



Appeal numbers: UT/2019/0089
UT/2019/0101

CORPORATION TAX – whether the UK legislation in relation to intra-group disposals is compliant with EU law – the applicable freedoms, whether or not the provisions in question restrict a freedom – whether or not any restriction can be justified – proportionality of restrictions – conforming interpretation and disapplication – consideration of movements of capital – whether to refer questions of EU law to the Court of Justice of the European Union

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

GALLAHER LIMITED

Appellant
(UT/2019/0101)
Respondent
(UT/2019/0089)

-and-

THE COMMISSIONERS FOR HER MAJESTY'S
REVENUE AND CUSTOMS

Respondents
(UT/2019/0101)
Appellants
(UT/2019/0089)

TRIBUNAL

MR JUSTICE MILES
JUDGE ASHLEY GREENBANK

Sitting in public by way of remote video hearing, treated as taking place in London, on 26, 27 and 28 October 2020

Philip Baker QC and Mr Imran Afzal, instructed by Freshfields Bruckhaus Deringer LLP, for Gallaher Limited

Rupert Baldry QC and Mr Ben Elliott, instructed by the General Counsel and Solicitor to HM Revenue & Customs, for the Commissioners for Her Majesty's Revenue and Customs

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DECISION

Introduction

1. This decision notice relates to appeals from the decision of the First-tier Tribunal (Judge Tony Beare) (the “FTT”) dated 25 March 2019.
2. The FTT decision concerned appeals made by Gallaher Limited (“Gallaher”) against two partial closure notices issued by Her Majesty’s Revenue and Customs (“HMRC”): the first, in relation to Gallaher’s return for the accounting period ended 31 December 2011 (the “2011 Appeal”); and the second, in relation to Gallaher’s return for the accounting period ended 31 December 2014 (the “2014 Appeal”).
3. The 2011 Appeal related to the conclusion in the partial closure notice that Gallaher was liable to pay corporation tax on gains arising on the transfer of certain intellectual property rights relating to tobacco brands (the “Brands”) and related assets to JT International SA (“JTISA”). JTISA was at the time, and remains, a company which is a member of the same group as Gallaher and was, and remains, resident in Geneva, Switzerland for tax purposes. We have referred to the transfer of the Brands and related assets by Gallaher to JTISA as the “2011 Disposal” in this decision notice.
4. The 2014 Appeal related to the conclusion in the partial closure notice that Gallaher was liable to pay corporation tax on gains arising on the transfer of shares in its subsidiary company, Galleon Insurance Company Limited (“Galleon”), to JT International Holding BV (“JTIH”). JTIH was at the time, and remains, the indirect parent company of Gallaher and was, and remains, resident in the Netherlands for tax purposes. We have referred to the transfer of shares in Galleon by Gallaher to JTIH as the “2014 Disposal” in this decision notice.
5. Before the FTT, Gallaher asserted: that the imposition of an immediate tax charge on gains arising from each of the 2011 Disposal and the 2014 Disposal was contrary to European Union (“EU”) law; and that the provisions of UK law, which govern the taxation of transfers of assets between companies, which are members of the same group, should be applied to the 2011 Disposal and the 2014 Disposal, in a manner consistent with EU law, to defer any tax charge which would otherwise arise on them.
6. We have set out a summary of the FTT decision at [28]-[32] below, but, in short, the FTT decided:
 - (1) that the imposition of an immediate tax charge in relation to the 2011 Disposal was not contrary to EU law;
 - (2) that the imposition of an immediate tax charge in relation to the 2014 Disposal was contrary to EU law, but that the relevant provisions of UK domestic legislation could not be interpreted in a manner which was consistent with EU law and that the FTT had therefore to disapply the legislation in a manner which removed the tax charge entirely.

7. With the consent of the FTT, Gallaher appeals to this Tribunal against the FTT's decision in relation to the 2011 Disposal (reference UT/2019/0101) and HMRC appeals to this Tribunal against the FTT's decision in relation to the 2014 Disposal (reference UT/2019/0089).

The relevant legislation

8. It will assist our explanation if we first set out the provisions of UK tax legislation, which are relevant in this case, and the provisions of EU law which Gallaher asserts those provisions of UK tax legislation contravene.

Relevant provisions of UK tax law

9. The relevant provisions of UK domestic legislation which apply to transfers of capital assets between two companies, which are members of the same group, are found in s171 of the Taxation of Chargeable Gains Act 1992 ("TCGA"), and the equivalent provisions, which apply to the intragroup transfer of certain intangible assets, are found in s775 and s776 of the Corporation Tax Act 2009 ("CTA 2009"). In its decision, the FTT referred to s171 TCGA, and s775 and s776 CTA 2009 together as the "Group Transfer Rules" and we have adopted the same terminology in this decision notice.

10. Section 171 TCGA applies to the transfer of chargeable assets between group companies for the purposes of corporation tax on chargeable gains. At all material times, and so far as relevant, it was in the following form:

171 Transfers within a group: general provisions

(1) Where—

(a) a company ("company A") disposes of an asset to another company ("company B") at a time when both companies are members of the same group, and

(b) the conditions in subsection (1A) below are met,

company A and company B are treated for the purposes of corporation tax on chargeable gains as if the asset were acquired by company B for a consideration of such amount as would secure that neither a gain nor a loss would accrue to company A on the disposal.

(1A) The conditions referred to in subsection (1)(b) above are—

(a) that company A is resident in the United Kingdom at the time of the disposal, or the asset is a chargeable asset in relation to that company immediately before that time, and

(b) that company B is resident in the United Kingdom at the time of the disposal, or the asset is a chargeable asset in relation to that company immediately after that time.

For this purpose an asset is a "chargeable asset" in relation to a company at any time if, were the asset to be disposed of by the company at that time, any gain accruing to the company would be a chargeable gain and would by virtue of section 10B form part of its chargeable profits for corporation tax purposes.

(2) ...

11. As the FTT noted in its decision (FTT [30]), where s171 applies, no charge to corporation tax on chargeable gains arises when one company transfers assets to another company which is a member of the same group. This is because the disposal is treated as taking place for such consideration as gives rise to neither a gain nor a loss. However, in some circumstances, a tax charge may arise in the future if the transferee company disposes of the assets or if the transferee company ceases to be a member of the group within six years of the transfer of the assets to it.

12. The definition of a “group” for these purposes is contained in s170 TCGA. However, it is common ground between the parties that each of JTIH, JTISA and Gallaher were members of the same group, of which Japan Tobacco Inc. (“JT”) was the parent company, or, as is referred to in s170 TCGA, the “principal company” of the group for these purposes at all material times.

13. Section 775 CTA 2009 and s776 CTA 2009 apply to the transfer of certain intangible fixed assets between group companies for corporation tax purposes. At all material times, and so far as relevant, they were in the following form:

775 Transfers within a group

(1) A transfer of an intangible fixed asset from one company (“the transferor”) to another company (“the transferee”) is tax-neutral for the purposes of this Part if—

- (a) at the time of the transfer both companies are members of the same group,
- (b) immediately before the transfer the asset is a chargeable intangible asset in relation to the transferor, and
- (c) immediately after the transfer the asset is a chargeable intangible asset in relation to the transferee.

(2) For the consequences of a transfer being tax-neutral for the purposes of this Part, see section 776.

...

776 Meaning of “tax-neutral” transfer

(1) This section sets out the consequences of a transfer of an asset being “tax-neutral” for the purposes of this Part.

(2) The transfer is treated for those purposes as not involving—

- (a) any realisation of the asset by the transferor, or
- (b) any acquisition of the asset by the transferee.

(3) The transferee is treated for those purposes—

- (a) as having held the asset at all times when it was held by the transferor, and
 - (b) as having done all such things in relation to the asset as were done by the transferor.
- (4) In particular—
- (a) the original cost of the asset in the hands of the transferor is treated as the original cost in the hands of the transferee, and
 - (b) all such credits and debits in relation to the asset as have been brought into account for tax purposes by the transferor under this Part are treated as if they had been brought into account by the transferee.
- (5) The references in subsection (4)(a) to the cost of the asset are to the cost recognised for tax purposes.

14. As the FTT also noted in its decision (FTT [30]), where s775 and s776 apply, no charge to corporation tax arises when one company transfers intangible fixed assets to another company which is a member of the same group. The legislation achieves this result by treating the transferee company as having held the relevant assets at all times when the relevant assets were held by the transferor company and as having done all things in relation to the relevant assets that were done by the transferor company. In certain circumstances, a tax charge may arise in the future, if the transferee company disposes of the assets or if the transferee company ceases to be a member of the group within six years of the transfer of the assets to it.

15. The definition of a “group” for these purposes is contained in s764 to s767 CTA 2009. It is in similar terms to the definition of a group for the purposes of corporation tax on chargeable gains. As we have mentioned above, it is common ground between the parties that each of JTIH, JTISA and Gallaher were members of the same group for these purposes at all material times.

16. Although the mechanism by which it is achieved is slightly different, the effect of both sets of rules is to defer the tax charge on the accrued gain until a later disposal or realization of the relevant assets or, in some circumstances, if the transferee company leaves the group. In both cases, the key condition for this treatment is that the relevant assets remain within the scope of UK corporation tax (s171(1A) TCGA and s775(1) CTA 2009). This will occur if either the transferee company is resident in the UK for tax purposes or if the transferee company is not resident in the UK for tax purposes but is carrying on a trade in the UK through a permanent establishment and the assets are held by the transferee company for the purposes of that trade or permanent establishment. It is the application of this condition to the 2011 Disposal and the 2014 Disposal which, Gallaher asserts, is contrary to EU law.

Relevant provisions of EU law

17. The main provisions of EU law for our purposes are Article 49 of the Treaty on the Functioning of the European Union (“TFEU”), which provides for freedom of

establishment, and Articles 63 to 65 TFEU, which provide for freedom of movement of capital.

18. Article 49 TFEU provides as follows:

Article 49

Within the framework of the provisions set out below, restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State.

Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the Chapter relating to capital.

19. Article 54 TFEU confirms that companies which have their registered office, central administration or principal place of business in the EU can take advantage of the freedom of establishment under Article 49 in the same way as natural persons.

20. Articles 63 to 65 TFEU provide as follows:

Article 63

1. Within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.

2. Within the framework of the provisions set out in this Chapter, all restrictions on payments between Member States and between Member States and third countries shall be prohibited.

Article 64

1. The provisions of Article 63 shall be without prejudice to the application to third countries of any restrictions which exist on 31 December 1993 under national or Union law adopted in respect of the movement of capital to or from third countries involving direct investment — including in real estate — establishment, the provision of financial services or the admission of securities to capital markets...

Article 65

1. The provisions of Article 63 shall be without prejudice to the right of Member States:

a. to apply the relevant provisions of their tax law which distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where their capital is invested; ...

2. ...

3. The measures and procedures referred to in paragraphs 1 and 2 shall not constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital and payments as defined in Article 63.

21. As identified by the FTT (FTT [37]), Council Directive 88/361/EEC, which required Member States to abolish restrictions on movements of capital, contained, at Annex 1 to that Directive, a “nomenclature” (the “Nomenclature”) classifying various capital movements in order to “facilitate the application of [the] Directive”. The Directive was made under Article 67 of the Treaty establishing the European Community, which was repealed by the Treaty of Amsterdam. However, the Nomenclature “retains the same indicative value, for the purposes of defining the term ‘movement of capital’ as it did before [the entry into force of Article 63 of the TFEU], subject to the qualification, contained in the introduction to the nomenclature, that the list set out therein is not exhaustive” (*Test Claimants in the FII Group Litigation v Inland Revenue Commissioners* (Case C-446/04) at [179]).

22. The various EU treaties were incorporated into and given effect in UK domestic law by the European Communities Act 1972 (“ECA”). Section 2(1) ECA provided as follows:

(1) All such rights, powers, liabilities, obligations and restrictions from time to time created or arising by or under the Treaties, and all such remedies and procedures from time to time provided for by or under the Treaties, as in accordance with the Treaties are without further enactment to be given legal effect or used in the United Kingdom shall be recognised and available in law, and be enforced, allowed and followed accordingly; and the expression “enforceable EU right” and similar expressions shall be read as referring to one to which this subsection applies.

23. As part of the arrangements for the withdrawal of the UK from the EU, the ECA is repealed by the European Union (Withdrawal) Act 2018 (“EUWA 2018”) with effect from 31 January 2020. However, the effect of s2 ECA (and other provisions of the ECA) is preserved, to some extent, until the end of the transition period on 31 December 2020. We refer to other provisions of the EUWA 2018 later in this decision notice, but it is not relevant to the discussion of the substantive issues in these appeals.

The relevant facts

24. The parties provided statements of agreed facts and issues for the 2011 Appeal and the 2014 Appeal. We have set them out in the paragraphs below with some amendments to reflect the defined terms that we have used in this decision notice.

The 2011 Disposal

25. The parties have agreed that the facts in relation to the 2011 Disposal are as follows:

(a) Gallaher is a UK resident company and is a member of the JT group of companies (the “JT Group”). JT is a publicly-listed company resident in Japan. The JT Group is a global tobacco group and distributes products in 130 countries

worldwide. Gallaher and JT were incorporated in, respectively, England & Wales and Japan;

(b) Gallaher became a member of the JT Group in 2007 when the shares in its UK resident parent company, Gallaher Group Limited (which at the time was called Gallaher Group Plc) (“GGL”), were acquired by a JT Group UK resident company called JTI (UK) Management Limited (“JTIUM”);

(c) JTIUM is owned by JTIH, a company resident in the Netherlands. JTIH also owns the entire shareholding in JTISA, a company resident in Geneva, Switzerland. Neither JTIH nor JTISA has a permanent establishment within the UK and neither is within the charge to UK corporation tax;

(d) following a restructuring that took place in 2009 and 2010, Benson & Hedges Limited (“B&HL”) became Gallaher’s immediate parent company. In turn, Gallaher Overseas (Holdings) Limited (“GOHL”) became the immediate parent of B&H Limited;

(e) thus, Gallaher is an indirect wholly-owned UK resident subsidiary of JTIH, which holds its interest in Gallaher through its wholly-owned UK resident subsidiaries JTIUM, GGL, GOHL and B&HL, whilst JTISA is a direct wholly-owned Swiss resident subsidiary of JTIH;

(f) JTISA has been based in Geneva since its incorporation in 1999;

(g) the 2011 Disposal involved the sale by Gallaher of the Brands and related assets to JTISA on 1 January 2011;

(h) all the Brands continue to be owned by JTISA;

(i) the consideration received by Gallaher for the 2011 Disposal was £2,410,316,000 (the “Consideration”). In respect of the Consideration, on 4 January 2011:

(i) JTIH made inter-company loans totalling the amount of the Consideration to JTISA;

(ii) JTISA paid the Consideration to Gallaher;

(iii) Gallaher paid a dividend for the amount of the Consideration to B&HL, and equivalent dividends for the amount of the Consideration were paid, sequentially, by B&HL to GOHL, by GOHL to GGL and by GGL to JTIUM; and

(iv) JTIUM paid a dividend in the amount of £1,260,090,000 to JTIH and, separately, repaid the balance of a £1,150,226,000 outstanding inter-company loan to JTIH;

(j) in consequence of the 2011 Disposal, JTISA acquired legal title to the Brands and related assets;

(k) as a consequence of the 2011 Disposal and contemporaneous contractual arrangements agreed between Gallaher and JTISA, Gallaher's role in relation to the Brands was to act as:

(i) a manufacturer in respect of the Brands; and

(ii) a limited risk distributor of the products bearing the Brands in the UK;
and

(l) following the 2011 Disposal, Gallaher continued to own the Mayfair brand rights (worldwide rights) and the rights to use certain other brands in Ireland and eastern Europe.

The 2014 Disposal

26. The parties have agreed that the facts in relation to the 2014 Disposal are as follows:

(a) Gallaher is a UK resident company and is a member of the JT Group. JT is a publicly-listed company resident in Japan. The JT Group is a global tobacco group and distributes products in 130 countries worldwide. Gallaher and JT were incorporated in, respectively, England and Wales and Japan;

(b) Gallaher became a member of the JT Group in 2007 when the shares in its UK resident parent company, GGL, were acquired by a JT Group UK resident company – that is to say, JTIUM;

(c) JTIUM is owned by JTIH, a company resident in the Netherlands. JTIH does not have a permanent establishment within the UK, nor is it within the charge to UK corporation tax;

(d) following a restructuring that took place in 2009 and 2010, B&HL became Gallaher's immediate parent company. In turn, GOHL became the immediate parent company of B&HL;

(e) thus, Gallaher is an indirect wholly-owned UK resident subsidiary of JTIH, which holds its interest in Gallaher through its wholly-owned UK resident subsidiaries JTIUM, GGL, GOHL and B&HL;

(f) on 16 September 2014, Gallaher sold all of the issued share capital which it held as registered shareholder in one of its subsidiaries, an Isle of Man incorporated company, Galleon, to JTIH;

(g) at the same time, Teofani Limited (“TL”), which held 0.01% of the issued share capital in Galleon as nominee for Gallaher, also sold its shareholding to

JTIH. Gallaher received all the consideration from JTIH in respect of the 2014 Disposal, including in relation to the shares held on its behalf by TL; and

(h) the consideration received by Gallaher for the 2014 Disposal was £2,089,000. The 2014 Disposal gave rise to a chargeable gain before adjustments of £1,551,000.

No tax avoidance motive

27. In addition, having reviewed the witness evidence, which was not challenged by HMRC, the FTT found, as facts, that there were good commercial reasons for each of the 2011 Disposal and the 2014 Disposal, that neither the 2011 Disposal nor the 2014 Disposal formed part of wholly artificial arrangements, which did not reflect economic reality, and that neither the 2011 Disposal nor the 2014 Disposal had the avoidance of tax as its main purpose or one of its main purposes (FTT [9]).

The FTT Decision

28. The FTT summarized the questions before it at paragraph [51] of its decision in the following terms:

“(a) first, which freedoms need to be considered in relation to the application of the Group Transfer Rules to the relevant Disposal? Is it the freedom of establishment set out in Article 49 of the TFEU or the freedom to move capital in Article 63 of the TFEU or both?

(b) secondly, if one or both of the freedoms needs or need to be considered, do the Group Transfer Rules create a restriction on the relevant freedom or freedoms?

(c) thirdly, if the Group Transfer Rules create a restriction on the relevant freedom or freedoms, can that restriction be justified on the basis that the circumstances of the transferee in the particular case are not objectively comparable to those which would have pertained if the transferee had been within the UK tax net?

(d) fourthly, if the Group Transfer Rules create a restriction on the relevant freedom or freedoms and the restriction cannot be justified on the basis of the lack of objective comparability, is the relevant restriction justified by overriding reasons in the public interest – namely, the balanced allocation of taxing powers between Member States?

(e) fifthly, if the relevant restriction on the freedom is justified, is the restriction proportionate – that is to say, does it go beyond what is necessary to achieve the objective of preserving the balanced allocation of taxing powers? and

(f) sixthly, if the relevant restriction on the freedom is not proportionate, how should the UK courts respond to the disproportionate restriction on the freedom which is created by the legislation? In other words, is it possible for the UK courts to adopt a conforming interpretation of any part of the UK legislation in order to achieve compliance with EU law or should some part of the UK legislation be disapplied, whether in whole or in part, in order to achieve that compliance?”

29. There was a further issue which arose in relation to the 2011 Appeal, but not the 2014 Appeal. This was the question of the value of the Brands at the time of the 2011 Disposal. This issue, to which the FTT referred as the “Valuation Issue”, was not before the FTT as it had been agreed that the FTT should address the EU law issues as a preliminary issue (FTT [14])

30. The FTT addressed those issues in turn in a reasoned decision. The decision notice is lengthy, but the FTT provided a summary of its conclusions at paragraph [52].

“52. In view of the length of this decision, a summary of my conclusions in relation to the above questions in relation to each Appeal is as follows:

(a) in relation to the 2014 Appeal:

- the fact that the Disposal gave rise to an immediate liability to tax which would not have arisen if JTIH had been within the UK tax net means that the Group Transfer Rules create a restriction on JTIH's freedom of establishment;

- that restriction is not justified on the basis that JTIH is not in an objectively comparable situation to that in which it would have been if it had been within the UK tax net;

- however, the restriction is justified by reference to overriding reasons in the public interest – namely, the objective of securing the balanced allocation of taxing powers between Member States;

- nevertheless, in requiring the tax in question to be paid immediately, the restriction goes further than is proportionate;

- the restriction would be proportionate if it were to provide for the tax in question to be paid in instalments;

- however, as there are various possible instalment payment bases which would be proportionate in this context, it is not within the competence of the UK courts to remedy the existing disproportionate restriction by selecting one of those options and applying the doctrine of conforming interpretation to treat the selected option as incorporated in the legislation;

- therefore, it is necessary to disapply the existing exclusion from the Group Transfer Rules for intra-group disposals to transferees which are outside the UK tax net in circumstances where that exclusion constitutes a restriction on the freedom of establishment, with the result that Section 171 should apply in those circumstances even though the transferee is not within the UK tax net; and

- in consequence, the EU Law Issue is determined in favour of Gallaher and the 2014 Appeal is upheld; and

(b) in relation to the 2011 Appeal:

- it is not necessary to consider whether the fact that the Disposal gave rise to an immediate liability to tax which would not have arisen if JTISA had been within the UK tax net means that the Group Transfer Rules create a restriction on JTIH's or Gallaher's freedom to move capital;

- however, it is necessary to consider whether that fact means that the Group Transfer Rules create a restriction on JTIH's freedom to establish Gallaher in the UK;
- the fact that the Disposal gave rise to an immediate liability to tax which would not have arisen if JTISA had been within the UK tax net does not mean that the Group Transfer Rules create a restriction on JTIH's freedom of establishment in the UK because the same liability would have arisen even if JTIH had been within the UK tax net; and
- as a result, the EU Law Issue is determined in favour of the Respondents and therefore the Valuation Issue in the 2011 Appeal needs now to be addressed.”

31. The effect of the FTT's conclusions was therefore that Gallaher was liable to an immediate charge to tax on gains arising from the 2011 Disposal, but that Gallaher did not suffer an immediate tax charge on gains arising from the 2014 Disposal. Furthermore, there was no deferred liability on any member of the JT Group either in the form of a potential liability to tax which would arise on a future disposal of the Galleon shares or on any company ceasing to be member of the group whilst owning the shares, or in the form of an obligation to pay tax in instalments.

32. In reaching these conclusions, the FTT took the view that, based on the current status of the case law of the Court of Justice of the European Union (“CJEU”), the application of the relevant provisions of the TFEU in these appeals was clear and that it was neither necessary nor appropriate to refer any of the questions before it to the CJEU (FTT [338]).

The grounds of appeal

33. Gallaher applied for permission to appeal against the FTT's decision in the 2011 Appeal. HMRC applied for permission to appeal against the FTT's decision in the 2014 Appeal. The FTT granted permission in each case.

34. Gallaher's grounds of appeal in the 2011 Appeal, as set out in its Notice of Appeal, were, in summary, as follows:

- (1) the FTT erred in holding that there was no restriction on JTIH's freedom of establishment under Article 49 TFEU in relation to the 2011 Disposal and, in particular, in its analysis of the decision of the CJEU in *Test Claimants in the Thin Cap Group Litigation v Inland Revenue Commissioners* (Case C-524/04) (“*Thin Cap*”);
- (2) the FTT erred in holding that Gallaher was not entitled to rely on JTIH's or Gallaher's freedom to move capital under Article 63 TFEU on the basis that the Group Transfer Rules relate to the treatment of groups of companies and the only freedom which could be considered in that context was the freedom of establishment under Article 49;
- (3) to the extent that it was unable to resolve the 2011 Appeal in favour of Gallaher, the FTT should have referred the matter to the CJEU for a preliminary ruling.

35. HMRC's grounds of appeal in the 2014 Appeal, as set out in its Notice of Appeal, were, in summary, as follows:

- (1) the FTT erred in holding that the Group Transfer Rules created a restriction on JTIH's freedom of establishment and/or in holding that any such restriction was not justified on the basis that JTIH was not in an objectively comparable situation to that in which it would have been if it had been resident in the UK;
- (2) the FTT erred in holding that any restriction on JTIH's freedom of establishment was not justified, in particular, in holding that the requirement to pay corporation tax immediately on the accrued gain on the Galleon shares at the time of their transfer to JTIH was not proportionate;
- (3) the FTT erred in holding that it was precluded from applying a conforming interpretation to the legislation, in particular, a conforming interpretation which provides an option for the tax to be paid in instalments; and
- (4) the FTT erred in rejecting HMRC's proposed "disapplication" of the legislation so as to provide for a deferral of the charge to tax for five years on the grounds that it constituted an amendment of the legislation and not a disapplication in any meaningful sense.

36. Before us, in relation to the 2014 Appeal, HMRC did not pursue its argument that the Group Transfer Rules did not create a restriction on JTIH's freedom of establishment. However, all the other issues referred to in the parties' Notices of Appeal remained in issue.

The parties' submissions on the substantive issues

37. We have set out, in the following paragraphs, a summary of the parties' submissions on the various issues that were before us. The parties' submissions were lengthy and detailed and inevitably focused on matters in greater detail than set out in their grounds of appeal. Our summary should not be taken to suggest that we have not taken into account the parties' more detailed arguments or other authorities to which we were referred.

The 2011 Appeal

38. We will deal first with the issues arising in relation to the 2011 Appeal.

The interaction of Article 49 and Article 63 TFEU

39. The first question before us in relation to the 2011 Appeal is the question of the interrelationship of the freedom of establishment under Article 49 TFEU and the freedom to move capital under Article 63 TFEU and accordingly whether Gallaher was required to bring its challenge to the operation of the Group Transfer Rules by reference to a particular freedom or could rely on both freedoms in the alternative.

40. On this question Mr Baker, for Gallaher, argues that the companies in the JT Group are entitled to bring their challenges to the Group Transfer Rules either on the basis of their right to freedom of establishment under Article 49 or on their right to freedom to move capital under Article 63. Although, it might be more common for complainants to rely upon the right to freedom of establishment in the group context, it is clear from the CJEU case law that Article 63 TFEU can be relied upon in relation to controlling shareholdings (see for example *Kronos International Inc. v Finanzamt Leverkusen* (Case C-47/12) (“*Kronos*”) [39] and *EV v Finanzamt Lippstadt* (Case C-685/16) (“*EV*”) [32] – [42]). Furthermore, in his submission, there is nothing in the CJEU case law to preclude a party from bringing a challenge to domestic legislation relying on the freedom to move capital where the freedom of establishment might not apply.

41. Mr Baker submits further that, even if the Tribunal takes the view that, in a straightforward case, any challenge to legislation, which applies exclusively to group companies, should be made by reference to Article 49 TFEU, there were additional factors in the 2011 Appeal which militated in favour of allowing Article 63 TFEU to be relied upon.

(1) First, the 2011 Appeal involves two shareholdings which are relevant to JTIH’s freedom to move capital: its shareholding in Gallaher and its shareholding in JTISA. JTIH may have exercised its rights to freedom of establishment under Article 49 in respect of its shareholding in Gallaher, but it can only have exercised its freedom to move capital under Article 63 in relation to its shareholding in JTISA. There is no authority for the view that only the freedom of establishment can be engaged in such circumstances.

(2) Second, Gallaher’s case is that there is also a restriction on Gallaher’s freedom to move capital in the form of the transfer of the Brands and related assets to JTISA. JTISA and Gallaher are sister companies and so Gallaher is not in a position to exercise its freedom of establishment in relation to JTISA.

42. Mr Baldry, for HMRC submits that the FTT correctly decided that, in the context of legislation which applies exclusively to group companies, the only treaty freedom which is engaged is the freedom of establishment under Article 49 TFEU (FTT [54]-[67], [239]-[241]). He says that the CJEU case law is clear that it is the nature of the legislation at issue in the proceedings which determines which freedom applies. Domestic legislation which is intended to apply only to shareholdings which enable the holder to exert a definite influence on a company’s decision making and to determine its activities falls exclusively within the scope of Article 49 TFEU on freedom of establishment. Domestic legislation which applies to shareholdings acquired solely with the intention of making financial investments without any intention to influence

the management and control of the company should be examined exclusively in the light of the freedom of movement of capital and Article 63 TFEU (*FII Group Test Claimants v Revenue & Customs Commissioners (No.3)* (Case C-35/11) [91] [92], *Thin Cap* [33], [34] and [101]). In the present case, the Group Transfer Rules apply exclusively to companies within groups. It follows that only the freedom of establishment in Article 49 TFEU is engaged.

Do the Group Transfer Rules represent a restriction on JTIH's freedom of establishment?

43. Mr Baker says that the relevant exercise of the freedom of establishment in this context is JTIH's acquisition of the shares in Gallaher. The immediate tax charge on the transfer of the Brands and related assets by Gallaher to JTISA represented a restriction on that freedom because it was likely to render the exercise of that freedom less attractive. The correct comparison for this purpose was with a wholly domestic situation, that is a transfer of an asset by a UK resident subsidiary of a UK resident parent company to a sister company which is also resident in the UK (*Société Papillon v Ministère du Budget, des Comptes Publics et de la Fonction Publique* (Case C-418/07) ("*Papillon*") [27] and [32]). In this scenario, no immediate tax charge would have arisen as the Group Transfer Rules would have applied.

44. Mr Baker submits that it is no answer to this point that a UK resident subsidiary of a UK resident parent company would have suffered the same tax charge on the transfer of the Brands and related assets to a Swiss resident company. It is acknowledged that a company which is exercising a treaty freedom may as a result be put in a potentially better position than an entirely domestic group (*Caixa-Bank France v Ministère de l'Economie, des Finances et de l'Industrie* (Case C-442/02) ("*Caixa-Bank*")).

45. Mr Baker criticised the FTT's analysis of the decision of the CJEU in *Thin Cap*. The CJEU decided in that case that an EU parent company's freedom of establishment was restricted by limitations on the deductibility of interest not only on loans which were made by the EU parent company to a UK subsidiary, but also on loans made by another subsidiary of the EU parent, irrespective of where it was resident, to a UK subsidiary of the EU parent company (*Thin Cap* [95]). The *Thin Cap* case demonstrated, by analogy, that the Group Transfer Rules did place a restriction on JTIH's freedom of establishment in this case.

46. Mr Baldry says that Article 49 is concerned with differential treatment under domestic law based on nationality. It is JTIH's nationality that matters. The correct comparison is whether the UK resident subsidiary of JTIH, Gallaher, is treated differently by reason of the nationality of its parent, JTIH, or whether the non-UK resident parent is treated differently because of the nationality of its UK resident subsidiary. This is the test that the CJEU applies in *Thin Cap* (at [94], [95]).

47. Mr Baldry submits that the 2011 Disposal does not involve a restriction on JTIH's freedom of establishment. Gallaher would have incurred an immediate tax charge on the disposal of the Brands to JTISA, a Swiss company, irrespective of whether its parent company, JTIH, was resident in the UK or in the Netherlands.

48. Mr Baldry dismisses the reference to *Caixa-Bank*. He says that it is an entirely different context and not relevant in this case.

Is any restriction on JTIH's freedom of establishment proportionate?

49. It is common ground between the parties that any restriction imposed by the Group Transfer Rules can be justified by reasons in the public interest, namely the objective of ensuring the balanced allocation of taxing powers between member states (*National Grid Indus BV v Inspecteur van de Belastingdienst Rijnmond* (Case C-371/10) (“*NGP*”) [45], [46] and [64]). The issue between the parties is whether any such restriction is appropriate to ensure the attainment of that objective and does not go beyond what is necessary to attain that objective, i.e. whether the restriction is “proportionate”.

50. Mr Baker, for Gallaher, says that the imposition of an immediate tax charge in relation to the 2011 Disposal is not proportionate. He refers by analogy to cases involving exit taxes on migration (such as *De Lasteyrie v Ministere de l'Economie, des Finances et de l'Industrie* (Case C-9/02), *N v Inspecteur van de Belastingdienst Oost* (Case C-470/04), and *NGI*). In those cases, the CJEU has held that, for the purposes of maintaining a balanced allocation of taxing powers between member states, the member state, of which a taxpayer is ceasing to be a resident, is justified in imposing a tax charge calculated by reference to the value of the taxpayer's assets at the time at which the taxpayer ceases to be so resident (and so at the time at which the asset in question ceases to be within the scope of taxation in that member state). However, if that measure is to be proportionate, the taxpayer must be permitted an option to defer the tax charge (see *NGI* [73]). Mr Baker also points to cases in which similar concepts have been employed by the CJEU in cases which are not “pure” exit tax cases to demonstrate that these concepts are not restricted to circumstances involving the taxation of unrealized gains (see *Commission v Germany* (Case C-591/13) (“*Germany*”) [71]).

51. Mr Baldry says that the correct approach is for this Tribunal to weigh all the aspects of the regime and to determine whether or not, to the extent that they might infringe a treaty freedom, the provisions of that regime are justified and proportionate in all the circumstances. The imposition of an immediate tax charge in the circumstances of the 2011 Appeal (and the 2014 Appeal) is an appropriate and proportionate response.

52. He submits that it is necessary to consider the objective of the relevant provisions. The objective of the Group Transfer Rules was to exclude an actual disposal made by a UK resident company to a company outside the scope of UK tax from the tax neutral treatment afforded by the Group Transfer Rules and to tax an actual gain realized by the UK resident company. The tax charges imposed by the legislation were consistent with the accepted principles of international double tax treaties (for example, the UK/Netherlands double tax treaty), which conferred upon the state of residence the right to tax gains accruing on the alienation of assets. The CJEU cases recognized the UK's right to tax that gain.

53. Mr Baldry says that the facts of these appeals differ from the exit tax cases (such as *NGI*) or the other cases in which such principles had been adopted by the CJEU (such

as *Germany*). In those cases, either gains were unrealized or the conditions imposed for the taxpayer to obtain the relevant relief imposed requirements, which dictated that the taxpayer would not have proceeds from which to pay the tax. In that context, the requirement for a deferral of the collection of the tax was appropriate. These appeals involved actual disposals and realized gains. In that context, there was no need for the deferral of the collection of that tax. The imposition of an immediate tax charge in the ordinary way did not go beyond what was necessary to achieve the objective.

Issues relating to Article 63 TFEU

54. As we have mentioned above, the FTT decided that the freedom to move capital under Article 63 TFEU was not engaged in the context of legislation targeted at groups of companies. However, the FTT went on to consider the position which would have obtained if it had decided that it was open to JT Group companies to rely upon Article 63 in relation to the 2011 Appeal. Those comments were clearly obiter. However, the FTT's conclusions were, in summary, as follows:

(1) There were two potential movements of capital within Article 63 TFEU in relation to JTIH's investment in JTISA: the first when JTIH established JTISA and subscribed shares in JTISA; and the second when JTIH made loans to JTISA to fund the acquisition of the Brands (FTT [234]).

(2) If Article 63 was engaged, the Group Transfer Rules did not impose a restriction on the exercise of JTIH's freedom to move capital because there was no necessary connection between the movement of capital and the transfer of the Brands and related assets (FTT [243]).

(3) The standstill provisions, in Article 64 TFEU, would have applied with the effect that the JT Group companies could not have relied on any restriction which arose from the application of the Group Transfer Rules (FTT [252]).

(4) The transfer of the Brands and related assets by Gallaher to JTISA was a movement of capital for the purposes of Article 63 (FTT [265]) and the Group Transfer Rules were a restriction on that freedom.

(5) Article 64 TFEU did not apply to the transfer of the Brands because it was not a "direct investment" for the purposes of Article 64 (FTT [270]).

(6) Article 65 TFEU did not apply to permit the UK to restrict Gallaher's right to move capital (FTT [271]).

55. Mr Baker challenged some of these conclusions in so far as they related to movements of capital by JTIH.

(1) First, Mr Baker submits that the Group Transfer Rules do impose a restriction on the exercise of JTIH's freedom to move capital for much the same reasons as they constituted a restriction on JTIH's freedom of establishment.

(2) Second, he points out that the standstill provisions in Article 64 TFEU could not apply to the loan made by JTIH because Article 64 applied to "direct

investments” and the loan was not a “direct investment” for the purposes of the Nomenclature.

(3) Finally, Mr Baker did not concede that Group Transfer Rules fell within the standstill provisions in Article 64 TFEU. Section 171 TCGA had been amended on several occasions since 1993 and s775 and s776 CTA 2009 were part of the intangible fixed assets rules, which were introduced in 2002.

56. Mr Baldry makes the following submissions.

(1) He supports the FTT’s conclusion that the Group Transfer Rules did not restrict the movements of capital comprising the establishment by JTIH of JTISA (FTT [243]).

(2) The alleged incompatible provisions in the Group Transfer Rules had, in substance, been part of the UK tax regime before 1993 and accordingly the standstill provision in Article 64 applies to prevent the application of Article 63 to the Group Transfer Rules in cases involving a “direct investment”.

For this purpose it was necessary to look at the substance of the legislation and its effect on the companies that were excluded from the benefit of the legislation (see Henderson J in *Test Claimants in the FII Group Litigation v Revenue and Customs Commissioners* [2008] EWHC 2893 (Ch), [2009] STC 254 at [98]). Any changes in the rules had not affected the basic proposition that a transfer of an asset by a UK company to a Swiss company could not benefit from the tax neutral treatment afforded by the rules.

(3) Article 64 applied to restrictions “involving” a direct investment. The only direct investment in the present case was JTIH’s establishment of JTISA, to which Article 64 applied.

(4) The FTT was wrong to conclude that the transfer of the Brands by Gallaher to JTISA was a separate movement of capital. Article 63 applies to financial investments and not the transfer of an asset for full consideration.

(5) As regards the application of Article 65, the UK was entitled to charge tax on the disposal of the Brands. The only point at issue in this case was the collection and payment of that tax. It was difficult to describe the collection and payment mechanism as “arbitrary discrimination” or a “disguised restriction” on the free movement of capital within paragraph 3 of Article 65.

The 2014 Appeal

57. The only issue between the parties in relation to the 2014 Appeal is whether or not the imposition of an immediate charge to tax without the option of deferral constitutes a proportionate means of achieving the objective of taxing the accrued gain on the Galleon shares. The parties’ submissions on this issue are essentially the same as those which they make in relation to that issue in relation to the 2011 Appeal as set out at [49] to [53] above.

Issues relating to the appropriate or permissible remedies

58. The next group of issues relate to the remedies which are available to this Tribunal if we find that the imposition of an immediate tax charge is contrary to EU law and that in order to be proportionate it would be necessary for UK tax law to offer the option to defer the tax charge.

The basis of deferral

59. The first issue relates to what type of deferral is required by EU law for a restriction to be regarded as proportionate.

60. In summary, Mr Baker and Mr Afzal, for Gallaher, submit that the appropriate remedy is for tax to be deferred until a disposal of the relevant assets outside the group or sub-group (a “realization basis”). On this basis, Gallaher would pay tax only when a relevant group company realized proceeds from the disposal of the relevant asset i.e. the Brands and related assets in relation to the 2011 Disposal or the shares in Galleon in relation to the 2014 Disposal.

61. Mr Baldry points out that the UK’s ability to tax the gain realized by the 2011 Disposal and the 2014 Disposal is recognized in the CJEU cases. Gallaher’s interpretation results in a position where the gain is potentially never taxed at all. Mr Baldry submits that the appropriate remedy is to permit Gallaher to pay tax by instalments (an “instalment basis”). He says that the most appropriate conforming interpretation is to import a requirement for the payment of tax by Gallaher by instalments over five years in a manner consistent with either Schedule 49 Finance Act 2013 (deferral of payment of exit charge) or the new legislation in Schedule 3ZC Taxes Management Act 1970 (“TMA 1970”) (see [88] below).

62. Both parties provided the Tribunal with drafting of changes to existing legislation to give effect to their preferred interpretation.

63. Mr Baker and Mr Afzal accept that there are cases in which the CJEU has found an instalment basis to be proportionate (see, for example, *DMC Beteiligungsgesellschaft mbH v Finanzamt Hamburg-Mitte* (Case C-164/12) (“*DMC*”) and *Verder LabTec GmbH & Co. KG v Finanzamt Hilden* (Case C-657/13) (“*LabTec*”). However, in those cases, the CJEU considered regimes in which the option to pay by instalments already existed in domestic law. Those cases simply confirmed that an existing instalment payment regime might be a proportionate means of achieving a legitimate objective. It did not follow that it was open to a national court or tribunal to provide a remedy which comprised a deferral of the tax charge on an instalment basis. Even if those cases could be read in that way, the CJEU case law has developed further following the decision of the CJEU in *Martin Wächter v Finanzamt Konstanz* (C-581/17) (“*Wächter*”) such that, even if domestic law provides for deferral on an instalment basis, it is nonetheless necessary for taxpayers to be given the option of deferral on a realization basis if the regime is to be proportionate.

64. Furthermore, even if in principle deferral on an instalment basis might be an appropriate remedy, Mr Baker and Mr Afzal submit that as a matter of EU law, national

courts and tribunals must provide a remedy which interferes with the protected EU law freedom to the least possible extent as opposed to a remedy which, although proportionate, departs from domestic law to the least possible extent. On this basis, a remedy involving a deferral on an instalment basis cannot be preferred over a remedy providing deferral on a realization basis.

65. Mr Baldry says that, even if the principles in the exit tax cases can be applied by analogy to the Group Transfer Rules, the CJEU case law is clear that it would be proportionate to provide a remedy by payment by instalments. He refers, in this context, to the decisions of the CJEU in *DMC* and *LabTec* in which the CJEU held that the relevant instalment bases (in the case of *DMC* involving instalments over 5 years, and in the case of *LabTec* involving instalments over 10 years) were proportionate regimes. He also distinguishes the decision of the CJEU in *Wächtler* on the grounds that it is a hardship case and should not be read as diverging from the earlier cases. On this basis, Mr Baldry says that it is open to this Tribunal to provide a remedy which requires payment on an instalment basis. He notes that the First-tier Tribunal in *Trustees of the P Panayi Accumulation and Maintenance Trusts Nos 1-4 v Revenue and Customs Commissioners* [2019] UKFTT 622 (TC) (“*Panayi*”) adopted this approach.

66. Mr Baldry challenges Gallaher’s assertion that a national court or tribunal must provide a remedy which interferes with the protected treaty freedom to the least possible extent. There is no authority for this proposition. The correct approach is that the national court or tribunal should go no further than is necessary to interpret the legislation in an EU law compliant way (see, for example, *The Prudential Assurance Co. Ltd v Revenue and Customs Commissioners* [2013] EWHC 3249 (Ch) (“*Prudential*”) [148], *Revenue and Customs Commissioners v IDT Card Services Ireland Limited* [2006] EWCA Civ 29 [91], *Routier and another v Revenue and Customs Commissioners* [2017] EWCA Civ 1584 [93]). This principle follows logically from the fact that the national court’s power to make conforming interpretation only arises where the legislation itself is not compliant. There is no jurisdiction to go further than is necessary to render the domestic law compliant with EU law.

Conforming interpretation or disapplication

67. The second issue relates to the manner in which the remedy should be given. The parties agree that there are two options open to the Tribunal: either to construe the relevant UK legislation in a manner which is consistent with EU law, a so-called “conforming interpretation” or “conforming construction”; or alternatively to disapply the offending provisions.

68. Both parties agreed that the FTT’s approach to disapplication was wrong. The FTT treated disapplication as involving a striking out of words or provisions in domestic legislation (FTT [221]-[228]). The correct approach was that disapplication required the relevant domestic legislation be read as applying without prejudice to directly enforceable EU law rights (*R v Secretary of State for Transport ex parte Factortame* [1990] 2 AC 85 at 140).

69. Both parties also agreed that, contrary to the FTT's view, the Group Transfer Rules were capable of a conforming interpretation to give effect to the relevant EU law rights and that the relevant principles to be applied were those set out in the decision of the Court of Appeal in *Vodafone 2 v Revenue & Customs Commissioners* [2009] EWCA Civ 446, [2010] 2 WLR 288 ("*Vodafone 2*"). In summary, those principles are that the obligation on the UK courts and tribunals to construe domestic legislation in a manner consistent with EU law is "both broad and far reaching" and the only constraints on that obligation are that the interpretation should "go with the grain of the legislation" and the exercise of that interpretative obligation "cannot require the courts to make decisions for which they are not equipped or give rise to important practical repercussions which the court is not equipped to evaluate" (*Vodafone 2* [37], [38]).

70. Mr Afzal for Gallaher submits that a realization basis does not involve the Tribunal straying into questions which it is not equipped to decide. The FTT was wrong to decide that Gallaher's proposed conforming interpretation did not go with the grain of the legislation. There were existing examples of circumstances in tax legislation applicable to corporation tax on chargeable gains where the taxation of a realized gain was deferred until a future realization of the relevant asset. Mr Afzal referred to s116 TCGA (qualifying corporate bonds) and s140 TCGA (incorporation of foreign branches) as two such examples.

71. By contrast, Mr Afzal submits that an instalment basis did not "go with the grain" of the legislation. A UK company, which was the transferee of an asset under a transaction within s171 TCGA would be taxed on any gain on the asset on a realisation basis not on an instalment basis. Furthermore, the imposition of an instalment basis involved the court or tribunal straying into matters which a court or tribunal was not equipped to decide, namely, the number and date of instalments.

72. Mr Baldry argues that the adoption of an instalment basis is within the ambit of the "highly muscular approach" to the doctrine of conforming interpretation required by *Vodafone 2*. It was not beyond the scope of the powers of the Tribunal as demonstrated by the decision of the FTT in *Panayi*.

73. He says that the approach also went with the grain of the legislation. There were examples of other instalment bases used in the legislation (see, for example, s49 Finance Act 2013 and Schedule 3ZB TMA 1970). It was the appropriate basis to apply when an asset would otherwise leave the scope of UK tax.

Effectiveness of instalments as a remedy

74. Finally, Mr Baker and Mr Afzal submit that, even if an instalment basis is a proportionate and appropriate remedy in these circumstances, the minimal deferral period should be five years and all the instalments should be prospective i.e. they should not run until the date of the final determination of these proceedings. They say this is required by the principle of effectiveness in EU law. Mr Baldry disputes this submission. He says that the imposition of an instalment basis from the date of disposal of the assets would not amount to retrospective taxation; the Tribunal would simply be making a decision as to what the law was at the time.

Referral to the CJEU

75. As we have mentioned above, the FTT decided (FTT [338]) that it was neither necessary nor appropriate to refer any of the EU law issues to the CJEU for a preliminary ruling. In its view, the application of the TFEU to the 2011 Disposal and the 2014 Disposal was clear.

The parties' submissions

76. Mr Baldry, for HMRC, submits that the FTT was correct in its view that all of the issues could be addressed by the Tribunal on the basis of well-established principles of CJEU case law. In particular, he says:

- (1) in relation to the 2011 Appeal: it is clear that:
 - (a) Article 63 TFEU has no application to cases involved in legislation which is directed at corporate groups;
 - (b) there is no restriction on JTIH's freedom of establishment as the same treatment would apply even if Gallaher's parent company had been incorporated and resident in the UK;
- (2) in relation to the 2014 Appeal, the only point of issue is whether or not the imposition of an immediate charge to tax on the disposal was proportionate. Once again, the effect of the CJEU case law is clear;
- (3) the question of remedies is a matter for the national court or tribunal. It is not a matter for CJEU.

77. Mr Baker and Mr Afzal for Gallaher also submit that it is not necessary for this Tribunal to make a reference to the CJEU in relation to the 2011 Appeal or the 2014 Appeal. But, they say, that is only the case if the Tribunal is proposing to decide both appeals in favour of Gallaher. If the Tribunal is proposing to determine either appeal against Gallaher, it cannot do so without making a reference to the CJEU.

78. Mr Baker and Mr Afzal refer to various issues, which, they say, would need to be resolved against Gallaher, and which are not "acte clair":

- (1) in relation to the 2011 Appeal:
 - (a) the interaction of Article 49 TFEU and Article 63 TFEU and, in particular, whether it is possible to rely upon Article 63 in the context of legislation, such as the Group Transfer Rules, which is targeted at groups of companies; and,
 - (b) even if Article 63 cannot generally be relied upon in such circumstances, whether the special circumstances of the 2011 Disposal – namely the fact that the company concerned (JTIH) has shareholdings both in a company in the UK on which the tax charge is imposed and in a company in a third country or the fact that the movement of capital occurred between sister companies – affected the analysis;

(c) whether the imposition of an immediate charge to tax under the Group Transfer Rules without an option to defer was a restriction on JTIH's freedom of establishment or its freedom to move capital where the transfer of assets was made to a person in a third country;

(d) whether the imposition of an immediate tax charge without the option to defer was proportionate;

(e) if it was possible for JTIH to rely upon Article 63 TFEU in relation to its movements of capital, the issues surrounding the application of Articles 64 and 65;

(f) whether the transfer of the Brands and related assets by Gallaher to JTISA was a movement of capital for the purposes of Article 63 TFEU; and

(2) in relation to the 2014 Appeal, whether the imposition of an immediate tax charge without the option to defer was proportionate.

79. Mr Baker and Mr Afzal acknowledge that the question of the form of any remedy is primarily an issue for the national court or tribunal. However, they submit that it is appropriate to make a reference to the CJEU on questions of EU law which impinge upon the nature or form of the remedy which the national court or tribunal proposes to grant. So, for example, in the context of the current appeals, it would be appropriate for this Tribunal to refer questions, such as: (i) whether a conforming interpretation, which provided an option for payment by instalments could be a proportionate remedy; (ii) even if payment by instalments was a proportionate remedy, whether it was possible for a national court or tribunal to require payment by instalments by a conforming interpretation or disapplication, in circumstances where there was no provision for payment by instalments under existing domestic law; and (iii) whether in deciding between a choice of two proportionate remedies, it was incumbent upon the national court or tribunal to adopt the remedy which imposed the least restriction on the relevant EU treaty freedom. A reference might also be made to the CJEU on questions which engaged general principles of EU law. For example, it should be open to this Tribunal to make a reference regarding the effectiveness of any potential remedy, including whether or not it was possible for the court or tribunal to impose a remedy by way of payment by instalments, where the instalment payments began before the date of the final determination of the issues between the parties by the court or tribunal.

The appropriate test

80. There was no dispute between the parties as to the principles which the courts and tribunals should apply in determining whether or not to make a reference to the CJEU. They are summarized by Rose J (as she then was) in *Coal Staff Superannuation Scheme Trustees Limited v Revenue and Customs Commissioners* [2017] UKUT 137 (“*Coal Staff*”) at [27], where she said:

“That test was considered recently by Judge Berner in *Capernwray Missionary Fellowship of Torchbearers v HMRC* [2015] UKUT 368 (*Capernwray*). In that case the parties applied jointly to the Upper Tribunal before the substantive hearing of the taxpayer's

appeal for the Judge to make a reference to the CJEU. Judge Berner referred to the authoritative summary of the approach to be adopted by courts and tribunals in considering whether to make a reference by Sir Thomas Bingham MR in *R v International Stock Exchange of the United Kingdom and the Republic of Ireland Ltd ex parte Else (1982) Ltd and another* [1993] QB 534 ('*Else*'). At p 545 Lord Bingham said:

'... I understand the correct approach in principle of a national court (other than a final court of appeal) to be quite clear: if the facts have been found and the Community law issue is critical to the court's final decision, the appropriate course is ordinarily to refer the issue to the Court of Justice unless the national court can with complete confidence resolve the issue itself. In considering whether it can with complete confidence resolve the issue itself the national court must be fully mindful of the differences between national and Community legislation, of the pitfalls which face a national court venturing into what may be an unfamiliar field, of the need for uniform interpretation throughout the Community and of the great advantages enjoyed by the Court of Justice in construing Community instruments. If the national court has any real doubt, it should ordinarily refer. I am not here attempting to summarise comprehensively the effect of such leading cases as *H. P. Bulmer Ltd. v. J. Bollinger S.A.* [1974] Ch. 401, *C.I.L.F.I.T. (S.r.l.) v. Ministry of Health* (Case 283/81) [1982] E.C.R. 3415 and *Reg. v. Pharmaceutical Society of Great Britain, Ex parte Association of Pharmaceutical Importers* [1987] 3 C.M.L.R. 951, but I hope I am fairly expressing their essential point.'

81. We should make a reference if (i) a matter of EU law is critical to our decision and (ii) we cannot “without complete confidence” resolve the issues ourselves. As Rose J noted in the *Coal Staff* case (at [28]), in considering these issues, we should have regard to factors such as the nature of the issues, whether they are likely to have application beyond the particular facts of this case, and the existence or absence of an established body of case law of the CJEU setting out the principles that should be applied to these facts.

The effect of the UK's withdrawal from the EU

82. We note, in passing, that the legislation which governs the UK's withdrawal from the EU provides that a UK court or tribunal cannot refer any matter to the CJEU on or after “IP completion day”, which is at 11pm on 31 December 2020 (s6(1)(b) EUWA 2018 as amended by s26(1) European Union (Withdrawal Agreement) Act 2020). There is nothing in the legislation to suggest that the impending withdrawal of the power of the courts to make a reference to the CJEU should affect our approach to the question as to whether a reference should be made in this case.

Application to the facts of this case

83. We have considered the issues that have been argued before us and have reached the conclusion that, having taken into account the various factors set out by Rose J in the *Coal Staff* case, we should make a reference to the CJEU for a preliminary ruling in respect of each of the following issues:

(1) Whether Article 63 TFEU can be relied upon in relation to domestic legislation such as the Group Transfer Rules, which applies to groups of companies?

(2) Even if Article 63 TFEU cannot more generally be relied upon, can it nonetheless be relied upon:

(a) in relation to movements of capital from a parent company resident in an EU member state to a Swiss resident subsidiary, where the parent company has shareholdings in both the Swiss resident subsidiary and the UK resident subsidiary on which the tax charge is imposed?

(b) in relation to a movement of capital by a subsidiary resident in the UK to a Swiss resident subsidiary of the same parent company resident in an EU member state, given that the two companies are sister companies and not in a parent-subsidiary relationship?

(3) Whether legislation, such as the Group Transfer Rules, which imposes an immediate tax charge on a transfer of assets from a UK resident company to a sister company which is resident in Switzerland (and does not carry on a trade in the UK through a permanent establishment), where both of those companies are subsidiaries of a common parent company, which is resident in another member state, in circumstances where such a transfer would be made on a tax neutral basis if the sister company were also resident in the UK (or carried on a trade in the UK through a permanent establishment), constitutes a restriction on the freedom of establishment of the parent company in Article 49 TFEU or, if relevant, a restriction on the freedom to move capital in Article 63 TFEU?

(4) Assuming Article 63 TFEU can be relied upon:

(a) was the transfer of the Brands and related assets by Gallaher to JTISA, for a consideration which was intended to reflect the market value of the Brands, a movement of capital for the purposes of Article 63 TFEU?

(b) did the movements of capital by JTIH to JTISA, its Swiss resident subsidiary, constitute direct investments for the purposes of Article 64 TFEU?

(c) given that Article 64 TFEU only applies to certain types of capital movement, can Article 64 apply in circumstances where movements of capital can be characterized as both direct investments (which are referred to in Article 64 TFEU) and also as another type of capital movement not referred to in Article 64 TFEU?

(5) if there was a breach of the freedom of establishment and/or of the right to free movement of capital:

(a) does EU law require that the domestic legislation be interpreted or disapplied in a manner which provides Gallaher with an option to defer the payment of tax;

(b) if so does EU law require that the domestic legislation be interpreted or disapplied in a manner which provides Gallaher with an option to defer the payment of tax until the assets are disposed of outside the sub-group of which the company resident in the other Member State is parent (i.e. “on a realization basis”) or is an option to pay tax in instalments (i.e. “on an instalment basis”) capable of providing a proportionate remedy;

(c) if, in principle, an option to pay tax by instalments is capable of being a proportionate remedy:

- i. is that only the case if domestic law contained the option at the time of the disposals of assets, or is it compatible with EU law for such an option to be provided by way of remedy after the event;
- ii. does EU law require national courts to provide a remedy which interferes with the relevant EU law freedom to the least possible extent, or is it sufficient for the national courts to provide a remedy which, whilst proportionate, departs from the existing national law to the minimum extent possible;
- iii. what period of instalments is necessary; and
- iv. is a remedy involving an instalment plan in which payments fall due prior to the date on which the issues between the parties are finally determined in breach of EU law, i.e. must the instalment due dates be prospective?

84. As can be seen from our summary of the arguments that have been made before us, despite the existence of a material body of CJEU case law which relates to broadly analogous situations, there is no authority to which we have been referred, which deals directly with legislation such as this, which provides for tax neutral treatment of intragroup transfers of assets and can apply in cases where the taxpayer company has realized a full market value consideration for the transfer. As a result, in respect of many of these issues, it is possible reasonably to hold differing views as to the implications of the application of the existing CJEU case law to the facts of these appeals.

85. By way of example:

(1) in the context of the interaction of Article 49 and Article 63 TFEU and, in particular, whether Gallaher can rely on Article 63 in addition to or as an alternative to Article 49 in the context of legislation which applies only to groups of companies, Mr Baker raises material issues which are not addressed by the existing case law concerning the application of the existing case law to facts in which there may be more than one movement of capital by JTIH to which the freedom applies or to facts involving a potential movement of capital by a company (Gallaher) which cannot be exercising a freedom of establishment under Article 49;

(2) whether, on the facts of the 2011 Appeal, the implication of the reasoning in the *Thin Cap* case is that the Group Transfer Rules can represent a restriction on the exercise of JTIH's freedoms (under Article 49 or Article 63) even though the same immediate tax charge would have arisen on a disposal of the Brands and related assets by Gallaher to JTISA even if the parent company (JTIH) had been resident in the UK for tax purposes;

(3) in determining, on the facts of the 2011 Appeal or the 2014 Appeal, whether any restriction which is imposed by the Group Transfer Rules on the exercise of the treaty freedoms is justified and proportionate, whether it is appropriate to extend the principles in the exit tax cases (such as *NGI*) to cases where the taxpayer in question (Gallaher) has realized proceeds for the disposal of the asset equal to the full market value of the asset;

(4) in the context of the remedies available to this Tribunal, whether it is open to this Tribunal to provide, by conforming interpretation or disapplication, for the payment of tax by instalments where there was, at the time of the disposals in question, no applicable provision for the payment of tax by instalments in the Group Transfer Rules.

86. These are material issues of EU law, which are critical to our decision. Whilst we would ordinarily be quite prepared to reach a decision on them, we cannot resolve the issues "with complete confidence" as required by the test set out by Sir Thomas Bingham MR in *R v International Stock Exchange of the United Kingdom and the Republic of Ireland Ltd ex parte Else (1982) Ltd and another* [1993] QB 534 and referred to by Rose J in her decision in the *Coal Staff* case. The other issues to which we refer at [83] above are consequential questions which arise from them.

87. Furthermore, it seems to us that the decisions in these appeals are likely to have application beyond the particular facts of this case.

88. We note that, following the FTT decision in these appeals, the Government introduced legislation to permit UK resident companies to enter into payment plans and to pay tax by instalments in relation to intragroup transfers of assets to companies resident in EEA member states under various regimes which form part of UK tax law, including those covered by the Group Transfer Rules. (Those provisions were introduced by s34 of and Schedule 7 to the Finance Act 2020 and are now found in s59FB TMA 1970 and Schedule 3ZC TMA 1970.) They apply to all accounting periods ending on or after 10 October 2018.

89. We have not heard argument on this point, but it seems to us that the responses of the CJEU to the questions that we have raised may well inform the interpretation of the new instalment regime. Even if the introduction of the new instalment regime is sufficient to ensure that the Group Transfer Rules are regarded as compliant with EU law for periods ending on or after 10 October 2018, there remains the question of the application of the Group Transfer Rules to the treatment of transfers in prior periods. Beyond the implications of the questions that we have raised for provisions of UK tax law, the transfer of assets between group companies is a relatively common transaction and we anticipate that the matters raised in this request for a preliminary ruling will be relevant to the interpretation of similar provisions in the domestic legislation of EU member states.

Decision

90. For these reasons, we have decided that a request should be made to the CJEU for a preliminary ruling in relation to the matters listed at [83] above. We will ask counsel to prepare a draft request to be settled by this Tribunal and submitted to the CJEU before the end of the transition period on 31 December 2020.

MR JUSTICE MILES

ASHLEY GREENBANK

UPPER TRIBUNAL JUDGES

Signed on Original

RELEASE DATE: 14 December 2020