. In the case supposed, the £10, if regarded as interest, is obviously interest at a reasonable commercial rate, a circumstance which helps to stamp it as interest."

183. Having then referred to two examples (*Lord Howard de Walden v Beck* 23 TC 384; and *Bennett v Ogston*) where the circumstances, rather than the contract itself, gave a straightforward answer to the question of the nature of a payment, Lord Greene turned his attention (at p 363) to a more complicated case:

> "The position is more complicated when A lends £100 to B at a reasonable commercial rate of interest and stipulated for payment of £120 at the maturity of the loan. In such a case it may well be that A requires payment of the £20 as compensation for the capital risk; or it may merely be deferred interest. If it be proved that the former was the case by evidence of what took place during the negotiations, it is difficult to see on what principle the £20 ought to be treated as income. In the absence of such proof, what inference ought to be drawn? Something may, perhaps, depend on the length of time for which the money is lent. If the period is short it is perhaps easier to treat the £20 as deferred interest. The longer the period the greater the element of risk, and if it was, say, 10 years, the probability that the £20 was not intended to be deferred interest would seem to be greater. A good example of the difficulty is to be found in the contracts of loan which used to be made on a gold basis when the currency had left, or was expected to leave, the gold standard. In such contracts the amount to be repaid was fixed by reference to the price of gold ruling at the repayment date, and if the currency depreciated in terms of gold, there was a corresponding increase in the amount of sterling to be repaid at the maturity of the loan. It could scarcely be suggested that this excess ought to be treated as income when the whole object of the contract

> was to ensure that the lender should not suffer a capital loss due to the depreciation of the currency.
>
> I refer to these problems, not for the purpose of attempting to solve them, but in order to show that there can be no general rule that any sum which a lender receives over and above the amount which he lends ought to be treated as income. Each case must, in my opinion, depend on its own facts and evidence *dehors* the contract must always be admissible in order to explain what the contract itself usually disregards, namely, the quality which ought to be attributed to the sum in question."

184. In this passage, therefore, Lord Greene is identifying a payment, the quality of which cannot be discerned from the contract. He is saying that the nature of such a payment must be determined by reference to the facts, and that evidence of those facts is not confined to the contract itself. In his example, however, Lord Greene did not suggest that the stipulated interest amount could be determined to be something other than interest; his focus was solely on the premium element. In relation to the interest, it is the contract that determines the quality of the payment.

185. That this is so is confirmed by what Lord Greene goes on to explain. He looks at the various ways in which a company may choose to raise money by way of an issue of debentures. He contrasts (at p 364) the various alternatives available to a company unable to issue its debentures at par at a normal rate of interest. On the one hand such a company might make the issue at par, but at a high rate of interest. The defect in the security is expressed in terms of interest, and it is unquestionably income and taxable as such, even though part of it is attributable to capital risk. By contrast, interest may be fixed at a more normal level and the issue may be made at a discount, or the issue may be made at par with a premium on redemption. The defect in the security is in these cases expressed in terms of capital, and would not, accordingly, be taxable as income. Lord Greene then summarises the position in the following way (at p 364-5):

> "I have for simplicity considered only the case where the variations in issue price and rates of interest are due only to differences in the security offered. This, of course, is not necessarily always the case. The precise terms of an issue may be affected by a variety of other considerations - the taste of the market; the terms of previous issues by the company; the political or international situation; the expectation of changes in money rates; the instability of the currency, etc. But these matters do not affect the principle. It is perfectly true that a company may be able to obtain subscribers by issuing debentures at par at a high rate of interest just as well as it can by issuing them at a lower rate of interest below par or with a premium on redemption. The two methods are, however, essentially different although actuarially they will normally produce the same result. But for Income Tax purposes the result is, I think, different, according as the company chooses the one method rather than the other. The Crown is, in my opinion, bound by the company's choice and cannot go behind it."

Were the Payments capital in nature?

186. It is clear, and there was no dispute on this, that the nature of a payment cannot be determined by the label attached to it, nor, to use the language of Megarry J in *Chevron Petroleum (UK) Ltd v BP Petroleum Development Ltd* [1981] STC 689 (at p 694), by the "wrappings" that might otherwise conceal the nature of the payments. Ms McCarthy argued that the reference to an interest prepayment in clause 2 of the 2002 Payment Agreement (by way of example) could not be conclusive. She submitted that the sum paid was not in fulfilment of Mr Curran's obligation under the 2002 Loan Agreement. Essentially the 2002 Payment Agreement was a new contract, the making of the 2002 Payment overtook (or in the terms expressed by Ms McCarthy, surpassed) the interest obligations under the 2002 Loan Agreement. It was not a payment of interest, but a payment in lieu of interest.

187. That proposition in itself would not, of course, say anything about the nature of the 2002 Payment, were it not to be interest. What Ms McCarthy then submits is that, adopting the economic analysis of the prepayment of interest that was set out in Herbert Smith's letter of 28 October 2008 (namely that economically it was no different to Mr Curran or any other investor buying interest payments using a discounted present value calculation), then since a purchase of interest coupons does not give rise to an interest payment, by analogy nor can the 2002 Payment.

188. What is said here is that there is clear authority from *IRC v Paget* [1938] 1 All ER 392 that payments received in circumstances where future interest obligations are disposed of are capital payments. In that case Miss Paget was the holder of foreign bonds. As the payment of interest on those bonds was blocked and could only be paid in foreign currency, she sold the interest coupons to, or through, coupon dealers in London. The Court of Appeal held that the proceeds of sale of the interest coupons were not income for income tax purposes. Sir Wilfred Greene MR said (at p 398):

> "The purchase price received by Miss Paget was not income arising from the bonds at all. It arose from contracts of sale and purchase, whereby Miss Paget sold whatever right she had to receive such income in the future, as well as her right to take what was offered by the defaulting debtors. It is, in my opinion, quite impossible to treat this as equivalent in any sense to "income arising from" the bonds."

189. On this basis, HMRC's contention is that it is wrong to treat the Payments as interest arising from the Loan Agreements. Rather, the Payments extinguished Mr Curran's obligations under the Loan Agreements to pay interest periodically throughout the remainder of each term. Indeed, it is further argued, whilst Mr Curran did not issue zero coupon bonds, the economic profile of the Loans taken together with the Payments was similar to that of a zero coupon bond.

190. Ms McCarthy also submitted that Mr Curran's case should not be treated any differently from that of Ms Paget. Mr Curran should be regarded as the purchaser of the interest payments under the Loan Agreements, and the Payments should likewise be regarded as of capital. Ms McCarthy cited *Schaffer v Cattermole* [1980] STC 650 in support of the proposition that the principle, derived from *Paget*, that the proceeds of sale of a right to receive income in the future cannot be treated as income, but are

capital, must be true for both the vendor and the purchaser. In that case, Shaw LJ (at 654) makes clear that, in a case of a sale and purchase of a government bond with accrued interest, there is both a sale and acquisition of a capital asset.

191. We do not consider that *Paget* can provide an answer in this case. The nature of the Payments depends on the actual transaction that has been undertaken. It cannot be determined by resort to economic equivalence. Whether or not the prepayment of interest can, in economic terms, be compared with the purchase and sale of interest coupons is irrelevant. Lord Greene made perfectly clear that actuarial equivalence does not lead to the same tax result. Mr Curran did not issue a zero coupon bond nor did he purchase strips of interest or anything else. His tax treatment cannot therefore be determined by reference to *Paget*, nor is he in the position of the purchaser in *Schaffer*.

192. An alternative argument put by Ms McCarthy, on the same theme of the payments constituting capital sums, is that the Payments were repayments of principal. This argument is essentially founded upon the effect of the RPPA formula under the Payment Agreements. We need not rehearse the terms of those agreements, but the argument requires us to focus on three aspects:

(1) Firstly, Mr Curran was permitted to pay all the "interest payable" for the Interest Periods for the remainder of the term of the Loans.

(2) Secondly, the Payment Agreements provide that "Subject to paragraph 4(b) [the RPPA formula] below, the full amount of the Loan remains payable notwithstanding the payment of the Interest Payment Amount".

(3) The RPPA formula itself. Ms McCarthy here draws our attention to the joint agreement of Professor Dent and Mr Stanton that the RPPA formula "determined the amount payable by Mr Curran to the lenders (TLL and OFL) in the event of the loans being repaid before their maturity dates" and that its effect "was to reduce the amount otherwise payable by a sum equivalent to the present value of the interest relating to the period after the early redemption date".

193. We do not consider that the views of the experts as to the effect of the RPPA formula carry the resolution of this issue any further. The agreed conclusion of the experts on this matter is, if we may respectfully say so, trite. In any event it is clear from the evidence that, whilst there was (unsurprising) agreement in the terms expressed, the experts differed on the effect of application of the formula, Professor Dent analysing it as a rebate of interest and Mr Stanton taking the view that there was simply a payment of a reduced amount of principal.

194. The first element of HMRC's argument refers to the reference to "interest payable". They say that interest was only payable once it had accrued, so that the only interest paid by Mr Curran under the Payment Agreements is the interest that had accrued at the date of the Payment Agreements.

195. As a matter of construction, this is clearly wrong. The reference to "interest payable" in the Payment Agreement refers in terms to interest payable for all the Interest Periods up to the end of the terms of the Loans. Interest payable does not

mean interest presently payable. Such a construction, in terms of the prepayment of interest, would make no sense at all.

196. As Mr Gammie argued, HMRC are faced with the fact that the Payment Agreements specifically provide that the full amount of the Loans remain outstanding. Ms McCarthy rightly points out that this provision is subject to the case where the whole or any part of the Loan is repaid early, but absent any such early repayment, the principal does remain outstanding.

197. Nevertheless, Ms McCarthy argues that the existence of the RPPA formula does have the result that the Payments are not of interest but are of capital. This argument is put in two ways. The first is that the amounts outstanding under the Loans must be analysed at any given time on the assumption that the Loans would be repaid early at that time. HMRC's analysis is that the amount payable under the RPPA formula would then represent the whole amount of the principal repaid. On this analysis therefore, when the Payments were made, the amount of principal repayable according to the formula would largely correspond to the difference between the original amount of principal less the amounts of the Payments.

198. We do not accept this argument. It depends on a hypothesis and not on the actual transaction we have to consider. It is entirely unclear how a characterisation of the Payments as capital at the outset could be maintained as the Loans continued in being and, on HMRC's analysis, the amount of principal repayable increased over time. We say nothing about the position that might obtain were a prepayment of interest and an early repayment of principal to be part of a pre-ordained transaction or series of transactions; despite the early indications, no case has been made by HMRC under *Ramsay*.

199. Ms McCarthy's second argument in this respect did not depend on an hypothesis, but on valuation. She submitted that the obligation to pay the principal amount at the end of the term of 30 years could not, following the prepayment of interest, be an obligation in the amount of the principal sum. The value of the obligation would, as we have seen, be discounted.

200. This argument in our view is also misconceived. It attempts to suggest that in ascertaining whether a payment is of interest or principal one should have regard to the value of the obligation to pay principal, rather than the substance of the actual obligation. It confuses value with the nature of the obligation, and can have no part in the analysis of the nature of the Payments.

201. Mr Gammie argued, consistently with the opinion of Professor Dent, that the RPPA formula essentially gave rise to a rebate of interest. We shall comment on that submission in a moment, but Ms McCarthy argued that if this was right, then the correct analysis was that all Mr Curran had done was to make a payment in advance. That, argued Ms McCarthy was not the same as making a payment of interest; in effect we understand the argument to be that the Payments were inchoate payments.

202. In support of this argument Ms McCarthy referred us to the judgment of the Court of Appeal in *Bronester v Priddle* [1961] 1 WLR 1294, a case concerning whether an excess amount paid as advances over commission earned under a contract of employment was repayable. Essentially it was held that where advance payments had been made in anticipation of commission being earned, and the commission did not in fact become due, the excess amounts had to be repaid notwithstanding that the employment contract was silent on the matter.

203. We do not consider that *Bronester v Priddle* can assist Ms McCarthy. Her argument was that if the effect of the RPPA formula was to give rise to a rebate of interest, that would mean that the Payments, to the extent of the rebate, would have to be treated as a mere advance, and not as a payment of interest in the first place. But *Bronester v Priddle* was essentially a case determined by construction of the employment contract in question. The important point is that the payments in that case were advances that were repayable in the sense that they had to be set against the commission when it became due. The commission did not cease to be due, nor did the advance give rise to a lawful right to the money in the hands of the employee. By contrast, in this case the Payments had the effect that no further interest fell due, and there can be no doubt that the lenders had a lawful right to the Payments received.

Conclusions on "interest" issue

204. Despite Ms McCarthy's efforts, we are clear that her submissions in all these respects cannot succeed. On a proper construction of the Payment Agreements, we consider that the Payments were payments that fulfilled the obligation of Mr Curran to pay interest, because they were payments of interest. In this case the contractual documents are clear, and it is not necessary to resort to extrinsic evidence. The parties chose to lend and borrow at interest, and they chose to offer and accept that such interest be paid in advance, on discounted terms. That was the choice of the parties, that was the substance and reality of what was done and, adopting what Lord Greene said in *Lomax v Dixon*, the Crown cannot go behind that choice.

205. For the reasons we have given, we do not consider that the Payments were of a capital nature.

206. We consider that the Payments fall squarely within the meaning given to interest by the authorities. They were, from Mr Curran's perspective, payments by time for the use of money, and from the lenders' perspective payments for the deprivation of the principal sum over the term of the Loans. We reject the argument that the present value of a future payment, discounted to reflect the time value of money, cannot by definition be "interest" because the effect of the present value calculation is to remove the effect of time. It does not remove the effect of time; it reflects it. All that the discount used to calculate the amounts of the Payments did was reflect the fact that the interest was to be paid in advance, rather than being spread over the term of the Loans. It did not in any way affect the fact that the calculation of the interest, both before and after discounting, reflected the period for which Mr Curran was entitled to the use of the principal sum. That interest, aggregated over the terms of the Loans, was calculated by reference to the term of

each Loan. The discounting of that aggregate amount of interest, to produce the amounts of the Payments, reflected only the accelerated payment, and did not in any way impinge on the fact that the interest, and accordingly the Payments, were made by reference to the time for which the monies lent could be used.

5 207. We conclude therefore that the Payments were of interest. Our conclusion in this respect does not depend upon the effect of the RPPA formula being that there would be a rebate of interest. That being the case, we do not think it would be right for us, in the context of the present case, to express a view on that.

B. Were the Payments interest paid at a rate in excess of a reasonable
10 **commercial rate?**

208. There is no dispute that the headline rate on each of the 2002, 2003 and 2007 Loans is anything but a reasonable commercial rate. But HMRC say that, in the circumstances of the Payments (and thus, as we have found, the prepayments of interest), the interest rate paid in respect of the Loans was grossly in excess of a
15 commercial rate. Were that to be the case, then the excess amount would be denied relief by s 353(3)(b) ICTA.

209. HMRC base this contention, firstly, on a submission that it is an essential feature of interest that it accrues by reference to the time that has elapsed. We do not accept that submission. There is nothing in the authorities to which we have referred
20 that suggests that a payment can only be interest if it is a payment "by time" that has already elapsed. A payment in advance can, as we have already found, equally be interest. That, if we may say, not only follows from the authorities, it is also the only conclusion that could be reached as a matter of common sense.

210. Secondly, Ms McCarthy repeated the argument that the rate had to be
25 determined by reference, not to the principal amount outstanding, but to the net present value of what was outstanding, or to the amount required to be paid under the RRPA formula were the Loans to have been repaid at the time of the making of the Payments.

211. Neither of these propositions can survive a moment's scrutiny. The Payments
30 were in respect of the whole of the interest liability over the terms of the Loans, discounted at the agreed interest rate. The hypothetical application of the RRPA is irrelevant to the calculation of the rate of interest paid in respect of the continuing use of the money borrowed by Mr Curran, or the continuing deprivation of the lenders in respect of the whole of the principal sum lent. Nor can the present value of the
35 obligation to repay the principal amount be anything to the point; it is the use or deprivation of the principal amount that gives interest its character, and the rate of interest therefore falls to be assessed by the same criterion, and not by valuation.

212. We therefore reject HMRC's submission in this respect.

C. Section 787 ICTA

213. As we have described, on the footing that the Payments have been found to be of interest, HMRC argues that the provisions of s 787 ICTA apply so as to deny Mr Curran interest relief.

5 214. We set out the terms of s 787 earlier, but for ease of reference we repeat those terms here:

> **787 Restriction of relief for payments of interest**
>
> (1) Relief shall not be given to any person under any provision of the Tax Acts in respect of any payment of interest if a scheme has been
10 effected or arrangements have been made (whether before or after the time when the payment is made) such that the sole or main benefit that might be expected to accrue to that person from the transaction under which the interest is paid was the obtaining of a reduction in tax liability by means of any such relief.
>
15 …
>
> (2) In this section "relief" means relief by way of deduction in computing profits or gains or deduction or set off against income or total profits.

215. We have found that Mr Curran took tax into account in deciding to enter into
20 the various transactions, but that he decided to enter into those transactions for investment reasons. That is not, however, conclusive, as s 787 refers not to the purpose of the taxpayer, but to the sole or main benefit that might be expected to accrue. Those words, although in a different tax context, were considered by the Court of Appeal in *Crown Bedding Co Ltd and another v IRC* 34 TC 107. Lord
25 Greene MR said (at p118):

> "[The] Sub-section speaks of the main benefit which might have been expected, it does not mean the main benefit which was in fact expected by those carrying out the transaction, but means the main benefit, in the opinion of the tribunal which ultimately has to decide, which might
30 have been expected by a person surveying all the facts and knowing all the law on the subject at the time. I do not mean that the views of directors, who are familiar with the facts, would be inadmissible in evidence. All I am saying is that the fact that directors expected or did not expect a particular result can by no means be conclusive of the
35 question although it may be evidence which the Commissioners should take into account in forming their opinion."

216. Accordingly, the test in s 787 is an objective test, although the expectations of Mr Curran as to any particular result should be taken into account.

217. The first question we consider in this connection is what, in the context of the
40 facts of this case, is the transaction under which the interest was paid. To assist us to answer this question we were taken to *MacNiven v Westmoreland Investments Ltd* [1998] STC 1132 in the Court of Appeal. In that case a company, WIL, had a large accrued interest liability to pension fund trustees which was of no benefit to it unless it actually paid the interest. The only way to achieve such payment was by means of a

loan from the trustees themselves. Such a loan was duly made, and the accrued interest liability was paid. The Court of Appeal held that on its natural construction s 787 did not require an examination of the circumstances surrounding each interest payment. The Special Commissioners had been correct to conclude that the transaction under which WIL paid the interest was the transaction giving rise to WIL's original borrowing from the trustees under which the accrued interest became payable, and that the main benefit of that transaction had been to reduce WIL's shorter term liabilities.

218. This approach was approved by Lord Hoffman in the House of Lords [2001] STC 237 (at p 260) where he said:

> "In my opinion it is plain that the 'transaction under which the interest was paid' is the original loan and not the arrangements which enabled WIL to pay it."

219. Mr Gammie relied on *MacNiven* to argue that in this case the transactions under which the interest was paid were the 2002, 2003 and 2007 Loans, and not the respective Payment Agreements. Ms McCarthy submitted that there was a distinction between the facts in *MacNiven* and the facts in this case that made all the difference. In *MacNiven* there was a genuine accrued interest liability, and all it did was make payment in respect of that liability. The interest that was paid was paid under the original loan agreement. By contrast, argues Ms McCarthy, in this case there was no liability or prospect of Mr Curran paying the interest under the Loans early. That opportunity arose out of a supervening transaction in each case, namely the Payment Agreements. It is accordingly, submits Ms McCarthy, the Payment Agreements that are the transactions by reference to which the sole or main benefit must be applied.

220. In our view there can be no inviolable rule that it is only the original loan that can be the transaction under which the interest is paid. Whilst arrangements enabling payment, such as the loan from the trustees to WIL, or any financing obtained by Mr Curran to enable him to make the Payments, would not be such a transaction, that is different from a transaction which gives an opportunity to make payment of interest in a different way than that envisaged under the original loan. It is a question to be determined according to the individual circumstances of a case as to what is the transaction under which interest has been paid.

221. In this case we find that the relevant transactions are the original Loans, as amended by the respective Payment Agreements. That the Payment Agreements operate to amend the Loan Agreements is clear from the terms of clause 5 of each Payment Agreement: "This letter does not constitute an amendment or variation to any term of the Loan Agreement *save as specifically provided for in this letter*." As the Payment Agreements made specific provision for the interest prepayments, notwithstanding the original provision for interest in the Loan Agreements, the Loan Agreements were amended or varied in that respect.

222. What this means is that we have to consider the benefit of the interest relief obtained by Mr Curran from the Payments as against the benefits of the original Loans, including the investments made by Mr Curran using the proceeds of those

Loans. In doing so we shall take into account the benefit to Mr Curran of receiving interest relief sooner than he would otherwise have done under the original Loans, and the non-tax benefits to him of making the Payments as opposed to paying interest over the terms of the Loans. We regard this as the proper approach, not only because in our view this represents the transaction under which the interest was paid, but also because we are required by s 787 to consider arrangements which may impact upon the benefits of the transaction.

223. In order to ascertain the benefits flowing from the relevant transaction, it is necessary to consider the position of the taxpayer before and after the transaction. If the position, properly analysed, is that the taxpayer has not received any enhancement of his existing position, or any material such enhancement, apart from the obtaining of interest relief, s 787 will prevent the relief from being obtained. That was the position in *Lancaster v IRC* [2000] STC (SCD) 138, where arrangements entered into for inheritance planning purposes involved a circular flow of funds. The taxpayer withdrew an amount of capital from a partnership account, and made a gift of that amount to his wife. His wife then made him a loan, and the money was credited to the taxpayer's partnership account. Relief for interest paid on the loan was refused, and the Special Commissioner dismissed the taxpayer's appeal. There was no financial benefit to the taxpayer in the entire arrangement apart from the interest relief. The taxpayer's position at the outset, owning partnership capital, was essentially the same as his position after the loan transaction.

224. The circumstances that arose in *Lancaster* are not replicated in this case. In relation to each of the Loans, Mr Curran obtained the benefit of his investment in the Loan Notes. In the case of the 2002 Loan, he was also enabled, by satisfying the contingency that he take up the 2002 Loan Notes, to obtain an equity interest in SOP. Comparing the position before and after the loan transactions, therefore, Mr Curran obtained certain benefits, as well as the interest relief on the making of the Payments, in contrast to a position of the taxpayer in *Lancaster* whose benefits were essentially the same after the transaction as they were before. It is therefore necessary to compare the benefit of the interest relief with the other benefits accruing to Mr Curran.

225. Whilst it is not necessary for every benefit to be capable of valuation in money terms in order that it be taken into account, where benefits are susceptible to such valuation the resultant values fall to be taken into account and compared. The question arises in this connection as to what is the appropriate comparison to make. On the one hand there is the benefit of interest relief; on the other the other benefits that the taxpayer derives from the relevant transaction. Any comparison made must be done on a consistent basis. Like must be compared with like.

226. Section 787 refers to the benefit of interest relief. In order for that to be a benefit, it is axiomatic that its value must be taken without regard to the cost of obtaining it. Except where arrangements may be made to eliminate such cost, the cost of making the interest payment will generally (if not always) exceed the benefit of tax relief on those payments. If such costs were to be taken into account no benefit in net terms could be said to have arisen. As that would defeat the evident purpose of s 787,

the reference to benefit must be taken to mean the gross benefit of the tax relief that would arise.

227. For comparison purposes, therefore, regard must be had to the gross benefits flowing from the relevant transaction. The amount of the borrowing is not for this 5 purpose netted off against the benefit. So, for example, the fact that an investment funded by a loan yields the same, or a lower return, than the cost of the corresponding borrowing does not mean that there is no benefit to be taken into account in respect of the investment. The benefit is the gross value of the investment.

228. On the other hand, if a benefit is indirectly obtained, such as in this case the 10 equity investment in SOP, which was financed separately by Mr Curran, but which he would not have been able to make but for his acquisition of the 2002 Loan Notes, any benefit can only be ascertained by taking into account the separate cost of obtaining that benefit. It is the net benefit, such as the profit potential taking into account the financing cost, of such an investment that falls to be included in the comparison 15 required to be made.

229. Applying this analysis to the transactions in question, it is plain that the obtaining of interest relief was not the sole or main benefit that might be expected to accrue to Mr Curran from the Loan transactions, as modified by the Payment Agreements. In each case Mr Curran obtained the benefit of the Loan Notes. Viewed 20 purely in terms of financial value, those benefits in each case outweighed the benefit of the interest relief obtained as a consequence of the Payments of interest. In the 2002 transactions, Mr Curran also received the benefit of profit potential on the equity investment in the preference shares in SOP. Taking all the circumstances into account, including the obtaining of interest relief earlier than it would otherwise have 25 been obtained under the Loans themselves, we find that the interest relief was not the sole or main benefit that might be expected to have accrued to Mr Curran.

230. In case we are found to be wrong in finding that the relevant transactions for s 787 purposes are the Loans as modified by the Payment Agreements, we turn to consider HMRC's submissions that, taking account only of the benefits obtained by 30 Mr Curran from making the Payments, the bare numbers spoke for themselves in showing that the sole or main benefit was the obtaining of the interest relief.

231. In closing submissions Ms McCarthy put forward a table to demonstrate in money value terms the correctness of that submission. We reproduce it below.

Year	**Tax relief**	**Present value gain (1)**	**Present value gain (2)**
2002	£355,998	£21,000 (£2,500 p.a. approx)	£350,000 (£3,077 p.a. approx)
2003	£302,315	£18,000 (£2,125 p.a.	£270,000 (£2,833 p.a.

		approx)	approx)
2007	£1,123,492	£84,000 (£8,750 p.a. approx)	£1,189,000 (£10,769 p.a. approx
Total	£1,781,805	£123,000 (£13,375 p.a. approx)	£1,809,000 (£16,679 p.a. approx)

232. The reference to "Present value gain (1)" is to the evidence given by Professor Dent as to the gain derived by Mr Curran in making the Payments of interest in advance at a discount rate higher than the interest rate on the Loans themselves. In each case the discount rate was ¼% higher than the corresponding interest rate. Professor Dent illustrated this by reference to the 2002 Loan (numbers are rounded). At the date of the 2002 Payment, the present value of all future interest payments, discounted at 8.00% was £911,000. The present value of those same interest payments, discounted at 8.25%, was £890,000. Mr Curran paid £890,000 to discharge his liability to future interest payments with a present value of £911,000. The gain to him was £21,000.

233. Present value gain (2) is also derived from Professor Dent's evidence. It arises because, in economic terms, following the making of each of the Payments, Mr Curran was relieved of his obligation to make the corresponding interest payments. The effect, as both Professor Dent and Mr Curran described it, on Mr Curran's cash flows was similar to making an investment of the amount paid early and gaining cash savings (which, in financial terms, are equivalent to cash receipts) for the remaining duration of the Loan.

234. Such an investment was effectively risk-free and, as we have earlier described, the standard benchmark for evaluating investments in risk-free opportunities is the rate of return on government bonds. This, according to Professor Dent, would amount to a rate of return (or redemption yield) of between 4% and 5%. Although something less that 1% should be added for the difference in liquidity between a gilt investment and the discharge of the interest obligation, the figure in the HMRC table is based, as was that of Professor Dent, on an assumed discount rate of 5%. Applying that discount rate, the present value of each of the interest obligations saved, the amount of each Payment, and the resultant "profit" were as follows:

Payment	**Present value of interest obligations saved**	**Amount of Payment**	**"Profit"**
2002	£1,240,000	£890,000	£350,000

2003	£1,021,000	£751,000	£270,000
2007	£3,783,000	£2,594,000	£1,189,000

235. Ms McCarthy submitted that the use of the interest rate on government bonds as a proxy for the applicable discount rate was based on a false hypothesis that Mr Curran would have invested in government bonds for 30 years. Mr Curran was looking for a 20% rate of return which, if substituted as the relevant discount rate, would give rise to a loss for Mr Curran, and not a profit.

236. For the reasons we described earlier, we reject this argument. The appropriate discount rate is that applicable to a proxy for a risk-free investment, and that is conveniently achieved by using the rate applied to government bonds, uplifted marginally to reflect loss of liquidity. For these purposes, therefore, we accept Professor Dent's figures as the basis on which we can make the necessary comparison of benefits accruing to Mr Curran.

237. In our view HMRC's table falls into the error of seeking to compare a gross benefit in the form of the tax relief on interest, with the net "gain" or benefit obtained by Mr Curran from making the Payments. The benefit of the interest relief must necessarily be calculated without regard to the cost, namely the amount of the Payment in each case. It is wrong to apply a different method of calculation when determining the other benefits accruing to Mr Curran. The appropriate comparison is not with the "gain" (that is the excess of the value of the interest obligation discharged over the amount of the Payment), but the value of that discharged obligation itself.

238. On this footing, we consider that the correct comparison is as follows. We replicate HMRC's table, substituting what we regard as the correct comparator (gross) figures for s 787 purposes:

Year	**Tax relief**	**Present value benefit (1)**	**Present value benefit (2)**
2002	£355,998	£911,000	£1,240,000
2003	£302,315	£769,000	£1,021,000
2007	£1,123,492	£2,678,000	£3,783,000

239. Whichever of the two bases of calculation are taken for the net present value of the interest obligation discharged (in (1), the rate of interest on the relevant loan, or in (2) the government gilt rate of 5%), the benefit of the interest relief is in each case outweighed by the other benefits to Mr Curran. We conclude therefore that, even if the transactions under which the interest was paid are the Payment Agreements only (and not the Loans as amended by the Payment Agreements), our conclusion would

be the same. Interest relief was not the sole or main benefit that might be expected to accrue to Mr Curran from those transactions.

Conclusions on 2002, 2003 and 2007 Payments

240. For the reasons we have given, we conclude that:

(1) The 2002, 2003 and 2007 Payments were payments of interest.

(2) Those Payments were not at a rate in excess of a commercial rate.

(3) Interest relief in respect of those Payments is not prevented from being given by s 787 ICTA.

241. Accordingly we find that the 2002, 2003 and 2007 Payments were of interest eligible for relief, in the respective years of assessment in which those Payments were made, under s 353 ICTA.

The Settlement Agreement issue

A. The validity of the Settlement Agreement

242. Our findings in relation to the 2002, 2003 and 2007 Payments, summarised above, effectively dispose of this appeal, subject to two caveats, each of which leads us now to consider the question of the validity of the Settlement Agreement. The first is that our conclusions on the Interest issue may subsequently be found to be wrong, in which event (subject to a separate issue of discovery) Mr Curran's case relies on the Settlement Agreement remaining valid and enforceable. The second is that, if we find that the Settlement Agreement is indeed invalid, as HMRC invite us to do, this may, on the basis of our conclusions on the Interest issue, require us to make further determinations in respect of outstanding assessments or the closure of open years of assessment.

243. We start with the relevant law. HMRC have responsibility for the care and management of income tax under s 1 of the Taxes Management Act 1970 ("TMA"), as applied to HMRC by s 5(1)(a) of the Commissioners for Revenue and Customs Act 2005 ("CRCA").

244. HMRC may make agreements with taxpayers. The effect of certain such agreements is set out in s 54 TMA which relevantly provides:

> "**54 Settling of appeals by agreement**
>
> (1) Subject to the provisions of this section, where a person gives notice of appeal and, before the appeal is determined by the Commissioners, the inspector or other proper officer of the Crown and the appellant come to an agreement, whether in writing or otherwise, that the assessment or decision under appeal should be treated as upheld without variation, or as varied in a particular manner or as discharged or cancelled, the like consequences shall ensue for all purposes as would have ensued if, at the time when the agreement was

> come to, the Commissioners had determined the appeal and had upheld the assessment or decision without variation, had varied it in that manner or had discharged or cancelled it, as the case may be.
>
> (2) Subsection (1) of this section shall not apply where, within thirty days from the date when the agreement was come to, the appellant gives notice in writing to the inspector or other proper officer of the Crown that he desires to repudiate or resile from the agreement.
>
> (3) Where an agreement is not in writing—
>
> > (a) the preceding provisions of this section shall not apply unless the fact that an agreement was come to, and the terms agreed, are confirmed by notice in writing given by the inspector or other proper officer of the Crown to the appellant or by the appellant to the inspector or other proper officer; and
> >
> > (b) the references in the said preceding provisions to the time when the agreement was come to shall be construed as references to the time of the giving of the said notice of confirmation…"

245. It will be apparent from the terms of s 54 that it is not concerned with the mechanics of the making of an agreement, but with the effect of an agreement once made. The question whether there is a valid agreement, the effect of which is then determined, in certain circumstances, by s 54 is almost always a matter of the general law (see *Schulenfrei v Hilton* [1998] STC 404).

246. Mr Curran contends that even if he is not – contrary to our earlier findings – entitled to the statutory interest relief, HMRC were precluded from issuing the discovery assessments by virtue of the Settlement Agreement.

247. Along with their forward tax agreement and construction arguments, HMRC say that the Settlement Agreement is voidable because of material non-disclosure by Mr Curran, and that it was avoided by the raising of the discovery assessments. Because the question of non-disclosure depends, to an extent, on the date the agreement was entered into, we must first consider that issue. Mr Curran's position is that agreement was reached at the Settlement Meeting on 3 November 2005, or at the latest by 2 December 2005, when Mr Curran signed the final version of the Letter of Offer and Side Letter and sent them (by fax and courier) to HMRC. HMRC say that the Settlement Agreement was not concluded until 2 November 2007, the date on which HMRC confirmed their agreement in writing to the Letter of Offer and Side Letter.

Conclusions on the Settlement Meeting

248. We accept that, whilst Ms Feighan had authority to negotiate a settlement with Mr Curran in respect of the tax years 2001/02 and 2002/03, she did not have actual authority to reach an agreement at the Settlement Meeting.

249. On the evidence of the Settlement Meeting itself, we conclude that this did not result at that time in an enforceable agreement between Mr Curran and HMRC. Having regard to the fact that the formal requirements of a letter of offer had been explained at the meeting, it would require cogent evidence that an enforceable

agreement had in fact been reached without such a letter having been produced. Whilst an accord of sorts was clearly reached, and which was later translated into the Side Letter, our view is that this was in the nature of an agreement in principle, which was at that stage non-binding. It required to be reduced to writing, and the terms themselves could at that stage have been the subject of further negotiation. The fact that a written agreement faithfully reflects what has earlier been negotiated does not of itself mean that agreement must necessarily be regarded as having been conclusively reached at the time of the negotiation. In this case, even though the evidence was that, in the event, following the Settlement Meeting there was no substantive further negotiation of the basis of the settlement, and that the terms of the Letter of Offer and Side Letter reflected the position reached at that meeting, with substantive discussions only on the quantum of relief and the necessary calculations, we do not consider that there was the required certainty on the part of both contracting parties immediately after the meeting that this would inevitably be the case.

The Letter of Offer

250. Mr Fisher pointed to the plain terms of the Letter of Offer itself. It was expressed as an offer. It was not an acceptance or any other form of written notification of an agreement. The Side Letter was itself consistent with this analysis. We agree. Although the form of the Letter of Offer and Side Letter is not of itself conclusive, it accords with our finding in relation to the Settlement Meeting. Any misunderstandings of the position that may have been entertained by Mr Curran or any of his advisers cannot affect the status in law of the Letter of Offer. It was in our view nothing more than an offer reflecting the negotiated terms.

251. It follows that we do not accept Mr Gammie's submission that the issue of the Letter of Offer by Mr Curran constituted notice in writing by him of an agreement for the purpose of s 54(3) TMA. At the stage the Letter of Offer was submitted, there was no agreement.

Tax repayment

252. The receipt by Ms Feighan of the Letter of Offer and Side Letter triggered the repayments on 7 and 8 December 2005. We have found that, although those repayments were not authorised by Ms Feighan herself, they were authorised by HMRC.

253. The repayments of tax were made only as a consequence of the settlement between Mr Curran and HMRC. They could not have been authorised on any other basis. The repayments were themselves performance of the agreement which had by that stage clearly been reached. The making of the repayments accordingly, in our view, constituted acceptance at that time by HMRC of the Letter of Offer and the Side Letter. No question of lack of authority on the part of Ms Feighan can arise in this context; the acceptance was by HMRC in making the repayments. We therefore conclude that the Settlement Agreement was a binding and enforceable agreement from 7 December 2005.

Application of s 54 TMA and s 5 CRCA

254. For the purpose of the application of s 54 to the agreement that arose, according to our finding, as a consequence of HMRC's performance of it, it is important to ascertain whether that agreement is or is not "in writing". If it is, then sub-sections (1) and (2) apply from the date of the agreement. If it is not, then s 54 will have effect only from the time of written confirmation.

255. In this case there was a written Letter of Offer and Side Agreement which, on our analysis, was accepted by HMRC by making the tax repayment on 7 December 2005. The terms of the agreement are thus set out in writing. However, we do not consider that this results in the agreement itself being in writing. Section 54(3) envisages not only that the terms agreed be confirmed in writing, but that the fact of the agreement must also be confirmed. The evident purpose of this provision is to provide evidential certainty, without the need for extrinsic evidence that an agreement has been concluded. Where an agreement is accepted by performance, that evidential certainty is absent unless or until there has been written confirmation of the agreement. On this basis, we therefore conclude that the agreement between Mr Curran and HMRC, which we have found was made on 7 December 2005, was not an agreement in writing, so that it is s 54(3) that must apply.

256. In that event, the deeming provisions of s 54 apply only where the terms agreed have been confirmed by notice in writing. There is no specified form of such a notice. The only requirement is that it should have been given by one party to the other. The intention of the section is to enable the effects of s 54 to apply only where there is documentary evidence of an agreement that has been made, but which is not itself in writing. Lack of formality should not therefore be a bar to the operation of the section. Anything in writing that has been sent by HMRC to the taxpayer, or vice versa, that reflects the agreement, is in our view, sufficient to constitute a notice in writing.

257. However, it is clear that the written notification must constitute not only a record of the terms of an agreement, but also the fact that an agreement has been reached. Even if a notice contains all the relevant terms, it cannot constitute a notice for s 54(3) purposes unless it has been issued after the agreement is reached, and itself confirms the fact of the agreement.

258. The Letter of Offer cannot satisfy this latter requirement. The agreement was made only on 7 December 2005, and the Letter of Offer was sent by Mr Curran on 2 December. It could not have confirmed the fact of the agreement, and did not do so.

259. HMRC submits that, to the extent that s 54 can apply, it operates from 1 November 2007, the date on which HMRC wrote to Mr Curran accepting the Letter of Offer. We agree, except that in our view this is not because the agreement was not reached before that date, it is because that was the date of the notice of confirmation. Although the agreement was in fact reached on 7 December 2005, it is treated, by s 54(3)(b) as having been reached for s 54 purposes on the date of the notice, namely 22 November 2007.

260. Even though s 54 applies to the Settlement Agreement, there is a dispute as to its effect for the various periods of assessment in question. Mr Curran's position is that it has effect for all periods, 2001/02, 2002/03 and succeeding years as provided by the agreement. HMRC say, firstly, that it cannot apply to 2002/03, because no appeal was made in respect of that year. Secondly they submit that an agreement made under s 54 cannot be binding as to the amount of relief available in future years.

261. On the first point we agree with HMRC. Although Mr Gammie argued that Mr Curran's appeal in respect of the 2001/02 assessment included an appeal against HMRC's decision to refuse relief, and so included 2002/03, we accept HMRC's argument that this cannot be so where the enquiry for the year 2002/03 remained open. Section 54 has no effect for the year 2002/03.

262. In relation to the second point, the extent of the effect of the application of s 54 was considered in *MacNiven*. In that case, to which we referred earlier in connection with s 787 ICTA, a scheme was said to have given rise to deductible charges on income for income tax purposes. HMRC raised assessments for the years 1987 to 1992. The taxpayer contended that it had entered into an agreement with HMRC under s 54 for the year ended 31 March 1988 and that this agreement had determined not only the question of what tax was payable in respect of that period, but also the amount of charges on income which were available to carry forward to subsequent accounting periods.

263. Lord Hope held that the effect of a s 54 agreement is to be found in the words of s 54 itself. It is limited to the same consequences as on the determination of an appeal. Lord Hope applied the reasoning of the Privy Council in *Caffoor and others (Trustees of the Abdul Caffoor Trust) v Comr of Income Tax, Columbo* [1961] AC 584 in finding (at [89] to [90]):

> **"[89]** … The finality that attaches to the determination of the appeal by the General Commissioners or by the Special Commissioners or to the settling of the appeal by agreement relates only to the amount chargeable under that assessment. The question as to the amount of any reliefs carried forward to subsequent periods remains open for examination as the assessment for each subsequent period is issued. This is because the Taxes Acts do not provide any means by which that amount may be determined conclusively, whether by appeal or by agreement, for any period other than that to which the assessment relates.
>
> **[90]** For these reasons I would hold that an agreement made under s 54 has no wider effect upon the position of either party than that which has been provided for by the statute. As Carnwath J indicated ([1997] STC 1103 at 1133), the issue turns simply and solely upon the machinery which the Taxes Acts provide for determining the amount in question between the commissioners and the taxpayer. That machinery is limited to determining conclusively the amount of tax chargeable for the year of assessment. It does not enable such determinations to be made, either on appeal or by agreement, as to the amounts of tax chargeable in future years."

264. On this basis, we agree with HMRC that s 54 can have no effect in relation to the succeeding periods for which it provided that relief would be available.

265. On the other hand, we do not consider that that is the end of the matter. On its terms s 54 applies only where there has been an appeal. It does not operate in other circumstances. It cannot, as *MacNiven* demonstrates, have effect for periods other than that to which the assessment (or adjustment) under appeal relates, even in a case where the agreement is as to the amount of a relief which is capable of being carried forward to subsequent years. But that does not mean that s 54 is the only means by which HMRC can be bound to an agreement. As we shall discuss later, when considering the question whether the Settlement Agreement is a forward tax agreement, it is clearly recognised that HMRC have a managerial discretion, so far as it is exercised within their powers, to enter into agreements with taxpayers which, independently of s 54, are binding on HMRC (see *Al Fayed and others v Advocate general for Scotland (representing the Inland Revenue Commissioners)* [2004] STC 1703, in which neither *MacNiven* nor *Caffoor* were cited as relevant authority).

266. The deeming provisions of s 54 do not impact the actual time from which HMRC are to be regarded as bound by the Settlement Agreement. As we have described, s 54 does not determine that date; it merely provides for certain consequences of the making of an agreement and the time at which those consequences have effect. Section 54 does not empower HMRC to enter into agreements. We agree with Mr Gammie that HMRC have a general power under s 5 CRCA to enter into agreements and, without more, will be bound by those agreements notwithstanding that s 54 might not apply to particular years of assessment, or might have effect from a different date to the date of the actual agreement.

267. It follows therefore that we conclude that, although s 54 has effect only in relation to 2001/02, the Settlement Agreement was, subject to arguments whether it was a forward tax agreement in certain respects, or was subject to rescission on the ground of material non-disclosure, binding on both Mr Curran and HMRC in relation to 2002/03 and succeeding years in relation to the 2002 and 2003 transactions.

Application of s 54 to the 2007 transactions

268. Despite Mr Gammie's arguments to the contrary, we do not consider that the Settlement Agreement can apply to the 2007 transactions. Those transactions were not contemplated by the Settlement Agreement and are clearly outside its terms. Although Mr Gammie raised public law arguments in this respect in his skeleton argument, these were not developed by either party in oral submissions. In light of the fact that there are parallel judicial review proceedings, and our own decision on the Interest issue renders the question otiose, we do not consider that we should address those arguments at this stage.

B. Was the Settlement Agreement *ultra vires* as a forward tax agreement?

269. HMRC did not argue that the whole of the Settlement Agreement was *ultra vires* as a forward tax agreement. They confined their submission in this respect to clause 6 of the agreement, which dealt with the deemed payments in years after the making of the 2002 and 2003 Payments. In support of HMRC's submission that clause 6 comprises a forward tax agreement and that HMRC could not bind themselves to grant ongoing interest relief in the terms of clause 6 of the Side Letter, Mr Fisher referred us to the *Al Fayed* case.

270. In that case Mr Al Fayed and his brothers (the petitioners) were not domiciled in the UK, and so were liable to UK tax on foreign source income only on the remittance basis. They would not be subject to UK tax on remittances that originated in a fund consisting exclusively of capital and which therefore did not constitute income or capital gains. To avoid a time-consuming and expensive investigation to determine whether remittances originated from a capital fund, in 1997 the Revenue entered into a forward tax agreement with the petitioners under which the petitioners agreed to pay specified annual sums in respect of specified future years of assessment, and the Revenue agreed to accept those sums in lieu of any income tax and capital gains tax to which the petitioners might otherwise have been liable.

271. The Court of Session held that the Revenue had a managerial discretion, and there were circumstances in which they had power to enter into an agreement with the taxpayer for the payment of a sum of money in respect of the taxpayer's liability, even where it might be said that they had foregone the collection of some part of the total amount of tax which was due. They could properly take into account the extent of the information which was likely to be obtainable, and the difficulty involved in identifying the extent of the exact sum which is due. Nevertheless, under taxation legislation the Revenue had the duty of collecting tax as it fell due in respect of actual transactions. The Revenue had no power to require a taxpayer to accept an advance assessment of his liability to tax in a future year or years. Likewise they had no power to contract with the taxpayer as to his future liability. Accordingly the Revenue had no power to enter into a forward tax agreement.

272. It is clear that, if clause 6 of the agreement is *ultra vires* on this account, it cannot be maintained as a matter of discretion on the part of the Revenue. Nor is termination of the agreement unfair so as to amount to an abuse of power. The question is whether the Settlement Agreement, to the extent of clause 6, is a forward tax agreement that is *ultra vires*.

273. Mr Fisher referred us to the judgment of the Lord President (Lord Cullen), and in particular to [74], where he said:

> "… even if the sum to be paid under an agreement between the respondents and the taxpayer was a reasonable estimate of the taxpayers' liability at the outset of the period covered by the agreement, it could not be taken as a measure of that liability throughout the period. The amount of the taxable remittances could readily vary, and it would no doubt be attractive to the taxpayer to maximise such

> remittances since he would know that the amount to be paid by him remained fixed for the period covered by the agreement. It is also possible that the tax regime would be subject to variation at some time within that period. In these circumstances we accept the respondents' argument that such an agreement would involve a failure on the part of the respondents to exercise their managerial discretion, in the words of the Master of the Rolls in *R* (*on the application of Wilkinson*) *v IRC* [2003] EWCA Civ 814, [2003] STC 1113 at para 45, to which we have referred earlier, 'as to the best manner of obtaining for the national exchequer the highest net return that is practicable'. We do not consider that they could exercise their power under s 9A of the 1970 Act to investigate the actual liability of the taxpayer in respect of such remittances, because they had disabled themselves from doing so by entering into the Agreement."

274. Mr Fisher argues that clause 6 of the Settlement Agreement is a forward tax agreement and is thus *ultra vires*. He says that clause 6 creates a fiction that loan interest continues to accrue and be paid by Mr Curran on the 2002 and 2003 Loans year on year, notwithstanding that the interest obligations under the 2002 and 2003 Loan Agreements have been extinguished. It is argued that the terms of the Settlement Agreement would mean that HMRC would be bound to accept a fictional deduction from Mr Curran's income over (potentially) the whole period of the Loans.

275. Mr Gammie, on the other hand, submits that the Settlement Agreement did not seek to estimate and set in advance amounts of relief that may or may not have arisen. Instead the Settlement Agreement merely agreed to settle the amount of tax relief that arose in the years in question, and it was agreed that 50% of that relief would be deferred until fixed dates in the future.

276. Mr Gammie also referred us to the judgment of the Lord President in *Al Fayed*, at [76]:

> "A back tax agreement relates to a situation in which the taxpayer has already incurred the tax liability, but its amount has not been determined. Fundamental to the legality of such an agreement is that the respondents have the power to require the taxpayer to pay what is due. As an alternative means to the same end they are regarded as having the power, in the exercise of their managerial discretion, to enter into a contract with the taxpayer for a payment in satisfaction of that liability. In that context they have power to arrange a compromise with the taxpayer, taking into account such factors as may be relevant. The fact that such an agreement is within the powers of the respondents cannot confer on them a power to enter into a forward tax agreement which otherwise would be *ultra vires*. Combining the two agreements in a single document, or agreeing that one is to form a consideration in respect of the other, makes no difference."

277. In our view clause 6 of the Settlement Agreement is not a forward tax agreement that is *ultra vires*. In contrast to the position in *Al Fayed*, clause 6 did not amount to an advance assessment of liability (or relief) for the years in question. The availability of the relief was determined by actual transactions that had already taken

place for the years of assessment under enquiry. What clause 6 amounted to was a mechanism for compromising Mr Curran's tax affairs in relation to the 2002 and 2003 Payments. The fact that the compromise involved spreading relief forward, including on a basis that eliminated the discount element of the Payments, does not bring this agreement into the realms of a forward tax agreement that can be *ultra vires*. Whilst agreements for future years based on notional sums which do not relate to actual transactions will be *ultra vires*, that does not apply to agreements compromising actual liabilities or claims for relief. The compromise of an existing liability or claim for relief is clearly within the powers of HMRC. It is not taken outside those powers merely because it is given effect by being expressed in terms of notional payments (or receipts) in future years. It is the substance of the agreement that is material for this purpose, and not its form.

C. Was the Settlement Agreement voidable for material non-disclosure?

278. We have so far found that the Settlement Agreement was binding with effect from 7 December 2005, and that no part of it was *ultra vires*. HMRC nevertheless submit that the Settlement Agreement is voidable in its entirety as a result of Mr Curran's material non-disclosure.

279. This highlights the importance of the finding as to the date of the Settlement Agreement having been reached. On the basis of our finding, HMRC's arguments as to non-disclosure are confined to the 2005 Restructuring, which it is agreed was not disclosed to HMRC before the date on which we have found the Settlement Agreement took effect. Were we to have accepted HMRC's argument that the Settlement Agreement was formally concluded only on 1 November 2007, the relevant undisclosed material would also have included the fact of the disposal by Mr Curran of the 2002 and 2003 Notes.

280. It is clear that the provision of misleading information, albeit honestly, by a taxpayer may vitiate an agreement otherwise made between the taxpayer and HMRC: *Scorer v Olin Energy Systems Ltd* [1984] STC 141 (CA) per Fox LJ at p 150; see also *Gray v Matheson* [1993] STC 178 per Vinelott J at pp 186-187. That does not mean that the provision of any erroneous information (or any omission to provide information) will be sufficient to make an agreement voidable. The information, or the failure to provide it, must be misleading. To be misleading, the information provided, or the information which has not been provided, must, viewed objectively, have a material impact on the decision of HMRC to enter into the agreement.

281. We shall consider first the issue of non-disclosure on the basis of our own finding as to the effective date of the Settlement Agreement. We shall then consider the alternative proposition on the assumption that HMRC's argument on the timing of the Settlement Agreement had prevailed.

Non-disclosure of 2005 Restructuring

282. There is of course no dispute that the Settlement Agreement was made on the basis of full and complete disclosure of all relevant facts (clause 1 of the Settlement

Agreement). The dispute is whether the facts that were not disclosed at the material time were "relevant facts", whether the facts that were not disclosed would, viewed objectively, have had had a material impact on the decision of HMRC to proceed with the Settlement Agreement and consequently whether the failure to disclose those facts renders the Settlement Agreement voidable.

283. Mr Fisher referred us back to the letter from Herbert Smith to HMRC of 17 October 2005. He argued that the reference in that letter to "Mr Curran agreed to grant security by way of a Deed of Charge granting a fixed charge to Tailored Loans over the Loan Note" misrepresented (through no fault of Herbert Smith) the true position, namely that the Deeds of Charge over the 2002 and 2003 Notes had in fact been released.

284. We have considered the evidence in relation to these omissions, and have concluded that, if Herbert Smith had known of the 2005 Restructuring at the time of their letter, they might well have referred to it, if only to dismiss it as having no relevance to the availability of relief in the tax years in question. But that does not make the fact of the 2005 Restructuring relevant for this purpose; indeed it only serves to emphasise its irrelevance in the context of Herbert Smith's letter. The purpose of that letter was to set out the technical arguments for the claims for interest relief in respect of the 2002 and 2003 Payments. The 2005 Restructuring, in that context, was not relevant to the question whether the statutory conditions applied.

285. Herbert Smith's technical analysis was accompanied by a separate without prejudice letter suggesting that discussions be held with a view to a negotiated settlement. We therefore have to consider whether the failure to disclose the 2005 Restructuring can be regarded as a material non-disclosure in relation to the formation of the Settlement Agreement.

286. On the evidence before us, the only stipulation made by HMRC when agreeing the settlement terms was that the 2002 and 2003 Loans were to remain outstanding. We have found that the issue of the 2002 and 2003 Notes being retained was not raised by Ms Feighan. So there is no evidence that HMRC made clear to Mr Curran that reliance would be placed on the continued existence of the Deeds of Charge, and the security over the 2002 and 2003 Notes. Can such reliance otherwise be inferred? We do not consider that it can. HMRC's case appears to be based upon an assumption that if the Notes were disposed of that would give rise to a requirement on the part of Mr Curran to repay the Loans, and the Settlement Agreement would then cease to apply. But if that were the case, then this was simply a misunderstanding by HMRC of the true legal position, namely that the Loans would not fall to be repaid unless on the disposal of the Notes, those Notes had been subject to the Deeds of Charge.

287. In our view such reliance by HMRC was unreasonable in the circumstances of the settlement. As that settlement had been predicated on HMRC's own insistence that the Loans remain outstanding, and should not be repaid, it would not be reasonable for HMRC to have expected disclosure of something that went to secure that aim, rather than prejudice it. This conclusion is unaffected, despite Ms

McCarthy's submissions in this respect, by whether or not Mr Curran himself intended to retain the Notes throughout the terms of the Loans. Mr Curran could reasonably have assumed that the 2005 Restructuring was not relevant as at no time had it been suggested that HMRC were relying on the maintenance of the Deeds of Charge, or on the Loans actually being repaid if the Notes were disposed of.

288. We conclude on this basis that, viewed objectively, disclosure of the fact of the 2005 Restructuring would not have led HMRC not to enter into the Settlement Agreement. The only stipulation was that the 2002 and 2003 Loans would not be repaid. Compliance with that requirement was reinforced by the release of the Deeds of Charge over the 2002 and 2003 Notes, thus making it less likely that the sole condition specified by HMRC would be breached.

289. This is a case, in our view, in which HMRC wish to resile from the Settlement Agreement, not because they would not have entered into it had they known of the 2005 Restructuring, but because they perceive now, with hindsight, that they ought to have made the agreement conditional on the Notes not being disposed of. In considering the precursor to s 54 TMA, Fox LJ in *Scorer v Olin* said (at p 150), in a passage approved in the House of Lords [1985] STC 218:

> "… The section is dealing with agreements as to how an assessment shall be dealt with. It is not dealing with the formulation of points of law. We do not know why the inspector agreed the computation. He may have made an error of law or he may have misunderstood the facts or he may have failed to think about the matter at all. Subject to the question, which I mention later, as to whether the taxpayer has provided misleading information, I do not see why the circumstances that the inspector has made a mistake either of law or fact should take the case outside s 510. Essentially, the question is not why he agreed but whether he agreed. The purpose of the section must be to protect the taxpayer by producing finality, and Parliament, I would suppose, must have contemplated that the taxpayer would be protected, even though the inspector made some error in his view of the facts or the law. That is a likely, if not the most likely, event in which the question of going back on the agreement would ever arise at all."

In our view, if HMRC were of the view that the existence of the Deeds of Charge over the 2002 and 2003 Notes somehow afforded them protection in that disposals of the Notes would result in the repayment of the 2002 and 2003 Loans, that was an error of the nature described by Lord Justice Fox. It was not induced by a non-disclosure of the 2005 Restructuring. It was a belief that was never articulated in discussions with Mr Curran or his advisers, and was accordingly so obscure that Mr Curran or his advisers could not reasonably have been expected to regard it as material to HMRC's decision to enter into the Settlement Agreement.

290. Ms McCarthy argued that Ms Feighan had read the relevant documentation and had said in her evidence that it appeared to her that if the Notes were disposed of by any means then Mr Curran would have had to repay the Loans. She submitted that in this way the operation of the Deeds of Charge and the corresponding provision in the Loan Agreements, was to mimic the effect of s 363 ICTA (return of capital). If that

was Ms Feighan's understanding at the time of the Settlement Meeting and beyond, and that as a result she took the view that it was not necessary for any condition to be included in the Settlement Agreement in that respect, then Ms Feighan was simply mistaken. That error might have been appreciated by Ms Feighan had she been informed of the release of the charges over the Notes, but it should equally have been understood from a reading of the plain terms of the 2002 and 2003 Loan Agreements. It cannot therefore be said that HMRC reasonably relied upon the existence of the charges. Such reliance was based on a flawed understanding of the meaning and effect of the Loan Agreements.

291. For these reasons, in our view, the Settlement Agreement was not voidable for non-disclosure.

Non-disclosure of the disposal of the 2002 and 2003 Notes

292. If HMRC were to have been right that the Settlement Agreement was not entered into until 1 November 2007, the question would arise whether the non-disclosure of Mr Curran's disposal of the 2002 and 2003 Notes in April 2006 rendered the Settlement Agreement voidable.

293. The same principles apply to this non-disclosure as applied to the non-disclosure of the 2005 Restructuring. The circumstances of the formal written acceptance must also be taken into account. At that stage this was presented as a "low key" administrative operation, which did not have attached to it any suggestion that HMRC were relying on everything remaining exactly as had been the case at the time of the Letter of Offer. That is unsurprising, as HMRC had already been operating the settlement for a number of years, and had included the material concern over retention of the Loans as a condition in the Side Letter, but had said nothing about any requirement that Mr Curran retain the Notes.

294. In our view, there is no evidence on which it may be objectively concluded that HMRC placed any reliance on the status quo being maintained in relation to the Notes. There had, according to our findings, been no indication at any stage by HMRC that the retention of the Notes by Mr Curran was a material factor, or that disposal of the Notes would lead HMRC to refuse to enter into the Settlement Agreement. Accordingly the failure in November 2007 to disclose the disposal of the Notes was not misleading so as to render the Settlement Agreement voidable.

D. Clause 6 of the Settlement Agreement

295. We have found that the Settlement Agreement is valid, and was not capable of being avoided by HMRC for material non-disclosure. We have also found that clause 6 of the Settlement Agreement is not ultra vires as a forward tax agreement. In that event, say HMRC, the conditions of clause 6 ceased to be satisfied on the disposal of the 2002 and 2003 Notes.

296. This proposition is founded upon the effect of s 363 which, in an ordinary case, would preclude interest relief to the extent that capital would be treated as having

been recovered on an assignment of a debt. The argument is that clause 6 should be construed so as to treat a notional payment for the years in question as eligible for relief only to the extent that the statutory conditions continue to apply in that period. Mr Gammie submits that clause 6 has the effect that, provided the 2002 and 2003 Loans are not repaid, Mr Curran is entitled to the interest relief provided for by clause 6 irrespective of whether the statutory conditions continue to be satisfied. On this basis, the relief applies notwithstanding the intervening disposal of the 2002 and 2003 Notes.

297. This, it seems to us, is a pure question of construction of the Settlement Agreement. We set it out earlier, but it is convenient to repeat the terms of clause 6:

> 6. The remaining sums in respect of both loans are to be treated as if half of the loan interest due on each loan were accrued and paid by me over the remaining span of both of the loans. Specifically;
>
> (a) The £1,000,000 loan will give rise to qualifying interest for each year until the end of the period of the loan (30 years) of £40,000 per annum. In the final year, 2031/2032 that figure will be £35,288.
>
> (b) The £850,000 loan will give rise to qualifying interest for each year until the end of the period of the loan (30 years) of £32,938 per annum. In the final year 2032/2033 that figure will be £27,975.
>
> (c) To the extent that the qualifying interest is not set against income and gains in the year it is accrued and deemed to arise in (a) and (b) above, it may be carried forward indefinitely and set against income and gains in any subsequent year.

298. It can be seen that this is a deeming provision. It had to be, as the 2002 and 2003 Payments had been made, and no actual payments of interest would be made in succeeding years. But there is not one deeming effect, but two. The first is to deem the interest payments to have been made according to the terms of the Loans over their remaining terms. If that had been the only deeming effect, we could have seen the force of HMRC's arguments. But it was not. Clause 6 goes on specifically to provide that the Loans will give rise to "qualifying interest" for each year until the end of the periods of the Loans. That clarifies the extent of the deeming provision, and we consider it is fatal to the construction that HMRC advanced.

299. Although the expression "qualifying interest" is not used in the relevant statutory provisions, we consider it is employed in this context to mean " interest … eligible for relief" under s 353 ICTA. There is no other possible meaning in this context. The background to the spreading of relief was the actual payments of (disputed) interest by virtue of the 2002 and 2003 Payments. The purpose of the Settlement Agreement was to give relief for those payments, but not all in the years of payment. Relief in respect of 50% of the Payments was postponed, to be given effect in subsequent years while the 2002 and 2003 Loans were outstanding. That analysis is not affected by the fact that the discount that had otherwise been applied to the calculation of the amount that Mr Curran paid in the form of the 2002 and 2003 Payments. That did not have the effect of simply treating the relevant amounts as having been paid as interest under the original Loans. The Settlement Agreement

could have had that effect, but according to its own terms it did not. Instead it made clear that the deemed payments were to be treated as payments of qualifying interest, or as interest eligible for relief. Since interest eligible for relief can only be interest that satisfies all the conditions for relief, the effect of clause 6 is to assume, whether or not it be the case, that the conditions are met.

300. In our view this is confirmed by the specific requirement in clause 3 of the Settlement Agreement that Mr Curran should not repay either of the 2002 or 2003 Loans prior to their respective repayment dates. If HMRC's construction of clause 6 were correct, such a provision would not have been necessary; on the repayment of the Loans the necessary condition, in s 360, that the interest be "on a Loan" would cease to have been satisfied, and relief would have come to an end on the terms of clause 6 itself. Furthermore, in light of the information requirements imposed on Mr Curran in the event of an early repayment of either Loan, it is difficult to understand, if HMRC's construction were to be the right one, why Mr Curran was not specifically required to notify HMRC if any of the statutory conditions had ceased to be satisfied.

301. The answer, in our view, is that, as we have found, HMRC's construction is not the correct one. Clause 6 provides for the treatment of the sums referred to as interest eligible for relief under s 363, and deems all the relevant conditions for such eligibility to be satisfied.

Discovery assessments

302. In Mr Curran's grounds of appeal he challenged the discovery assessments made by HMRC on the basis that those assessments did not satisfy the requirements of s 29 TMA. This challenge was not developed in Mr Gammie's skeleton argument, nor was it referred to in the skeleton argument of Mr Fisher and Ms McCarthy. We heard no substantive argument on the issue at the hearing. Although each party helpfully provided us with written submissions, we have decided, in light of our decisions on other matters in this appeal, that it would not be appropriate, on the basis of the written submissions alone, for us to come to any view on this question.

Summary of conclusions

303. In summary, we have concluded, firstly, in relation to interest:

(1) The 2002, 2003 and 2007 Payments were payments of interest.

(2) Those Payments were not at a rate in excess of a commercial rate.

(3) Interest relief in respect of those Payments is not prevented from being given by s 787 ICTA.

304. Accordingly we find that the 2002, 2003 and 2007 Payments were of interest eligible for relief, in the respective years of assessment in which those Payments were made, under s 353 ICTA.

305. Secondly, in relation to the Settlement Agreement:

(1) The Settlement Agreement was a binding agreement from 7 December 2005.

(2) Section 54 TMA applies in relation to the Settlement Agreement only in respect of the tax year 2001/02. Section 54 has effect in that respect from 1 November 2007, the date of the notice of confirmation under s 54(3).

(3) The Settlement Agreement was nevertheless binding on both Mr Curran and HMRC from the date of the contractual agreement, namely 7 December 2005, the first date on which HMRC made a payment to Mr Curran in performance of the agreement.

(4) The Settlement Agreement, or clause 6 of the Settlement Agreement, was not ultra vires, or thereby invalidated, by being a forward tax agreement.

(5) There was no material non-disclosure by Mr Curran such as to render the Settlement Agreement voidable. This is the case whether, as we found, the Settlement Agreement was made on 7 December 2005, or as HMRC contended, on 1 November 2007.

(6) Clause 6 of the Settlement Agreement should be construed so that Mr Curran is treated as having paid interest eligible for relief under s 353 ICTA in the stated amounts, irrespective of whether or not the statutory conditions continue to apply.

Decision

306. We allow the appeals.

307. We understand that there is no dispute on the figures. However, if any further determination is required as a consequence of our conclusions, the parties are at liberty to apply.

Costs

308. Any application for costs must be made within 28 days after the date of release of this decision. As any direction as to costs will be for detailed assessment, it will not be necessary for the application to be accompanied by a schedule of costs.

Application for permission to appeal

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.

5

ROGER BERNER
TRIBUNAL JUDGE

RELEASE DATE: 14 August 2012

10