

<p>1 Thursday, 28 April 2016 2 (1.29 pm) 3 MR JUSTICE HILDYARD: Yes, who starts, Mr Gardiner? 4 MR GARDINER: Yes, my Lord, yes. 5 MR JUSTICE HILDYARD: Good afternoon. I'm sorry for the 6 inconvenience of this curious starting time and I'm very 7 grateful to you for your cooperation in it. 8 Opening Submissions by MR GARDINER 9 MR GARDINER: No, we're certainly hopeful, within reason, 10 we'll be able to finish, hopefully, by the right kind of 11 time tomorrow afternoon. 12 My Lord, as you have seen, I appear in this case 13 with my learned friends, Mr Bayfield, Mr Walford, on 14 behalf of the joint administrators of Lehman Brothers 15 International (Europe), an unlimited company I'll refer 16 to as LBIE. My learned friends, Mr Goy and Miss Addy, 17 appear on behalf of Her Majesty's Revenue and Customs, 18 whom I will refer to as HMRC or more likely, The 19 Revenue. 20 I'm conscious of the fact that we gave your Lordship 21 a long reading list. I hope you've had an opportunity 22 to read those papers. That will obviously enable me to 23 take, I hope, the matter more quickly than otherwise. 24 You will also, I am sure, be familiar with the history 25 of this administration. The downfall of Lehman's and</p> <p style="text-align: center;">Page 1</p>	<p>1 If I could then go to the core bundle, and just look 2 at the application. The application, you'll see, is the 3 first item in the core bundle at tab 1. The relevant 4 question that we're asking your Lordship to determine is 5 on the second page of the application. If I just read 6 that: 7 "Whether or not the payment in LBIE's administration 8 of statutory interest, pursuant to rule 288.7 of the 9 Insolvency Rules 1986, is a payment of yearly interest 10 for the purposes of section 874.1 of the Income Tax Act 11 2007, such that it is capable of giving rise to 12 an obligation on LBIE and/or the joint administrators to 13 deduct a sum representing income tax, pursuant to and in 14 accordance with section 874.2 of the Income Tax Act 15 2007, such that the joint administrators should 16 consider, before paying statutory interest to any 17 particular creditor, whether or not any such obligation 18 in fact exists." 19 So the crunch point, at the end of the day, is 20 whether those proposed payments constitute yearly 21 interest, as that concept is understood in the relevant 22 tax legislation, and in particular, for the purposes of 23 section 874 of the Income Tax Act 2007. As 24 your Lordship will appreciate, I am a tax lawyer, I've 25 spent the whole of my life dealing with tax cases, and</p> <p style="text-align: center;">Page 3</p>
<p>1 LBIE was said to have precipitated the financial crisis 2 of 2008 and thereafter, but here we are today, when the 3 joint administrators have, at least as at 30 April 2014, 4 paid off at 100p in the pound, all the then proven debts 5 of LBIE, and there is now presently perceived to be 6 a surplus, estimated at between £6.6 billion and 7 £7.8 billion. As stated in paragraph 5 of our skeleton, 8 in consequence of that, the joint administrators are 9 contemplating making preparations for a distribution of 10 statutory interest, under rule 288.7 of the Insolvency 11 Rules 1986. This application is made in connection with 12 that, and as far as the documentation in this case is 13 concerned, there is -- fortunately, there is volume one 14 of the documents, which we call the core bundle, and 15 that I'm going to go to in a moment, although only very 16 briefly, which contains the application and the witness 17 statements, and I'll deal with those matters very, very, 18 very quickly because at the end of the day, this is 19 a question of law. The only documentation that I'm 20 going to refer to is that volume and the two volumes of 21 authorities. I have no intention of referring to 22 volumes 2, 3 and 4, I think, of the rest of the 23 documentation. So, therefore, unusually perhaps, for 24 cases that one's involved in these days, the 25 documentation isn't too bad.</p> <p style="text-align: center;">Page 2</p>	<p>1 at the end of the day, obviously I will deal with that, 2 but we apprehend the starting point in this case is one 3 of insolvency law, to determine what is the true nature 4 of statutory interest. We will say that, actually, 5 that's not going to cause any controversy in this 6 particular court, because the nature of statutory 7 interest has already been determined in this 8 administration by Mr Justice David Richards, as he then 9 was, in another application on behalf of my clients, the 10 joint administrators, in a case which we call Waterfall 11 IIA and the proper title to which is Lomas & Ors v 12 Burlington Loan Management, which is at tab 47 of the 13 second volume of the authorities -- I'm not going to go 14 to it now, I'll come to it later, and the relevant parts 15 of which, of course, we've already asked your Lordship 16 to have a look at. 17 MR JUSTICE HILDYARD: Yes, well in case it assists, with the 18 disclaimer that I shouldn't think I'd pass a Mastermind 19 quiz on it, I have read the 13 items that you asked me 20 to read, in case that helps you. 21 MR GARDINER: My Lord, very much so, yes, thank you. So as 22 I say, there are two points of law. The first being, if 23 I can call it this, a matter of insolvency law which we 24 say is determined already in that particular judgment. 25 I'll obviously take your Lordship to the relevant points</p> <p style="text-align: center;">Page 4</p>

<p>1 but you've obviously already read it. Then the second 2 point, which is much of the burden of my argument, is 3 what constitutes yearly interest for the purposes of 4 section 874, as that concept is understood in the tax 5 legislation. Your Lordship will appreciate that the 6 deduction procedure under 874 applies, because the 7 person making the payments would be a company, but it 8 applies only if it's yearly interest, and of course, 9 there may well be a number of exemptions and reliefs 10 which means the company doesn't have to duck the tax. 11 For example, there's the point we make in paragraph 12 12 of our skeleton. There are provisions in double 13 taxation conventions so, for example, if the money is 14 paid to a non resident, he may well not have 15 a liability. He then gets an order from the 16 Inland Revenue Commissioners which is served on my 17 clients, to the effect that they don't have to deduct 18 tax on making a payment to such a person. So there are 19 a number of exemptions and reliefs and we don't know the 20 extent to which this obligation would be applicable to 21 the payments out of statutory interest that would fall 22 to be made. Your Lordship will appreciate the judgment 23 in Waterfall IIA is under appeal to the Court of Appeal. 24 We say it's correct in all relevant respects, but at 25 least, in any event, as far as this case is concerned,</p> <p style="text-align: center;">Page 5</p>	<p>1 the background to the case, and then paragraphs 9 and 10 2 onwards, he refers to the surplus. Could I perhaps just 3 make this point: his witness statement was given on 4 22 December 2015. He refers to the latest progress 5 report in paragraph 9 of the joint administrators, as to 6 the then estimated apparent surplus, and we make the 7 point in our skeleton argument that that has actually 8 now been updated by the latest report by the joint 9 administrators, dated 12 April 2016, a figure of 10 6.6 billion to 7.8 billion, estimated as being the 11 amount of the surplus. That we refer to in our skeleton 12 at paragraph 5. I just make that as an update to what 13 he says in paragraph 9.</p> <p>14 Then paragraph 10, what he refers to as the final 15 dividend, at least as to the then proved debts, which 16 were distributed at 100P in the pound, on or about 17 30 April 2014. Then paragraph 12 sets out the other 18 impediments to making the distribution of surplus, and 19 I'm not going to go into those, but it is actually of 20 relevance in this case to the authorities, when we come 21 to them, to take on board the fact that this is 22 an administration, we are concerned with debts owed to 23 creditors, creditors who one apprehends, did not intend 24 to lend their money to LBIE for five years, or for any 25 period of time at all. They weren't making a long term</p> <p style="text-align: center;">Page 7</p>
<p>1 and we would obviously respectfully invite your Lordship 2 to follow it. In the light of the Revenue's skeleton, 3 at least at the moment, I don't apprehend that my 4 learned friends challenge the reasoning of the learned 5 judge in that case, although we will say that they do 6 not face up to the full rigour of his reasoning.</p> <p>7 So we say as far as 874.1 of the Income Tax Act is 8 concerned, that a distribution of statutory interest 9 would not constitute a distribution of yearly interest. 10 The Revenue say to the contrary. Obviously the joint 11 administrators wish to carry out their duties under the 12 insolvency rules, and the resolution of this dispute 13 would remove one of the major barriers to making such 14 distributions. That, of course, is why we're here 15 today.</p> <p>16 So having made the point that, essentially, the 17 dispute revolves around a question of law, could I very 18 briefly, just mention one or two points from the witness 19 statements. They are again in that core bundle, the 20 first bundle that we looked at just now. The first 21 witness statement is by Mr Downs, who is one of the 22 joint administrators. Tab 2 of the bundle. Obviously, 23 your Lordship having indicated that you've managed to 24 read this, I'm just going to take it very briefly. 25 Paragraphs 7 to 8, he refers to the administration and</p> <p style="text-align: center;">Page 6</p>	<p>1 or medium term or any kind of investment in LBIE. They 2 weren't investing their money for a return at interest 3 recurring over a period of time with LBIE. They are 4 caught up with the statutory consequences of LBIE having 5 gone into administration and the statutory moratorium 6 that has, in effect, applied. Therefore, whether you 7 look at it fortunately or unfortunately or unhappily, 8 they have been without their money for a very 9 considerable period of time, wholly unintended and not 10 as an intended investment, seeking a particular return 11 over that period of time on their money.</p> <p>12 MR JUSTICE HILDYARD: But it is common ground, is it not, 13 that whilst the question of what yearly interest, what 14 characteristics that has to have to qualify as such, the 15 payment made by way of statutory interest is interest?</p> <p>16 MR GARDINER: Yes. That is conceded throughout, yes. It's 17 interest. We say there, something I have to develop at 18 some length, I'm afraid, there is a distinction, we say, 19 between yearly interest and interest. One can see 20 that -- I'm afraid, I think all the years I've been in 21 practice, I don't think I've ever actually had to go, in 22 real seriousness, back to Addington's Act in 1803 but in 23 this case, I think I do. But there we are.</p> <p>24 But the point I'm making there is it is relevant, 25 when we come to look at the authorities and what they</p> <p style="text-align: center;">Page 8</p>

<p>1 say about the concept of yearly interest, that this is 2 not an intended investment, so as to procure a recurring 3 interest return over a period of time. They are caught 4 up in the maelstrom of the administration, through no 5 intention, no purpose to achieve that at all, they are 6 just statutory consequences.</p> <p>7 As you will see set out on page 4 in paragraph 12, 8 all these other various sort of impediments to the 9 distribution of surplus, and various other impediments 10 that obviously there have been over the years, in 11 getting in the monies and actually paying out the 12 amounts by way of 100 per cent of the amounts owed over 13 a period of some five to six years.</p> <p>14 At paragraph 14 onwards of Mr Downs' witness 15 statement, he notes the progress so far, in resolving 16 those issues, and again, on the basis that your Lordship 17 has read it, I don't propose to read any of that to you. 18 Then we go to paragraphs 19 to 22, which refers to 19 section 874, which is the statutory provision relevant 20 here, of the Income Tax Act 2007, and the correspondence 21 with the Revenue. One can see set out at paragraph 25, 22 if one goes on to paragraphs 23 onwards, the Revenue's 23 stated guidance that my clients, the joint 24 administrators and all on their behalf, 25 PricewaterhouseCoopers, corresponded with the Revenue,</p> <p style="text-align: center;">Page 9</p>	<p>1 MR GARDINER: My Lord, that's right, when you take that into 2 account with the insolvency rules, yes. So if this were 3 an insolvency in the form of a liquidation, or 4 an administration, the same point arises.</p> <p>5 MR JUSTICE HILDYARD: What is the effect of INS 743.3, is 6 that simply a concession or is it an interpretation, or 7 what is it?</p> <p>8 MR GARDINER: The effect of?</p> <p>9 MR JUSTICE HILDYARD: INS 743.3.</p> <p>10 MR GARDINER: Sorry, yes. That is just simply what was 11 published by the Inland Revenue Commissioners at the 12 time, as being their understanding, or their perceived 13 understanding of the law. What Miss Rass says in her 14 witness statement is that shouldn't really be published, 15 that was really an internal guidance note that if and 16 insofar as people were paying money to the 17 Inland Revenue Commissioners themselves, that would 18 apply, but it wouldn't apply generally.</p> <p>19 MR JUSTICE HILDYARD: So it was published but in error?</p> <p>20 MR GARDINER: That's right.</p> <p>21 MR JUSTICE HILDYARD: And now what is said, as I understand 22 it, is it may apply in liquidations but it does not 23 apply in administrations?</p> <p>24 MR GARDINER: No, I think what they say is it doesn't apply 25 at all unless you're actually making a payment of</p> <p style="text-align: center;">Page 11</p>
<p>1 and one sees it set out there and perhaps I'll just read 2 it very briefly:</p> <p>3 "25. The insolvency legislation provides that where 4 the IP [the insolvency practitioner] has a surplus of 5 money remaining after full payment of all creditor's 6 preferential and non-preferential debts claimed in the 7 insolvency, then interest at a prescribed rate must be 8 paid on those debts, from the relevant date or the 9 reckonable date, for interests purposes, under the Taxes 10 Management Act 1970, whichever is the later, to the date 11 of payment of the claim. Payment of interest is made by 12 the IP under the Insolvency Act 1986, section 189 in 13 liquidation bankruptcy provisions."</p> <p>14 Then it says:</p> <p>15 "There is no obligation or right for the IP 16 [insolvency practitioner] as a payer to deduct income 17 tax for a low interest payment."</p> <p>18 So that was the published statement of Her Majesty's 19 Revenue and Customs. The point was taken up on behalf 20 of the joint administrators with the Revenue, and the 21 Revenue at first said, "Yes, you don't have to deduct 22 tax."</p> <p>23 MR JUSTICE HILDYARD: And section 189, and in particular, 24 subsection 2, is in exactly the same terms as 288; is 25 that right?</p> <p style="text-align: center;">Page 10</p>	<p>1 interest to the Inland Revenue Commissioners.</p> <p>2 MR JUSTICE HILDYARD: Yes.</p> <p>3 MR GARDINER: And I think that's right. Yes, that is their 4 position.</p> <p>5 MR JUSTICE HILDYARD: So they publish for their own benefit?</p> <p>6 MR GARDINER: Yes, they published that in error.</p> <p>7 MR JUSTICE HILDYARD: I see.</p> <p>8 MR GARDINER: They published it, my clients took it on the 9 basis that that means there is no obligation to deduct 10 tax. They agreed at first, they agreed at second 11 attempt, "Yes, you don't have to deduct tax", then third 12 attempt, they said "No, we've got it wrong, it was 13 issued in error. The view we made was issued in error 14 and the right answer is you have to deduct tax".</p> <p>15 MR JUSTICE HILDYARD: I mean, it's disquieting, I have to 16 say, but I'm really asking for the purpose of the scope 17 and effect of what I'm asked to decide. Is it common 18 ground that the same interpretation must be given to 19 statutory interest and yearly interest in the context of 20 189.2 as in 288.7, so that the effect would be that any 21 order made by the court, subject of course to appeal, 22 would apply in all insolvency processes?</p> <p>23 MR GARDINER: My Lord, yes. That is our position. As 24 I understand it, that is their position.</p> <p>25 MR JUSTICE HILDYARD: Their position?</p> <p style="text-align: center;">Page 12</p>

<p>1 MR GARDINER: Yes.</p> <p>2 MR JUSTICE HILDYARD: That if it was a debt owed to the</p> <p>3 Revenue, some different position would still obtain?</p> <p>4 MR GARDINER: My Lord, yes, that is their position, yes.</p> <p>5 MR JUSTICE HILDYARD: I see.</p> <p>6 MR GOY: My Lord, maybe I can come back to that when it's my</p> <p>7 turn.</p> <p>8 MR JUSTICE HILDYARD: Yes, thank you, Mr Goy.</p> <p>9 MR GARDINER: Yes, my learned friend Mr Bayfield just</p> <p>10 reminds me, perhaps helpfully, that in Waterfall IIA,</p> <p>11 paragraph 15 -- I don't need to take you to it now,</p> <p>12 I can just read it -- paragraph 15, at the end of</p> <p>13 paragraph 15 of Mr Justice David Richards' judgment, he</p> <p>14 says -- this is referring to the court committee and its</p> <p>15 recommendations -- he says:</p> <p>16 "An important purpose was to introduce a uniform</p> <p>17 regime for interest in all insolvency proceedings,</p> <p>18 including interest, for periods after the commencement</p> <p>19 of the insolvency proceedings."</p> <p>20 MR JUSTICE HILDYARD: Well that's partly -- I spotted that</p> <p>21 in paragraph 15, and I was intrigued to know the scope</p> <p>22 of what is put by the Revenue in that regard.</p> <p>23 MR GARDINER: Your Lordship has it, as I understand it,</p> <p>24 entirely correctly, that the position is the same in</p> <p>25 a liquidation as in an administration. They say that</p> <p style="text-align: center;">Page 13</p>	<p>1 burden of Miss Rass' witness statement, and she sets out</p> <p>2 all the various statements made out by Her Majesty's</p> <p>3 Revenue and Customs in the appendices to her statement.</p> <p>4 I'm not going to take you to any of those.</p> <p>5 MR JUSTICE HILDYARD: Right, okay. I'll read those again.</p> <p>6 MR GARDINER: The point is at the end of the day, this</p> <p>7 matter is a question of law. The only point I'm trying</p> <p>8 to make at the moment is that that correspondence, that</p> <p>9 mistaken view, has led to this case not coming on,</p> <p>10 perhaps, as early as it might have done in the course of</p> <p>11 the administration. Had that view not been taken,</p> <p>12 perhaps we would have been here, arguing about this two</p> <p>13 years ago. There we are.</p> <p>14 There are one or two points I would like to make,</p> <p>15 and one point in particular, on Miss Rass' statement,</p> <p>16 and this is just for clarification. It's her statement,</p> <p>17 if I can go to, which is at tab 4, and it's in</p> <p>18 particular, paragraph 12. Just before, at paragraphs 8</p> <p>19 to 12, it's just the terminology she used and I just</p> <p>20 want to clarify this, because I think the terminology</p> <p>21 she's used, if I can put it at its mildest, is</p> <p>22 unfortunate. In paragraph 8, if your Lordship has it</p> <p>23 behind tab 4 --</p> <p>24 MR JUSTICE HILDYARD: Yes.</p> <p>25 MR GARDINER: -- she says:</p> <p style="text-align: center;">Page 15</p>
<p>1 it's yearly interest if there is a calculation period</p> <p>2 more than 12 months. We say it's not yearly interest.</p> <p>3 The only exception as far as they're concerned, is if it</p> <p>4 were monies payable to the Inland Revenue Commissioners,</p> <p>5 then you wouldn't have to deduct tax under 874 in those</p> <p>6 circumstances.</p> <p>7 MR GOY: Could I just interrupt. There is a reason for</p> <p>8 that, there is a statutory provision that has that</p> <p>9 effect.</p> <p>10 MR GARDINER: Yes, I'm not disputing it.</p> <p>11 MR JUSTICE HILDYARD: Has this therefore been recalled, this</p> <p>12 INS -- it's been wiped off the face of the public map,</p> <p>13 has it?</p> <p>14 MR GARDINER: Yes, it's been recalled. It is right to say</p> <p>15 it was published. It wasn't a mistake that it was</p> <p>16 published, it was published. I think what the other</p> <p>17 side say is the position stated in it is mistaken,</p> <p>18 because they say it wasn't intended to apply generally.</p> <p>19 MR JUSTICE HILDYARD: When was it published?</p> <p>20 MR GARDINER: Originally, I can't remember, I'm sorry.</p> <p>21 MR JUSTICE HILDYARD: In due course, someone will tell me.</p> <p>22 MR GARDINER: We'll find out. When it had been withdrawn on</p> <p>23 behalf of the Commissioners, they actually said "Yes,</p> <p>24 but it's still our position", but then subsequently said</p> <p>25 "No, no, the statement was made in error." That's the</p> <p style="text-align: center;">Page 14</p>	<p>1 "I stated the Revenue's position that a withholding</p> <p>2 tax obligation arises under section 874."</p> <p>3 Then she goes on, just four lines down:</p> <p>4 "As I explained below, if such a withholding tax</p> <p>5 obligation does not apply to the payments of statutory</p> <p>6 interest, HMRC will have no means of recovering any</p> <p>7 income tax in respect of those sums for the numerous</p> <p>8 creditors of LBIE and/or the assignees of such creditors</p> <p>9 who are not resident in the UK at the time of receipt."</p> <p>10 Now just as a matter of clarification, that</p> <p>11 terminology of recovering any income tax, presupposes</p> <p>12 that there is a liability, and one is seeking to recover</p> <p>13 the tax in respect of a liability.</p> <p>14 MR JUSTICE HILDYARD: Well you make the point in your</p> <p>15 skeleton that this is simply the policy of the Treasury</p> <p>16 and the legislature, that this is the way of things.</p> <p>17 MR GARDINER: My Lord, I just wanted to get over that point</p> <p>18 and draw attention to it. When she goes on at</p> <p>19 paragraph 12, talking about a loss to the Exchequer and</p> <p>20 all the rest of it, the loss to the Exchequer is no</p> <p>21 different in legal liability terms than the loss to the</p> <p>22 Exchequer, if you might like to describe it as such,</p> <p>23 being in a sense, that the UK income tax does not</p> <p>24 actually extend to the Australian income of</p> <p>25 an Australian resident, it's simply outside the charge.</p> <p style="text-align: center;">Page 16</p>

<p>1 In consequence to the statutory provisions, we don't 2 seek to charge non-residents in respect of UK source 3 income that is not subjected to tax by deduction at 4 source. 5 MR JUSTICE HILDYARD: Where she says, although if you prefer 6 Mr Goy to answer on her behalf, that's understandable, 7 where she says it's "in practice limited to some", 8 that's not in practice, that's by law? 9 MR GARDINER: That's by law, my Lord, that's the point, yes. 10 It's the terminology of "recovery, practice, loss to the 11 Exchequer." It's all absolutely irrelevant because 12 Parliament, in its wisdom in 1995, expressly by statute 13 said, "We are not going to charge to tax, this type of 14 income." And therefore there's no liability and we 15 merely say, and it's the point that your Lordship 16 obviously picked up from paragraph 12 of our skeleton, 17 that that's inappropriate language, we say. 18 Essentially, there is no liability as a matter of law 19 and that's it. So the crunch question is, is this 20 yearly interest or not, and that will determine whether 21 for a non resident, that is the liability or not, as the 22 case may be. 23 So that's all I want to -- you will also see in 24 a minute, I'm sure you obviously have read all the 25 documentation -- my instructing solicitors raised</p> <p style="text-align: center;">Page 17</p>	<p>1 So that, I hope, from my point of view at least, is 2 the last time I'll refer to what is called the core 3 bundle, volume 1, and thereafter I'm intending to go on 4 to the legislation and the cases, but I thought it might 5 be the most helpful way to proceed, if I could indicate 6 at the outset what I will call, perhaps, the heart of 7 our case and lead up to, perhaps, submissions which in 8 a sense, I might make at the end of our opening address. 9 But I thought it might be helpful, in looking at the 10 authorities which are not necessarily the easiest to 11 look at, if I indicated from the outset, as it were, the 12 signposts that I think are important in the legislation 13 and from the authorities. If you would allow me just to 14 develop that a little. This goes, really, to what we 15 say is at the heart of our case. That is dealing with 16 the term "yearly interest". As I think I said a moment 17 ago, that first appeared in our tax legislation in 1803, 18 what we refer to as Addington's Act. Income tax was 19 first introduced by Pitt in 1799. This is the time of 20 the revolutionary wars in France and the Napoleonic wars 21 and all the rest of it. Pitt's Act was a bit of a damp 22 squib, it didn't produce very much. 1803 is the 23 foundation of our income tax. It's almost remarkable to 24 me, when I look back at it, the structure actually was 25 introduced in 1803. It introduced the scheduler system,</p> <p style="text-align: center;">Page 19</p>
<p>1 certain questions as to the accuracy of a number of 2 points that Miss Rass made in her statement at tab 4, 3 and she put in a second witness statement which is at 4 tab 8, clarifying certain points. In particular, 5 I would perhaps make the point that in her first witness 6 statement, she referred to some £1.2 billion of tax, et 7 cetera, and she accepted, as we accepted, that 8 potentially, there might be significant sums but nobody 9 actually knows. 10 MR JUSTICE HILDYARD: So I cannot be updated as indicated. 11 Yes. 12 MR GARDINER: Yes. 13 MR JUSTICE HILDYARD: Except as to the aggregate amounts of 14 the anticipated surplus. 15 MR GARDINER: That's right, my Lord, nobody's made any 16 calculation as to how many non-residents would be owing 17 a particular interest, et cetera, and the rest of it, we 18 just do not know, but it would be inappropriate to say 19 there's £1.2 billion of tax at stake. 20 MR JUSTICE HILDYARD: I suppose it could change from day to 21 day, if the debt is dealt with. 22 MR GARDINER: Absolutely. That's perhaps one reason why 23 it's not particularly important or necessary to make 24 a calculation today because that calculation might be 25 wholly inaccurate in six months' time.</p> <p style="text-align: center;">Page 18</p>	<p>1 it introduced terms which to a tax lawyer, are in one's 2 bones, in a sense, of it talks about "income arising or 3 accruing", and the word "accruing" is actually rather 4 important, as we'll see when we look at the cases. It 5 also introduced, in section 208 of the Income Tax Act of 6 1803 -- 7 MR JUSTICE HILDYARD: Which section was it? 8 MR GARDINER: 208, my Lord. 9 MR JUSTICE HILDYARD: It's always said, London is to 10 Paddington what Pitt is to Addington. 11 MR GARDINER: Yes, very good. 12 MR JUSTICE HILDYARD: But not in the context of tax. 13 MR GARDINER: We have them all, actually. All the great 14 prime ministers of that particular period of time. 15 We'll come on to 1842, when income tax, having been 16 abolished in 1816 -- there was a wonderful period of 17 time, 1842, it's reintroduced by Pitt and 1852, 18 Gladstone wants to get it on the act and he introduces 19 his Income Tax Act in 1853. 20 As I say, this has a long provenance, yearly 21 interest. It's introduced in that particular provision 22 and it's introduced in circumstances where it allows the 23 payer to deduct tax at source, on making a payment of 24 yearly interest. It's that provision, section 208, 25 which is the provision from which our section 874 is</p> <p style="text-align: center;">Page 20</p>

<p>1 ultimately derived and from which we get the term 2 "yearly interest". I'll come to the precise terms of 3 the historic analysis, because we've set that out in the 4 appendix to our skeleton, in perhaps more detail, in 5 a moment, but just for the moment, that is the starting 6 point. It's the starting point where there are two 7 features that are of interest. One is at the time, 8 interest generally, apart from yearly interest, was not 9 charged to tax. There's no dichotomy in the 1803 Act 10 between yearly interest and interest. Although 11 interest, in general, is actually brought into charge in 12 1805. But the other and perhaps more significant 13 feature is that yearly interest is brought in in 14 connection with two other items. I think your Lordship 15 will have seen but we'll see when we look at the 16 legislation. It's brought in with annuities and other 17 annual payments, and as the authorities establish, that 18 must mean that yearly interest constitutes a form of 19 annual payment.</p> <p>20 MR JUSTICE HILDYARD: That's a sort of eiusdem generis 21 construction, is it?</p> <p>22 MR GARDINER: My Lord, yes. We can see it in all the early 23 cases that I'll take you to, but <i>Bebb v Bunny</i>, <i>Goslings</i> 24 and subsequently, Lord Maugham in the House of Lords. 25 Because it says "other annual payments", it must mean</p> <p style="text-align: center;">Page 21</p>	<p>1 this point now. Your Lordship will appreciate they were 2 introducing something really quite new and novel in 1799 3 and 1803, a new income tax, a tax on people's personal 4 income. Never been done before. They were concerned, 5 as the government, in not having to, as it were, 6 interfere into taxpayer's affairs, in not having to make 7 demands of a taxpayer in respect of his income, and the 8 really rather clever way in which they did it was, and 9 this is the fundamental basis of <i>Addington's Act</i>, was 10 deduction of tax at source. So, in effect, they put 11 an obligation or a power, an authority on the payer of 12 the income, to deduct tax at source. And that meant 13 that, firstly, they avoided having to make direct 14 assessments by the government, which of course meant 15 that the costs of collection and all the rest of it, 16 were much reduced, and secondly, of course, they avoided 17 the opprobrium of having to make assessments against the 18 individual who was liable, in respect of his income tax 19 liability. So that was the purpose of it, and that 20 purpose was something to which -- it applied to yearly 21 interest, annuities and annual payments, but not to any 22 other form of interest. And, again, from the outset, as 23 we shall see when we look at the 1803 Act, it's using 24 this phrase which will recur and was retained for some 25 200-odd years, of "income arising or accruing".</p> <p style="text-align: center;">Page 23</p>
<p>1 that those items before that, yearly interest and 2 annuities, are simply particular forms of an annual 3 payment. To any tax lawyer, we could look at all the 4 authorities, but I don't think we need to, because those 5 are probably sufficient. Once an annual payment is in 6 one's bones, in a sense, it's a recurring thing, going 7 on year by year or capable of going on year by year, 8 it's something of some permanence. It's not 9 a one-off-type thing. Annual payments recur or are 10 capable of recurring year by year.</p> <p>11 So the original concept in 1803 was of an ongoing 12 continuing right to which we submit it was appropriate 13 to apply the principle and procedures of allowing the 14 payer to deduct income tax, on account of the payee's 15 liability, on an ongoing basis.</p> <p>16 MR JUSTICE HILDYARD: And it's sufficient, is it, if it's 17 capable of recurring rather than intended to be 18 recurring year by year?</p> <p>19 MR GARDINER: My Lord, that's right, that's the case of <i>Bebb</i> 20 <i>v Bunny</i>. I'll come to it in detail in a moment, but as 21 a matter of law, that is correct.</p> <p>22 MR JUSTICE HILDYARD: Capable.</p> <p>23 MR GARDINER: Yes. But the point about the ongoing 24 collection machinery, and to put this in focus, we can 25 see it when we look at our appendix but I'll just make</p> <p style="text-align: center;">Page 22</p>	<p>1 So it's the meaning of these words in their context 2 that lies at the heart of the dispute in this case. If 3 one just thinks in semantic terms, if one thinks of the 4 words, I mean they're familiar words in ordinary 5 parlance. "Yearly", we submit, means something year by 6 year. If one needs any judicial definition of 7 "interest" -- again, at the heart of tax lawyers, 8 Mr Justice Rowlatt was the great tax lawyer, the great 9 tax judge of the earlier part of the 20th century for 10 some sort of 25 years, and he, in a case called <i>Bennett</i> 11 <i>v Ogston</i> which is otherwise of no relevance to us, but 12 famously defined interest as being "the payment by time 13 for the use of money." So "yearly", year by year, 14 payment by time for the use of money.</p> <p>15 We say that within the meaning of those words, what 16 the cases have identified is the essential qualities of 17 yearly interest to which the deduction source provisions 18 applied. It must have some degree of permanence, some 19 ongoing effect, demonstrating that it has been paid for 20 the use of money over a period of time. And over that 21 period of time, the interest accrues, providing, of 22 course, it is presently payable, either now or due in 23 the future. Because unless it is presently payable now 24 or in the future, there is nothing to accrue. (Pause)</p> <p>25 If I could just perhaps illustrate that by a very</p> <p style="text-align: center;">Page 24</p>

<p>1 simple example. Suppose I agree to lend my learned 2 friend, Mr Goy, £1,000 for five years, at a rate of 3 interest of 12 per cent per annum. That's no aspersion 4 as to his creditworthiness or whatever, it's simply for 5 the sake of an example. So I agree to lend him for 6 a number of years, let's say five years, £1,000 at 7 12 per cent per annum, and interest is payable -- it 8 doesn't matter whether it's quarterly, half yearly or 9 yearly or whatever, interest is provided for, to be 10 payable at some point. Now the interest on that debt 11 accrues day by day, and in the terminology of the case 12 of <i>Bebb v Bunny</i>, <i>de die in diem</i>, day by day. So on 13 a simple basis, looking at for example, a period of a 14 month, £10 will have accrued over the first month, and 15 then another £10 on the second month, and so on. But 16 the interest is only payable as and when it is payable. 17 But because of those contractual circumstances, the 18 interest accrues during that period of time. I think as 19 I've already said, it's self evident that it cannot 20 accrue unless it is payable at some point in time. We 21 say it's an essential element of yearly interest that 22 there exists an obligation to pay interest at some time, 23 now or in the future, and that such an obligation is 24 present during the time that the interest accrues 25 because without that, interest does not accrue.</p> <p style="text-align: center;">Page 25</p>	<p>1 has sufficient permanence, as it does in my example, it 2 constitutes yearly interest. The interest on it 3 constitutes yearly interest. 4 The point I'm making is that one will see in the 5 cases, there are a number of strands identifying the 6 same simple concept. When one starts, and can see 7 virtually all of it in the decision in <i>Bebb v Bunny</i> 8 which is the first case on this, but one can see it in 9 the subsequent cases, where they're looking at 10 an obligation giving rise to such interest as being 11 something in the nature of attaching to real property. 12 <i>Bebb v Bunny</i> itself, the vice chancellor in that case 13 was assimilating the indebtedness in that case to a real 14 property right, the unpaid property slightly(?) being 15 assimilated, in his judgment, to a mortgage. One can 16 see it in some of the other cases we refer to, and I'll 17 take your Lordship to them in detail later, but if 18 I just mention a run of them at the moment. We refer at 19 paragraphs 29 and 30 to the decision of 20 Mr Justice Rowlatt in a case called <i>Garston v Carlisle</i>. 21 We quote what he says about it, "form of investment". 22 <i>Re Cooper</i>, a decision of the Court of Appeal on judgment 23 debts, the Master of the Rolls, Lord Cozens-Hardy, says 24 this isn't the kind of yearly interest that was 25 intended, and then in particular, Lord Sumner, again in</p> <p style="text-align: center;">Page 27</p>
<p>1 The legislation, when it's looking at yearly 2 interest, is looking to the type of indebtedness that 3 produces such interest. And as some of the cases -- 4 we'll see this, it's the thread running through lots of 5 the cases -- some of the cases identify it as interest 6 on an investment. The situation of a person who has 7 passed out money to another over a period of time in 8 which interest accrues and is payable periodically. The 9 legislation used the terms "arises and accrues" for some 10 200 years. Yearly interest accrues in those 11 circumstances, but per contra, a one month calculation 12 in respect of a past period, does not create interest 13 which accrues. That interest merely arises, it has 14 never accrued. That's because it is the creature of 15 something which wasn't intended, within the legislation, 16 to constitute yearly interest. It's merely 17 a calculation at a moment of time. It's not the type of 18 ongoing obligation that was intended to create accruing 19 yearly interest. 20 So interest accruing is being earned, earned by the 21 creditor, and incurred by the debtor, day by day, 22 throughout a period. As a creditor, I'm earning 23 interest day by day, my learned friend is incurring 24 interest day by day. I'm earning the accruing debt, and 25 he is incurring the accruing liability. If that debt</p> <p style="text-align: center;">Page 26</p>	<p>1 the Court of Appeal, in <i>Gateshead Corporation v Lumsden</i> 2 which we refer to at paragraph 28. So that's a flight 3 of cases, looking at it on the basis it has to be some 4 kind of investment giving rise to this type of interest, 5 the interest that accrues over a period. That's the way 6 in which they look at it there, and there are a number 7 of Scottish cases, but two in particular that we refer 8 to, where they refer to the similar concept of there 9 being a tract of future time. So interest accruing as 10 a tract of future time. We submit, and that's why, in 11 opening the case, I'm giving this sort of guidance, in 12 a sense, to the authorities. We submit they're all to 13 the like effect of recognising the concept that gives 14 rise to yearly interest. We say this: that as I'm sure 15 your Lordship will have seen, my learned friend's 16 argument is that it all comes down to a period of 17 calculation. That's what they said in their letter of 18 2 March, and I'll come to that later, 2 March of this 19 year. That is, to put it shortly, what they're saying, 20 at least as their primary argument in their skeleton. 21 If you have a period of calculation of a year or more in 22 these circumstances, you're yearly interest; if less, 23 you're not. That's their position. If that were right, 24 that no doubt should have been the basis on which all 25 those cases in the 19th and 20th century should have</p> <p style="text-align: center;">Page 28</p>

7 (Pages 25 to 28)

<p>1 been decided. None of them were decided on that basis. 2 So their submission before your Lordship is completely 3 contrary to that whole line of authority. 4 In particular, and we would attach perhaps, the 5 greatest importance in this particular case to the 6 decision of the Court of Appeal in Gateshead Corporation 7 v Lumsden. I refer to the previous Court of Appeal 8 decision, and there are two of them, in re Cooper and 9 Goslings, et cetera, but Gateshead v Lumsden in 10 particular, we attach a great deal of significance to, 11 because in our submission, the argument put in that 12 particular case, and rejected by the Court of Appeal, is 13 the very same argument that's being put by my learned 14 friends in this particular case, and it was rejected. 15 MR JUSTICE HILDYARD: I mean you say forbearance and 16 a moratorium are very similar. 17 MR GARDINER: Yes. We say, if you actually understand 18 Gateshead v Lumsden and what Lord Sumner was saying, 19 he's saying it's forbearance, it's exactly the same, we 20 say, as a matter of quality. And here there is 21 a moratorium. It's an enforced forbearance in a sense, 22 but it is a forbearance, an unintended consequence, 23 giving rise to a calculation, and it's not within the 24 context of yearly interest accruing over a period of 25 time, intended. As I said in opening, these creditors</p> <p style="text-align: center;">Page 29</p>	<p>1 relate to the heart of the case. I thought, having said 2 that, if I could give your Lordship five, relatively 3 short propositions which we say are decisive of this 4 case. Ordinarily, I'd give them at the end of my 5 argument, and this is in anticipation of looking at the 6 authorities and the cases, but I think it might be 7 helpful to give them now. Fortunately, they are fairly 8 short. 9 The first is this: that to have yearly interest, 10 there must be an obligation to pay interest, now or some 11 time in the future, in respect of a period during which 12 the same accrues. That period needs at least to be 13 capable of being for a year or more. 14 Secondly, and following on from that, a period of 15 accruer is a necessary constituent of yearly interest. 16 (Pause) 17 Thirdly, interest does not accrue during a period 18 when there is no obligation to pay the same, even though 19 such an obligation might arise in the future. 20 That follows here, in relation to statutory interest 21 and the judgment of Mr Justice David Richards in 22 Waterfall IIA, in particular, paragraphs 149 and 154. 23 Fourthly, if, as in the present case, any 24 entitlement to interest only arises on or after the 25 repayment of the principal, then it cannot be yearly</p> <p style="text-align: center;">Page 31</p>
<p>1 did not intend to lend this money on a particular basis, 2 over the period of time that it's taken. 3 We do say, and I say it's an absolutely crunch point 4 in this particular case. If learned friend's argument 5 is right, he has to submit that Gateshead v Lumsden is 6 wrong, and with the greatest respect, before 7 your Lordship, he can't say that. It's a decision of 8 the Court of Appeal. 9 Then finally, or just to wrap up the opening, we 10 then come back to the decision of Mr Justice David 11 Richards. He's already held that the interest in this 12 particular case does not accrue at all. It does not 13 accrue over a period, it doesn't accrue at all, it 14 simply arises at a point of time, on the identification 15 of a surplus. There's no tract of future time. It 16 cannot be said that it arises from an investment or 17 loan, intended to subsist for any period. These 18 creditors have simply been caught up by the 19 administrative process. They weren't making loans 20 invested in LBIE for any period of time. The length of 21 time that they remain outstanding and any interest 22 payable is simply either a fortuitous or unhappy 23 consequence of the forced administration, as far as they 24 are concerned. 25 So all those points, in my respectful submission,</p> <p style="text-align: center;">Page 30</p>	<p>1 interest, there is no accruer or continuation of the 2 interest, there is merely a one-off obligation 3 calculated by reference to a past period. (Pause) 4 Then fifthly and lastly, we say the period of 5 calculation cannot be the discrimen. In that regard, we 6 particularly draw attention to the case of Gateshead v 7 Lumsden, where the interest was paid for many years. 8 Sadly, we don't know how long, it might even have been 9 30, but for many years, but it was still held not to be 10 yearly interest. Another case is where the interest is 11 paid for less than a year but it is still held to 12 constitute yearly interest. 13 MR JUSTICE HILDYARD: So points one to four are necessary 14 qualities, point five is not a necessary quality? 15 MR GARDINER: Yes. 16 MR JUSTICE HILDYARD: Yes. Just as it occurs to me, I'm 17 going to ask it in case later, I dwell on it, 18 a preference right would probably qualify for one, two 19 and three but possibly not four? 20 MR GARDINER: Yes. 21 MR JUSTICE HILDYARD: A preference share right? 22 MR GARDINER: Yes. Because there is a right there to which 23 is -- well, the only point, if it were a fixed 24 preference share, then yes, because it gives rise to 25 a right and the interest would accrue on it over</p> <p style="text-align: center;">Page 32</p>

<p>1 a period of time. The company might default in not 2 paying it or whatever, but the amount of interest would 3 be accruing over that period of time. 4 MR JUSTICE HILDYARD: Yes, because it wouldn't be 5 an absolute obligation to pay. 6 MR GARDINER: No. 7 MR JUSTICE HILDYARD: I'm just wondering how a preference 8 share fits in. You would accept that the coupon payable 9 on a preference, to try and use a neutral term, would or 10 could be yearly interest, except for the fact that it 11 doesn't arise after payment of principal? 12 MR GARDINER: Well, first of all of course, it's not debt, 13 I mean in strict terms it's a dividend, so therefore, 14 we're only talking in terms of analogy. But if it were 15 a fixed rate preference share upon which five per cent 16 per annum were payable, yes, then it would satisfy the 17 accruer concept. If it were a situation whereby -- say 18 you were talking about ordinary shares, then of course, 19 you wouldn't get any kind of accruer at all, because the 20 only right of an ordinary share would be once a dividend 21 is actually paid. 22 MR JUSTICE HILDYARD: Yes. But subject to your debt point, 23 the preference share, the obligation to pay, is only if 24 there's a declaration dividend to that effect? 25 MR GARDINER: Yes, but that's why I'm making the point that</p> <p style="text-align: center;">Page 33</p>	<p>1 contrary to the ratio of the Court of Appeal in 2 Gateshead v Lumsden. When we come to look at that case 3 in detail, we will see that the argument advanced in 4 that case was in all essentials, the same as the 5 principal argument advanced in this case on behalf of 6 the Revenue. It was rejected by the Court of Appeal. 7 Therefore, in our respectful submission, the position is 8 quite plain. In any court below the Supreme Court, this 9 point is actually covered by binding authority, of that 10 case in particular. (Pause) 11 So, my Lord, having said that, if I might then go to 12 our skeleton and develop the argument from that, because 13 obviously, I need to show your Lordship the legislation 14 that I briefly referred to, and the cases. If I could 15 then look at our skeleton. I'll simply take 16 paragraphs 1 to 12 as read, dealing with the facts and 17 witness statements, et cetera, and obviously, I'm 18 grateful your Lordship's had time to read all that 19 material. Paragraphs 13 to 16 deal with statutory 20 interest, in particular, dealing with rule 288.7 and 21 dealing with the judgment of Mr Justice David Richards 22 in Waterfall IIA. I'd like to deal with that after I've 23 dealt with the tax legislation, if I might. I think 24 that might be the most helpful way in which I can 25 develop it.</p> <p style="text-align: center;">Page 35</p>
<p>1 if it were a fixed rate preference share accruing over 2 a period of time, so the company had to pay it, insofar 3 as it had profits to do so -- 4 MR JUSTICE HILDYARD: Right. 5 MR GARDINER: -- then the amount would accrue over a period 6 of time. If it's purely discretionary, then it 7 wouldn't. But I mean that is assuming, of course, there 8 is a debt, and there wouldn't be, because it's 9 a preference share. But I accept your Lordship's point 10 that it's just a matter of analogy. But as I said, just 11 finishing off, if I might, my fifth point and 12 fortunately, my last one here, I referred to Gateshead v 13 Lumsden, with interest payable for many years but still 14 held not to be yearly interest, and then the other cases 15 where the interest is paid for less than a year but it's 16 still held to constitute yearly interest. That's 17 following the principle in <i>Bebb v Bunny</i>. In both 18 instances, the calculation period is not the discrimen 19 to determining whether it's yearly or not. It's the 20 qualities that do, it's the period of accruer, and 21 contemplated accruer that does. So we say that the 22 contentions of the Revenue in this case are contrary to 23 that whole line of authority which is referred to in our 24 skeleton between paragraphs 20 and 36, and I'll take 25 your Lordship to that later. But in particular, we say</p> <p style="text-align: center;">Page 34</p>	<p>1 The tax legislation starts at paragraph 17 of our 2 skeleton. There we set out section 874.1 and 2. 3 I don't think I need take you to it, but it's at tab 12 4 of volume 1 of the authorities that I think for our 5 purposes, we've simply reproduced it in paragraph 17, 6 which I think ought to be sufficient for present 7 purposes. So the section applies if a payment of yearly 8 interest arising in the United Kingdom is made. We make 9 the point here, and perhaps the point I make on the 10 history, that the tax law rewrite project, which some 11 think was a great boon and some of the rest of us think 12 was a bit of a disaster really, losing some of that 13 which had been built up over a long period of time, made 14 certain changes to our terminology, being for the better 15 understanding of -- I think the man in the street was 16 the idea. And, therefore, the terminology "arising and 17 accruing", which had lasted for over 200 years, from 18 1803, is simplified into "arising" from 2005 onwards. 19 Which we have in 17, one can see, 874.1: 20 "This section applies if a payment of yearly 21 interest arising ..." 22 So the old provision about deduction of tax at 23 source, was talking about "arising or accruing". The 24 point taken about the tax law rewrite project was that 25 "arising" will have encompassed "arising and accruing",</p> <p style="text-align: center;">Page 36</p>

<p>1 so therefore "arising" is a simpler term. But anyway, 2 there we have 874. I would then like to commence, 3 really, with historical analysis which we've set out in 4 the appendix to our skeleton which we refer to in 18 and 5 which I've briefly touched on, because one can see the 6 way in which the concept was dealt with in the 7 legislation over the years from that development. If 8 one could then refer to the appendix to our skeleton. 9 We refer at paragraphs 1 and 2 to Pitt's Act, but 10 I don't think I need take you to that at all. 11 Paragraph 3, referring to Addington's Act and it's the 12 point I made about section 208 already. We say in 13 paragraph 3: 14 " ... introduced the principle of deduction of tax 15 at source, as well as the scheduler system." 16 The two most fundamental parts of our income tax 17 system: 18 "Interest on money was not one of the scheduled 19 sources of income, however ..." 20 And here is the phrase which we reproduced but I'll 21 take you to the legislation: 22 " ... annuities, yearly interest of money or other 23 annual payments, whether the same shall be received and 24 payable half yearly or any shorter or more distant 25 periods were expressly charged by section 208 of the</p> <p style="text-align: center;">Page 37</p>	<p>1 that introduced the preceding year basis. If one needs 2 to pick it up, it's eight-odd lines down: 3 "Profits or gains in the preceding year." 4 MR JUSTICE HILDYARD: Yes. 5 MR GARDINER: So there one can see Addington's Act. Then 6 behind tab 14 is the particular provision that we say is 7 the antecedent of the provision we're concerned with, 8 874, here. That's just below the middle of the page, 9 the second break on that page. There one sees in Roman 10 numerals, section 208. Perhaps if I just read that out: 11 " ... and be it further enacted that upon all 12 annuities, yearly interest of money or other annual 13 payments, whether such payments shall be payable within 14 or out of Great Britain, either as a charge on any 15 property of the person or persons paying the same, or as 16 a reservation thereafter, or as a personal debt or 17 obligation, by virtue of any contract, or whether the 18 same shall be received and payable half yearly or at any 19 shorter or more distant periods, they shall be charged 20 ..." 21 So if we just pause there. It's "whether the same 22 shall be payable half yearly or any shorter or more 23 distant periods", so it's talking about periodic 24 payments over a period, and charged in respect of yearly 25 interest. It's charging the yearly interest, regardless</p> <p style="text-align: center;">Page 39</p>
<p>1 1803 Act." 2 The point we make in footnote 20, we say it is also 3 clear from the wording of the provision, it goes on to 4 refer to "such annual payment", that yearly interest is 5 regarded as a type of annual payment. That provision is 6 in tab 13. These provisions start in the first bundle 7 of the authorities at tab 13. 8 The first page behind tab 13 just gives the 9 schedule D charge. It's remarkable that we have 10 schedule A, B, C, D and E back in 1803, that have lasted 11 with us for well over 200 years. Just notice the first 12 line of schedule D: 13 " ... upon the annual profits or gains arising or 14 accruing to any person or persons residing in Great 15 Britain." 16 One sees there the term "arising or accruing". And 17 then the second page, at the top of the page, and this 18 is schedule D, the third case. I'm sure your Lordship 19 will remember when you were at the bar, that we were all 20 taxed on the basis of being within case 2 of schedule D, 21 carrying on a profession. Case 1 was trades, case 2 was 22 professions, case 3 always included interest, annuities 23 and other annual payments. The only point I would make 24 about that -- again, I don't need to take to you it, but 25 again, looking at a feature of our income tax regime,</p> <p style="text-align: center;">Page 38</p>	<p>1 of whenever they're payable. And then the statutory 2 notice: 3 " ... for every 20 shillings of the annual amount 4 thereof, the sum of one shilling without deduction, 5 according to and under and subject to the provisions by 6 which the duty in schedule 1 may be charged ..." 7 And that's the preceding basis. But it then goes 8 on: 9 " ... provided that in every case where the same 10 shall be payable by any person or persons out of any 11 profits or gains charged by virtue of this Act, no 12 assessment shall be made upon such annuity, interest or 13 other annual payment, but the whole duty due in respect 14 of such profits or gains, shall be charged without 15 regard to such annual payments ..." 16 So pausing there, it's there referring to "such 17 annual payment", and it's plainly encompassing within 18 that terminology, yearly interest, annuities, as well as 19 annual payments. It's, therefore, plainly in its own 20 terms, expressly encompassing yearly interest as being 21 an annual payment: 22 " ... and the person so liable to make such annual 23 payment shall be authorised to deduct out of such annual 24 payment at the rate of one shilling for every 25 20 shillings of the amount thereof, except for the party</p> <p style="text-align: center;">Page 40</p>

<p>1 to whom the payment is to be made, shall produce 2 a certificate of exemption or abatement." 3 And that, I think for the moment, is all I need 4 read. So clearly, therefore, in the terminology, and we 5 will see all the subsequent authorities, yearly interest 6 is an annual payment. 7 The way in which that worked just makes the point 8 that the government was, as it were, putting the burden 9 on the payer of these amounts. If the payer had taxable 10 income of 100 and was then making a payment of yearly 11 interest of, say, an amount less than that 100, then the 12 payer would be taxed on his 100 of income but would not 13 be given a deduction for the yearly interest he was 14 paying out of it, but was given the ability to deduct 15 the tax on that yearly interest because he had already 16 paid tax on the income out of which he was making the 17 payment. So that's how it worked, and that's how they 18 imposed the deduction of tax at source, which avoided 19 the government, the Revenue, having to directly assess 20 the recipient of that yearly interest or annual payment. 21 As far as the terminology there, as we'll see, it's 22 picked up, that terminology, in all the cases, <i>Bebb v</i> 23 <i>Bunny</i>, <i>Goslings</i>, subsequently <i>Moss' Empires</i>, et cetera, 24 <i>Lord Maugham</i>, et cetera, that is a species of annual 25 payments, that is something that recurs, and part of the</p> <p style="text-align: center;">Page 41</p>	<p>1 from property. Again, you can see in the first part of 2 that, it refers to the preceding year basis. But then 3 the second part: 4 "The profits on all Exchequer bills and other 5 securities bearing interest payable out of the public 6 revenue and all discounts and on all interest of money 7 not being annual interest payable, paid by any persons." 8 So in 1803, there is a deduction at source provision 9 brought in in respect of yearly interest, no charge on 10 any other form of interest. In 1805, they bring in 11 a general charge on all interest other than yearly 12 interest, because yearly interest is covered by the 13 deduction at source procedure for the first time. But 14 the point that is plain from these particular provisions 15 is that yearly interest was intended to be something 16 going on, as we say, accruing interest over a period in 17 the future. That was the animal, if I may call it that, 18 identified in 1803, without any other interest being 19 charged. When they do introduce a charge in respect of 20 any other interest, they don't actually produce a charge 21 giving rise to a deduction at source, in respect of any 22 other interest. If and insofar as that ever actually 23 occurs, that only occurs in 1888, some 83 years later. 24 (Pause) 25 So we make that point in paragraph 6, that the</p> <p style="text-align: center;">Page 43</p>
<p>1 quality of the thing is its recurrence or capacity to 2 recur. 3 So that, reverting to our skeleton, is the point 4 that we make in paragraph 4, where we refer to the 5 deduction provision which I've just read out and I've 6 just attempted to explain. Then perhaps more 7 significantly, paragraph 5, we say: 8 "Thus at inception, the deduction of tax at source 9 in respect of interest, only applied to yearly interest, 10 as opposed to any other form of interest." 11 And we say: 12 "It must have been the rationale that such deduction 13 procedures were only intended for ongoing, continuing 14 situations of some permanence and significance, such as 15 yearly interest and other annual payments. Non-yearly 16 interest was not generally charged to tax." 17 And then paragraph 6 of our skeleton, and again, 18 this is the 1805 Act, behind tab 15. This is, for the 19 first time, bringing in a charge in respect of all 20 interest. If one looks behind tab 15, the third page, 21 towards the end of the page, one can see the heading 22 "The third case", that's the third case of schedule D: 23 "The duty to be charged in respect of profits of 24 an uncertain annual value, not charged to schedule A." 25 Schedule A, your Lordship will appreciate, is income</p> <p style="text-align: center;">Page 42</p>	<p>1 Income Tax Act 1805 substituted a new schedule D case 3, 2 profits of uncertain annual value and the words I've 3 just read out. Under the 1805 Act, all interest clearly 4 chargeable, and there was clearly a distinction between 5 yearly interest that was charged by section 192 of the 6 1805 Act which if paid out of profits or gains, was 7 deductible at source, and non-yearly interest, which 8 I've just looked at, for which no deduction of tax at 9 source provision applies. So the deduction of 10 provisions, therefore, as a conception, were only 11 intended to apply to recurring yearly interest. We make 12 the point by reference to section 192 which is behind 13 tab 16. We make that point in our footnote 22. If 14 I just read it there and then we look at tab 16, which 15 is section 192 of the 1805 Act. Looking at our 16 footnote 22, section 192: 17 "Where any payment shall be made from profits or 18 gains not charged by this Act, or any interest of money 19 shall not be reserved or charged or payable for the 20 period of one year, the tax is charged directly, 21 otherwise deduction at source was used." 22 So, again, talking about payable for a period of one 23 year, it says there. That's the connection as far as 24 yearly interest is concerned with a period, and we say 25 it's a period of accrual because nobody in their right</p> <p style="text-align: center;">Page 44</p>

<p>1 mind has interest paid day by day. You accrue interest 2 day by day, but it's payable at certain periods. 3 MR JUSTICE HILDYARD: Do I have to worry about the words 4 "not otherwise charged", which as a matter of fact 5 appear in 1803 as well in the side note, or is that 6 irrelevant? 7 MR GARDINER: No, it's the dichotomy that yearly interest 8 was charged by the deduction at source procedure, so 9 that was the way in which it was charged. All other 10 interest is then just charged generally under 11 schedule D. 12 MR JUSTICE HILDYARD: I'm sorry, I've misunderstood. In 13 1803, I thought only annual interest came into charge. 14 MR GARDINER: That's right, my Lord, yes. 15 MR JUSTICE HILDYARD: So why does it say "not otherwise 16 charged? "Duty charged on all annual interest not 17 otherwise charged"; does it mean anything? 18 MR GARDINER: It isn't otherwise charged. Yes, I'm sorry, 19 my learned friend is right, it might be for example, if 20 you have a bank that was trading in securities, that it 21 might be otherwise charged on case one of schedule D, 22 because it's dealing in interest. 23 MR JUSTICE HILDYARD: Yes. I see. 24 MR GARDINER: Yes, I'm sorry. I'm grateful to my learned 25 friend.</p> <p style="text-align: center;">Page 45</p>	<p>1 So, again, slightly enlarged terminology, but 2 basically to the same effect, and again, demonstrating 3 that yearly interest was clearly an annual payment. 4 At paragraph 7 we say (Inaudible) Income Tax Act 5 1806, that does not really assist us, we haven't 6 referred to it. Then we say in paragraph 8 that income 7 tax was abolished in 1816 but re-introduced by Sir 8 Robert Peel in 1842. Then this might be helpful. 9 Your Lordship may not be entirely familiar with the 10 history of the Income Tax Act, but the 1842 Act was the 11 main Act introduced by Pitt. Then Gladstone introduced 12 the 1853 Act. There is then a consolidation Act in 13 1918, there is a further consolidation Act in 1952, and 14 a further consolidation Act in 1970. Indeed, the final 15 consolidation Act in 1988. 16 Then paragraph 8, the Income Tax Act 1842. 17 Section 102 at tab 18. You see 102. I'm not going to 18 read this out, but would your Lordship just take it from 19 me, that those terms are identical to the terms that 20 we've already seen. One can see it's section 102 and 21 runs down, relevantly, if one looks at the right hand 22 margin, to the terms "interest secured on rates." Just 23 before that. There are various passages that we've 24 already seen. So, basically, as they reintroduce the 25 Act, they've reintroduced the provisions that were</p> <p style="text-align: center;">Page 47</p>
<p>1 MR JUSTICE HILDYARD: Yes. Okay. 2 MR GARDINER: So if one just looks then, behind tab 16 at 3 section 192. So we've seen the non-yearly interest 4 brought into the schedule D case 3 charge. Then 192: 5 "... and defer(?) enacted that upon all annuities, 6 yearly interest of money or other annual payments, 7 whether in Great Britain ..." 8 Et cetera, et cetera. 9 And then five lines down: 10 "Whether the same ...(reading to the words)... 11 shorter or more distant periods." 12 So it's, again, the same terminology. Then four 13 lines on, the proviso towards right hand side of the 14 page: 15 "Provided that every case where the same shall be 16 ...(reading to the words)... on the person liable to 17 such annual payment [and again, such annual payment] 18 without distinguishing such annual payment on the person 19 so liable to make ...(reading to the words)... liable to 20 deduction from which a deduction has been made, shall be 21 authorised to deduct out of such annual payment [and 22 again, such annual payment] at the rate of one shilling 23 for every 20 shillings of the amount thereof ...(reading 24 to the words)... exemption or abatement as herein before 25 mentioned."</p> <p style="text-align: center;">Page 46</p>	<p>1 there, starting with 1803 onwards that we've already 2 seen. 3 MR JUSTICE HILDYARD: Yes. 4 MR GARDINER: And then Gladstone in 1853. This is our 5 paragraph 9. Gladstone's Income Tax Act 1853, 6 section 40. I'd better take your Lordship to that, 7 because that's the provision that the initial cases, 8 <i>Bebb v Bunny</i> and <i>Goslings</i>, et cetera, refer to. 9 Section 40: 10 "Where there was a deduction at source, this was to 11 be determined by the rate at the time the interest 12 became due." 13 That was the provision in the 1853 Act. The 1842 14 Act also brought: 15 "All interest in money, annuities ...(reading to the 16 words)... schedule D." 17 One sees behind tab 19, the 1853 Act. The third 18 page, schedule D, again it talks about annual profits or 19 gains arising or accruing, and the last three lines on 20 the page: 21 "... in respect of all interest of money, annuities 22 and other annual profits and gains not charged by virtue 23 of any other schedules contained in this Act, to be 24 charged for every 20 shillings in the annual amount." 25 Then behind tab 20 is the deduction provision, and</p> <p style="text-align: center;">Page 48</p>

<p>1 I had perhaps better just read the opening five or six 2 lines because this is the provision referred to in the 3 authority. So it's section 40 of the 1853 Act: 4 "Deductions of duty on payment of rent, interest 5 ... every person who shall be liable to the payment of 6 any rent or any yearly interest of money or any annuity 7 or other annual payment, either as a charge on any 8 property or as a personal debt or obligation by virtue 9 of any contract, whether the same shall be received or 10 payable half yearly or at any shorter or more distant 11 periods, shall be entitled, as hereby authorised on 12 making such payment, to deduct and retain thereout, the 13 amount of the rate of duty which at the time when such 14 payment becomes due, shall be payable under this Act." 15 So very much as we've seen before, but there it is, 16 section 40 in the 1853 Act. As one can see, "Determined 17 by the rate at the time the interest became due." 18 Those last few words I read: 19 "... which at the time when such payment becomes 20 due, shall be payable under this Act." 21 Then the next provision, paragraph 10 of our annex, 22 is possibly the most significant of the provisions that 23 we're referring to in this, as far as analysis. Perhaps 24 I can just read that. Paragraph 10 of our annex: 25 "Subsequently, where deduction at source applied [so</p> <p style="text-align: center;">Page 49</p>	<p>1 "... and whereas under and by virtue of the 40th 2 section of the Act passed on the 16th and 17th years of 3 Her Majesty's reign [so that's 1842, chapter 34], 4 persons liable to the payment of rent, yearly interest 5 or any annuity or other annual payment therein 6 mentioned, are entitled and authorised on making such 7 payment, to deduct and retain thereout, the amount of 8 the rate of income tax which shall be payable at the 9 time when such payment becomes due." 10 MR JUSTICE HILDYARD: I'm so sorry, was it the 1853 Act that 11 was being referred to? 12 MR GARDINER: Yes, I'm sorry, my Lord. 13 MR JUSTICE HILDYARD: You said 1854 but it's 1853. 14 MR GARDINER: Your Lordship is correct, yes, I'm sorry. 15 MR JUSTICE HILDYARD: And something in that caused this 16 concern, and this supplements 40. 17 MR GARDINER: Yes. Section 40 of the 1853 Act provides for 18 the principle of deduction at source. This is changing 19 the rate at which that deduction is to be made. 20 MR JUSTICE HILDYARD: I see, and is that all it does? 21 MR GARDINER: That's all it does, yes. 22 MR JUSTICE HILDYARD: So right at the end, "anything in the 23 said recited Act to the contrary notwithstanding", the 24 only thing to the contrary was the rate? 25 MR GARDINER: The rate, my Lord, that's absolutely correct.</p> <p style="text-align: center;">Page 51</p>
<p>1 the kind of provisions we've been looking at, section 40 2 and the like], the determination of the rate was altered 3 by section 15 of the Revenue number 1 Act 1864, which 4 specified [these are the terms] 'that the persons liable 5 to and making any such payment as aforesaid, shall be 6 entitled and are hereby authorised to deduct and retain 7 thereout, the amount of the rate or a proportionate 8 amount of the several rates of income tax which were 9 chargeable by law upon or in respect of such rent, 10 interest, annuity or other annual payment or the source 11 thereof, during the period through which the same was 12 accruing to. Anything in the said recited Act to the 13 contrary, notwithstanding.' As a result, the tax rate 14 was to be determined by a reference to averaging the tax 15 rates over the period of accruer, rather than simply 16 taking the tax rate at the time the interest became 17 due." 18 That provision is behind tab 21. If I just go to it 19 very briefly. It's the Revenue number 1 Act 1864. The 20 heading "Income tax levied under section 40." That's 21 the provision we see: 22 "... at the rate payable during the period when the 23 same was accruing." 24 So it's referring to section 40, which is only 25 referring to yearly interest:</p> <p style="text-align: center;">Page 50</p>	<p>1 MR JUSTICE HILDYARD: Right. 2 MR GARDINER: So section 40 of the 1853 Act provides for the 3 principle of deduction at source on yearly interest. It 4 said: you should deduct at source by reference to the 5 rate when the amount is due. That is substituted by the 6 periods of accruer over which the interest accrues. The 7 rates or a combination of the rates over a period of 8 accruer. That's what this does. So it refers to 9 section 40. It then says that: 10 "The persons liable to the payment of rent, yearly 11 interest or any annuity or other annual payment therein 12 mentioned, are entitled and authorised on making such 13 payment, to deduct and retain thereout, the amount of 14 the rate of income tax which shall be payable at the 15 time when such payment becomes due." 16 That's what section 40 had enacted. 17 MR JUSTICE HILDYARD: Yes. 18 MR GARDINER: But then this is the change: 19 "Being enacted that the persons liable to and making 20 any such payment as aforesaid, shall be entitled and are 21 hereby authorised to deduct and retain thereout, the 22 amount of the rate, or a proportionate amount of the 23 several rates of income tax which were chargeable by law 24 upon or in respect of such rent, interest ... " 25 And interest there it must be, when it's referring</p> <p style="text-align: center;">Page 52</p>

<p>1 to "such", must be referring to yearly interest, so it's 2 referring to yearly interest: 3 "... annuity or other annual payment or the source 4 thereof during the period through which the same was 5 accruing due, anything in the said recited Act to the 6 contrary notwithstanding." 7 MR JUSTICE HILDYARD: I see, so maybe I have confused 8 myself. What this was doing was two things, not one. 9 One was saying "We're going to have a different rate 10 now", and because there was a different rate earlier, we 11 have to work out what, in the intervening period, was 12 the appropriate rate, and it's done according to the 13 rate in effect at the time, but it adds the words 14 "during the time it was accruing due"; is that right? 15 MR GARDINER: I think when it refers to "or a proportionate 16 amount of the several rates of income tax", let's assume 17 for a simple example, it's accrued over two years. 18 MR JUSTICE HILDYARD: Yes. 19 MR GARDINER: In the first year there is a rate of, say, 10 20 per cent, in the second year a rate of 5 per cent, you 21 will end up with 7.5. 22 MR JUSTICE HILDYARD: Right. Do you say that the words 23 which you stress, "accruing due," were there sub 24 silentio before, or do you say that this was a new 25 requirement?</p> <p style="text-align: center;">Page 53</p>	<p>1 point, we say it was always there, sub silentio as 2 a quality, it's simply recognising that now. 3 MR JUSTICE HILDYARD: Yes. 4 I don't know when would be a good time for a break. 5 How are you doing, transcript writers, are you feeling 6 like a break now or do you want to soldier on to the end 7 of the history or what would you like? 8 THE SHORTHAND WRITER: If we could have one now, that would 9 be appreciated. 10 MR JUSTICE HILDYARD: Is that all right? 11 MR GARDINER: Yes, we're actually making quite good time in 12 terms of the progress. 13 (3.05 pm) 14 (A short break) 15 (3.12 pm) 16 MR GARDINER: My Lord, I'm grateful. It's been drawn to my 17 attention that at paragraph 9, in the third line from 18 the end, we refer to the 1842 Act and your Lordship has 19 actually already picked it up, I think. We should have 20 actually referred to the 1853 Act, paragraph 9 of our 21 appendix. 22 MR JUSTICE HILDYARD: Yes. 23 MR GARDINER: Could we just substitute 1853 for 1842, I'm 24 sorry about that. 25 My point is really in relation to the 1864 Act which</p> <p style="text-align: center;">Page 55</p>
<p>1 MR GARDINER: No, we say that the concept of yearly interest 2 was always recognising -- 3 MR JUSTICE HILDYARD: Sub silentio, this was spelling out 4 what it meant? 5 MR GARDINER: Yes, this was recognising that fact and using 6 that fact as giving rise to the rate that you deduct 7 tax. 8 MR JUSTICE HILDYARD: Right. 9 MR GARDINER: So it's recognising the concept that I've 10 already said is in the legislation. 11 MR JUSTICE HILDYARD: Right. 12 MR GARDINER: That has been there from 1803 onwards, and 13 it's then using that fact which it recognises as 14 a criterion for yearly interest to exist. It's 15 recognising that fact and saying "We'll now use that 16 combination of rates over the period of accruer as being 17 the rate", and so just the rate at due. 18 MR JUSTICE HILDYARD: The important point from my point of 19 view, is the characteristic of accruing over the period, 20 is a characteristic which was always a characteristic of 21 annual or yearly interest, though it was not until this 22 date, 1864, that express words were used? 23 MR GARDINER: My Lord, that's why this is probably the most 24 significant provision in the historic analysis, yes. 25 But as I think your Lordship, obviously, already has the</p> <p style="text-align: center;">Page 54</p>	<p>1 I think I've made, but we say that that provision 2 presupposes that yearly interest must accrue over 3 a period. It doesn't provide for any other basis of 4 determining the rate, it's talking about the rates over 5 the period of accruer. It therefore presupposes that 6 yearly interest, because it's only concerned with yearly 7 interest, not with any other kind of interest, accrues 8 over a period. That provision stood until 1927, so some 9 63-odd years. In 1927, it was changed to the rate when 10 the interest was due. It's interesting to note that 11 during that 63-year period, this is referred to in 12 paragraph 11 of our appendix, the Customs and 13 Inland Revenue Act 1888 brought in a deduction at source 14 provision in respect of any other interest, yearly or 15 otherwise, not payable out of profits or gains brought 16 into charge. So from 1888 to 1927, we have a provision 17 concerned with yearly interest, where the rate of tax 18 was determined by reference to the rates applicable 19 during the periods of accruer, and the provision 20 introduced in 1888 by section 24.3, which we'll look at 21 in a moment, that applies to all types of interest, so 22 yearly or otherwise, in respect of payments made out of 23 income not already taxed, was based on the tax rate at 24 the time of payment. So there one has, at least for 25 that period of time, some 39-odd years, the dichotomy</p> <p style="text-align: center;">Page 56</p>

<p>1 between a provision recognising yearly interest, tax 2 deducted by reference to the rates during the period of 3 accruer, and all types of interest not adopting tax 4 during a period of accruer, for the good reason, as we 5 would say, that all types of interest might well apply 6 to interest that didn't apply to periods of accruer, and 7 therefore, the tax rate is the rate at the time of 8 payment. And that provision, the 1988 provision, is 9 behind tab 22.</p> <p>10 MR JUSTICE HILDYARD: Yes.</p> <p>11 MR GARDINER: One can see it's section 24.3: 12 "Upon payment of any interest of money or annuities 13 charged with income tax under schedule D [so any 14 interest of money, not any yearly interest of money] and 15 not payable or not wholly payable out of profits or 16 gains brought into charge to such tax, the person by or 17 through whom such interest [any interest] or annuities 18 shall be paid, shall deduct thereout, the rate of income 19 tax in force at the time of such payment."</p> <p>20 MR JUSTICE HILDYARD: I'm being silly about this, 21 Mr Gardiner. This, you say, does not replace 1864, but 22 extends the deduction method to other forms of interest, 23 or does it replace 1864?</p> <p>24 MR GARDINER: No, it doesn't replace 1864, 1864 goes on in 25 exactly those terms, by reference to the periods of</p> <p style="text-align: center;">Page 57</p>	<p>1 MR GARDINER: And applies to any kind of interest. So it 2 could be yearly or otherwise.</p> <p>3 MR JUSTICE HILDYARD: Yes.</p> <p>4 MR GARDINER: And that just points to the distinction that 5 when the draftsman is applying for a rate to deal with 6 that, instead of adopting the rate of accruer, which is 7 there on the statute book and continues in the case of 8 yearly interest, he adopts a different rate because he's 9 recognising that yearly interest accrues over a period 10 of time, any other type of interest may well not accrue 11 over a period of time. That must be the rationale for 12 the distinction.</p> <p>13 MR JUSTICE HILDYARD: So the absence of that expression?</p> <p>14 MR GARDINER: Yes. So when one has, for this period of 15 a considerable number of years, the dichotomy between 16 yearly interest, the rates applicable to the periods of 17 accruer, because the draftsman recognises that for all 18 types of interest, yearly or otherwise, there may be 19 situations where there isn't a period of accruer which 20 is peculiar, particularly to yearly interest, therefore 21 he can't adopt the principle of having the rates during 22 the period of accruer, he adopts the rate as at the time 23 of payment.</p> <p>24 MR JUSTICE HILDYARD: Yes.</p> <p>25 MR GARDINER: So simply the inference being, as we would</p> <p style="text-align: center;">Page 59</p>
<p>1 accruer, until 1927. The only thing that's changed in 2 1927 is that instead of the periods of accruer, from 3 1927 onwards, they refer to the tax rate at the time 4 when the interest was due.</p> <p>5 MR JUSTICE HILDYARD: I haven't seen 1927, you'll come to it 6 in due course, but just focussing on 1888, it says: 7 "Any interest of money or annuities charged with 8 income tax under schedule D and not payable ...(reading 9 to the words)... such tax."</p> <p>10 MR GARDINER: It's the latter point, my Lord, that is the 11 distinction. The 1864 Act applied to payments made out 12 of profits brought in to charge to tax.</p> <p>13 MR JUSTICE HILDYARD: I'm sorry, that's what I'm getting at. 14 So it's those words which explain that this new 15 provision, the 1888 provision, doesn't apply to the 1864 16 regime?</p> <p>17 MR GARDINER: My Lord, that's absolutely right, yes. So the 18 1864 regime goes on because it's only applicable to 19 payments made out of profits and gains brought into 20 charge --</p> <p>21 MR JUSTICE HILDYARD: I'm sorry, I was being silly. Yes, 22 okay.</p> <p>23 MR GARDINER: And the 1888 Act applies to payments out of 24 income that has not been taxed.</p> <p>25 MR JUSTICE HILDYARD: Yes.</p> <p style="text-align: center;">Page 58</p>	<p>1 say, non-yearly interest is something which might not 2 accrue. We say there's a lot in the history of these 3 points and I'll be making it as I go along, but this is 4 probably the most significant of the lot. So it 5 presupposes that yearly interest, like other annual 6 payments, is something that necessarily accrues, it 7 grows over a period.</p> <p>8 I think I can be fairly brief with the rest of the 9 appendix. As I said earlier this afternoon, I make the 10 point in paragraph 12 about this distinction. 11 Paragraph 13 of our appendix, we talk about the 12 consolidation of the rules in the Income Tax Act 1918, 13 rule 21 and rule 19, but they're the same rules that 14 we've seen developed so far. Then we go to the 15 Consolidation Act in paragraph 14 in 1952, section 169 16 and section 170. And, again, they're the same as rules 17 19 and 21 of the 1918 Consolidation Act. Then there is 18 a change in 1965, when corporation tax was introduced. 19 It was always regarded at the tax bar as a watershed 20 year. It was when the Wilson government came in and 21 created capital gains tax and corporation tax at a fell 22 swoop. Corporation tax made it necessary to make 23 a number of changes. All one can say is that in 1969, 24 what happens, as one can see in 15 and 16 of our 25 appendix, they took yearly interest away from annuities</p> <p style="text-align: center;">Page 60</p>

<p>1 and other annual payments, but as we say, that wasn't 2 intended to create any difference in meaning, as far as 3 yearly interest was concerned, having regard to all the 4 case authority hitherto. And there's no suggestion 5 whatsoever that they were attempting to do so, it was 6 simply to make a difference in the people to whom the 7 deduction obligation should apply. 8 MR JUSTICE HILDYARD: You mentioned 1927. Do I have to 9 worry about 1927? 10 MR GARDINER: No, the only difference in 1927, my Lord, is 11 just simply that the period of accruer as being the 12 rate, was changed to the period due. We suspect it was 13 because of the impending enactment of surtax, but it's 14 a factor that one just recognises as the change but not 15 of any great significance. The great significance in my 16 respectful submission, is the dichotomy in the drafting 17 during that particular period of time, the recognition 18 of the quality of yearly interest as being in respect of 19 a period of accruer. 20 And then that takes us up -- we end up in 21 paragraph 17 of our appendix. Perhaps just to notice at 22 the end of paragraph 16, the 1969 Act, the direct 23 terminology as section 874, the last four lines of 24 paragraph 16: 25 "Sections 26.1 and 4 of the Finance Act 1969 gave</p> <p style="text-align: center;">Page 61</p>	<p>1 applying to the two. 2 MR JUSTICE HILDYARD: But when does it arise and when does 3 it accrue, I suppose? 4 MR GARDINER: Well, we say the statutory interest in this 5 case arises and doesn't accrue. 6 MR JUSTICE HILDYARD: Right. 7 MR GARDINER: Otherwise interest which is intended to be the 8 type of ongoing interest, yearly interest, always 9 accrues. 10 MR JUSTICE HILDYARD: And is it common ground between you 11 that the fact that "accruer" is no longer used, doesn't 12 make any difference, it was simply intended to 13 clarify -- introducing want of clarity at the same time, 14 as it were? 15 MR GARDINER: Well I hope that's common ground, it ought to 16 be common ground. I don't know whether it is. We would 17 say it follows from the remit of the tax law 18 simplification project. They weren't intending to 19 actually produce a change in the law. 20 MR JUSTICE HILDYARD: That's a central point, in which case, 21 Mr Goy, that's common ground, is it? I don't have to 22 worry about it. When I see "arising", I can take it to 23 mean, if one is assisted by that sort of thing, 24 "accruing or arising"; is that right? 25 MR GOY: Can I come back to that, if you don't mind?</p> <p style="text-align: center;">Page 63</p>
<p>1 an obligation to deduct at source on account of the 2 Revenue in the case of yearly interest paid by 3 companies, as well as certain other categories of payers 4 ... (reading to the words)... someone whose usual place 5 of abode is outside the UK." 6 And that is what we have now in section 874. But 7 the critical terminology, in our respectful submission, 8 is the terminology "yearly interest". In our respectful 9 submission, the historical analysis does actually help 10 to understand what yearly interest has meant for 200-odd 11 years and what it still means today, in the light of the 12 authority and the legislation, and the legislation that 13 I've already referred to. It's been a well known 14 concept in tax legislation for over 200 years. As we 15 say, there is nothing in the present legislation to 16 suggest that Parliament intended to change the meaning 17 of yearly interest. As far as "arising and accruing", 18 the tax law simplification project was simply to try and 19 modernise some of the language. It wasn't intended to 20 make a substantive change. 21 MR JUSTICE HILDYARD: What was the reason for using two 22 words originally, "arising or accruing"? 23 MR GARDINER: I suspect that it was they recognised that 24 some interest might just arise whilst other interest 25 accrued, and they wanted to make sure that they were</p> <p style="text-align: center;">Page 62</p>	<p>1 MR JUSTICE HILDYARD: Okay. 2 MR GARDINER: Anyway, that's what we say as far as the 3 historical analysis. 4 If I might, then, I might go on to the case law in 5 respect of the yearly interest which we deal with in 6 paragraphs 20 to 36 of our skeleton. We set out at, 7 I think, paragraph 17, section 874 already, and we 8 referred to the history in 18 and made a point by 9 reference to the history in 19. It's really 10 paragraph 20 onwards, where we talk about the nature of 11 yearly interest. We make the point in paragraph 20 that 12 deduction of tax must also only be applied to yearly 13 annual interest. Then the first reported case which 14 seems to be referred to in virtually most, at least, of 15 the subsequent cases, is the case of <i>Bebb v Bunny</i>. 16 I would like to go to it in a moment. It was decided in 17 1854, and it's at tab 30. That's the second volume of 18 the authorities, the case law volume. If one looks just 19 at the headnote: 20 "A purchaser liable to pay interest on his purchase 21 money, may deduct income tax from such interest. It was 22 the practise to deduct the tax from the interest on 23 debts upon promissory notes and the like, in the offices 24 of the masters and chancellor. The tax is not deducted 25 on payment of purchase money into court but the</p> <p style="text-align: center;">Page 64</p>

<p>1 purchaser, it seems, may apply to have it deducted when 2 the purchase money is paid out of court." 3 But then one notices here, what the headnote writer, 4 at least, is picking up as part of the ratio of the 5 case: 6 "The words 'yearly interest' in section 40 mean not 7 only interest accruing de anno in annum, but any 8 interest at a fixed rate per cent per annum, though 9 accruing de die in diem." 10 We say the decision of the vice chancellor in this 11 particular case, if I can put it this way, I don't want 12 to put it too high, is really definitional as to the 13 concept of yearly interest, and within that definition, 14 we say, he recognises the significance of de die in 15 diem, which of course, is accruing day by day. And as 16 we'll see in my learned friend's skeleton, of course 17 they don't recognise that as part of the definition. 18 This is Sir William Page Wood, later the Lord 19 Chancellor, Lord Hatherley, and at page 437, at the top 20 of the page, he says: 21 "Most mortgage deeds contain only a covenant to pay 22 the principal with interest at a certain rate per annum 23 ...(reading to the words)... After that, it accrues de 24 die in diem and the interest without any particular 25 reservation, ordinarily is received half yearly, from</p> <p style="text-align: center;">Page 65</p>	<p>1 And then towards the end of that paragraph, four or five 2 lines from the end, towards the right hand side of the 3 page: 4 "I consider the Act very singularly worded, the 5 yearly interest being used, apparently, in the same 6 sense as annual payment. But I am clearly of the 7 opinion that it means at least all interest at a yearly 8 rate and which may have to be paid de anno in annum, 9 such as interest on purchase money, as well as mortgage 10 interest, and that, therefore, the purchaser is entitled 11 to deduct the tax in this way." 12 So he's looking at section 40, he's looking at 13 yearly interest payable out of profits and gains brought 14 into charge and he's looking at it on the basis that 15 yearly interest is payable year by year or capable of 16 being year by year. But significantly, and this is part 17 of his definitional approach, as we say, he's looking at 18 something accruing over a period. Something of some 19 permanence or capable of some permanence of continuity, 20 therefore a deduction at source regime applies, for the 21 Revenue and the parties, an ongoing type of thing. 22 That's the passages in particular, apart from the 23 headnote and the first passage, that we set out in 24 paragraph 22 of our skeleton. We say that first 25 paragraph there is definitional and it includes the</p> <p style="text-align: center;">Page 67</p>
<p>1 year to year. It is difficult to see the distinction 2 between interest so reserved and paid and that which by 3 special agreement [and perhaps he's putting this on 4 a particular basis by those words] accrues on purchase 5 money which also goes on from day to day and may run on 6 for a year or stop at any time on payment of the 7 purchase money which in some shape or other forms a lien 8 on the property." 9 So it seems to us that he's assimilating that 10 situation with the position of a mortgage, ie 11 an instrument that gives rise to interest accruing from 12 day to day, de die in diem. Then down the page, after 13 the next main paragraph, the paragraph beginning "The 14 whole difficulty", and that is what we say is the 15 definitional part of his judgment: 16 "The whole difficulty is in the expression; yearly 17 interest of money' but I think it is susceptible of this 18 view that it is interest reserved at a given rate 19 per cent per annum, or at least in the construction of 20 this Act, I must hold that any interest which may be or 21 becomes payable de anno in annum, though accruing de die 22 in diem is within the 40th section. I cannot make any 23 solid distinction between interest on mortgage money and 24 interest on purchase money." 25 Section 40 being of the 1853 Act that we've seen.</p> <p style="text-align: center;">Page 66</p>	<p>1 words "accruing de die in diem", from day to day. That 2 identifies the kind of investment that somebody makes so 3 as to earn interest over a period of time, whenever the 4 interest is payable, be it payable quarterly, 5 semi-annually or yearly. That's what we say towards the 6 end of paragraph 22. 7 And then paragraph 23 of our skeleton, we then go on 8 to the next case, which is Goslings and Sharpe v Blake, 9 the decision of the Court of Appeal. That's at tab 32A. 10 A is the decision in the Queen's Bench Division. My 11 learned friends wanted the decision in tax cases 12 included at B. I am simply going to look at the Queen's 13 Bench Division which, of course, your Lordship will 14 appreciate, is approved by the judges. I don't know why 15 the tax case is there, but my learned friend will 16 actually deal with that, no doubt. So we say in 17 paragraph 23 there's the decision in Goslings: 18 "... and the question is whether or not, interest 19 received by a banker on certain loans for a specified 20 time of less than a year, was yearly interest 21 ...(Reading to the words)... in the case of such a loan, 22 there was no intention for the loan to remain 23 outstanding for a long period. The interest was not 24 yearly interest, even if calculated by reference to 25 a yearly rate."</p> <p style="text-align: center;">Page 68</p>

<p>1 In a sense, if my learned friend's argument were 2 right, they should have said "This is seven days, 3 therefore it's a calculation period of less than a year, 4 therefore it can't constitute yearly interest." But 5 they don't say that. So in the Court of Appeal, 6 Goslings and Sharpe, bankers, Lord Esher, the Master of 7 the Rolls, at page 326, in the first paragraph of his 8 judgment, he says: 9 "The point which we have to decide in this case is 10 as follows: where a banker or any other man lends money 11 for a specified time, less than a year, to be re-paid at 12 that fixed time, with the interest that has become due 13 up to that time, whether in such a case, the banker or 14 lender is bound to allow the borrower to deduct income 15 tax for the interest which he has to pay." 16 Now it is that case and that only, which was the 17 subject matter of the judgment of the Queen's Bench 18 Division and no other case is presented to us as 19 a matter for decision: 20 "The question then is whether such a case is within 21 the terms of the 40th section of the Act of 1853." 22 And then page 327, he refers to the language, and 23 then about five lines down the page, the sentence 24 beginning "Dealing with this." Having referred to the 25 language of the 40th section, he said:</p> <p style="text-align: center;">Page 69</p>	<p>1 ordinary ...(reading to the words)... to repay the loan 2 in six months and if not then paid, a covenant to pay 3 interest until the loan is repaid ...(reading to the 4 words)... mortgages is intended to go on." 5 Is what he's saying. And then subsequently in the 6 page -- 7 MR JUSTICE HILDYARD: So this was a then quirk, was it, that 8 mortgages were in practice or often, repayable, 9 according to their terms, within six months, but not 10 expected to be repayable in the event, for over a much 11 longer period; is that right? 12 MR GARDINER: My Lord, that is plainly the case from the 13 case of <i>Bebb v Bunny</i>, Sir William Page Wood, and 14 likewise, Lord Justice Lindley is recognising that at 15 that time, things obviously change, as we can see later. 16 MR JUSTICE HILDYARD: But he says this is a different case, 17 it's a short banking loan. 18 MR GARDINER: Yes. And it's again this dichotomy between 19 something of the nature of investment intending to 20 produce income over a period of time that recurs, 21 et cetera, and here is just simply a short accommodation 22 by a banker. He makes that distinction, I think, just 23 above the middle of the page, when he says: 24 "In point of business, therefore, a mortgage is not 25 a short loan but a banker's loan at three months is</p> <p style="text-align: center;">Page 71</p>
<p>1 "Dealing with this, according to ordinary English 2 idiomatic language." 3 MR JUSTICE HILDYARD: This is the <i>eiusdem generis</i> point? 4 MR GARDINER: Yes, it's the annual payment point, my Lord, 5 yes. So it's a species of annual payment, that's what 6 he says. In consequence of that, he says two or three 7 lines further on: 8 "Any yearly interest or money surely cannot be 9 interest for less than a year in ordinary English." 10 Then over the page, 328, you'll see just below the 11 middle of the page, he refers to <i>Bebb v Bunny</i> and the 12 decision of Sir William Page Wood, and I think he says 13 that that case was well decided, but there's nothing 14 more that I would like to draw attention to in his 15 judgment. Lord Justice Lindley at page 330, says: 16 "I am of the same opinion. The question is one of 17 considerable difficulty, turning upon the meaning of the 18 expression 'annual interest'. 19 So he's accepting the fact that yearly interest and 20 annual interest are interchangeable. Because it 21 wouldn't have been a case of any difficulty at all, if 22 it was just the period of calculation, because the 23 period of calculation was only seven days. He said: 24 "The difficulty is not lessened by the circumstances 25 that most mortgages are loans for six months. The</p> <p style="text-align: center;">Page 70</p>	<p>1 a totally different thing." 2 MR JUSTICE HILDYARD: Right, and then Lord Justice Bowen 3 emphasises the narrow scope? 4 MR GARDINER: Yes, my Lord. That's the earlier part of 5 Lord Justice Bowen: 6 "We're dealing with this case with short loans only, 7 that is to say, with loans ...(reading to the words)... 8 and are not continued for a long period. It seems to 9 me, not yearly interest at all." 10 MR JUSTICE HILDYARD: "Is not calculated on the year nor on 11 the supposition that the loans would last for a year, 12 therefore it is not yearly interest." 13 MR GARDINER: Yes. It may be a small point on that 14 particular case, but I do make the point that if it were 15 simply the period of calculation, that would have been 16 the most instantly easy way to resolve it, but that is 17 not the way in which they resolve it, they look to it on 18 the basis of a qualitative criterion that yearly 19 interest must possess. 20 That's why we say on the basis of those two cases, 21 just reverting to our skeleton, paragraph 24 and then 22 25, just looking at those two cases, we say: 23 "... that interest for a year is necessarily 24 considered the period over which it is envisaged that 25 the interest will accrue ...(reading to the words)...</p> <p style="text-align: center;">Page 72</p>

<p>1 matter how the interest rate is expressed." 2 25, which is why we put it in bold type, we say: 3 "It follows from the above that it is a prerequisite 4 that yearly interest must be capable of accruing and 5 must accrue for some period and repayable from year to 6 year whilst it accrues." 7 That's going back to the propositions I gave 8 earlier, the same proposition as the first two. We say: 9 "This is the key point and to avoid any 10 misunderstanding, this is the key point to this case 11 ..." 12 We're not there referring to <i>Bebb v Bunny</i> or 13 <i>Goslings</i>, we're referring to this case: 14 "... establishing that statutory interest cannot be 15 yearly interest." 16 And then paragraph 26, we make our point that I've 17 already made by reference to the history of the 1864 18 Act, section 15, the period of accruer being determinant 19 of the rate. That's the point that we make at 20 paragraph 26. I've made all my submissions on that and 21 won't repeat them. It's just a summary, in a sense, of 22 them, in paragraph 26. I won't even read that out. 23 27. Again, this is another decision of the Court of 24 Appeal in 1911. In particular, the judgment of Lord 25 <i>Cozens-Hardy</i>, the Master of the Rolls then. This is</p> <p style="text-align: center;">Page 73</p>	<p>1 shall pay the judgment debt in accordance with the terms 2 of the judgement. To pay in accordance with the terms 3 of the judgment is to pay the amount for which judgment 4 has been recovered, with the legal interest attached to 5 it by the statute. Assuming that payment by the debtor 6 of the debt, less the income tax, would be payment, yet 7 that a notice requiring him to pay the whole sum was 8 nonetheless right and that the notice was valid on this 9 ground also." 10 So on the headnote there is an alternative or 11 an additional basis upon which they can decide the case. 12 We're concerned, in our respectful submission, with the 13 first basis, which is very much in the judgment of the 14 Master of the Rolls. 15 MR JUSTICE HILDYARD: I mean is <i>Cooper</i> -- it prima facie 16 looks very much on point, but when you look at it, is it 17 really? Because one interpretation of <i>Cooper</i> is that 18 all they were looking at was the validity of the notice, 19 and the notice said "You have to pay up the principal 20 and the statutory sum", and the issue as to whether the 21 payer could deduct didn't really arise, it was only 22 a question of the validity of the notice. 23 MR GARDINER: Yes. My Lord, in that respect it's rather 24 like <i>Jefford v Gee</i>, neither of those cases, actually, is 25 particularly helpful at the end of the day.</p> <p style="text-align: center;">Page 75</p>
<p>1 behind tab 35. This is a case of interest on a judgment 2 debt. It's the case of <i>Cooper</i>. If one just notices the 3 headnote: 4 "A bankruptcy note is required payment of a certain 5 sum claimed as being the amount due on a final judgment. 6 In the margin of the notice, particulars of the amount 7 claimed were given, namely debt [so much], interest at 8 4 per cent to date [so much]. Objection was taken that 9 this notice was bared, as it claimed interest in full 10 without allowing for income tax which could or ought to 11 have been deducted by the debtor. Held that a judgment 12 debt, though by law, carrying interest from the date of 13 the judgment, was not a transaction to which the 14 language of the income tax acts relating to yearly 15 interest of money applied, and that the notice was valid 16 and the receiving order based upon it might be valid." 17 So, again, looking at the headnote and what is 18 discerned to be the ratio, it's not looking at the 19 period, it's looking at the nature of the interest 20 flowing from a judgment debt, and it's saying that is 21 not the language of the Income Tax Acts relating to 22 yearly interest which encompasses such interest. Then 23 it goes on: 24 "Held also by Lord Justice Butler that what the 25 bankruptcy notice has to require is that the debtor</p> <p style="text-align: center;">Page 74</p>	<p>1 MR JUSTICE HILDYARD: Lord Denning in <i>Jefford v Gee</i> says 2 "I'm not going to get into that", and I don't think the 3 court should get into that. 4 MR GARDINER: And that, in a sense, is what 5 Lord Justice Buckley is saying here. He says "If the 6 notice specifies the gross amount of interest, then you 7 leave it to the payer as to whether he has an obligation 8 to deduct or not." 9 MR JUSTICE HILDYARD: Lord Justice Buckley says that. Do 10 the rest say that? 11 MR GARDINER: Well Lord Justice Buckley says that, and then 12 if you actually -- the Master of the Rolls doesn't 13 because he gives his judgment first and then 14 Lord Justice Buckley comes along later. Then 15 Lord Justice Kennedy says "I am of the same opinion", so 16 I rather assume they must be agreeing with what 17 Lord Justice Buckley has just said. Then he says: 18 "My own view is that this is not a deduction that 19 could be made in respect of income tax as claimed by the 20 appellant here." 21 MR JUSTICE HILDYARD: So he does tread where Lord Justice 22 Buckley and, later, Lord Denning, don't like to tread? 23 MR GARDINER: Yes, and he agrees with the Master of the 24 Rolls, because the Master of the Rolls has already said 25 it's not yearly interest.</p> <p style="text-align: center;">Page 76</p>

<p>1 MR JUSTICE HILDYARD: Right, I see. So you do pray in aid 2 two judgments, but you can't pray in aid 3 Lord Justice Buckley, who deals with it only on the 4 notice point? 5 MR GARDINER: Save only this, my Lord, that his opening 6 sentence says: 7 "Not differing from anything that the Master of the 8 Rolls has said." 9 MR JUSTICE HILDYARD: Right. 10 MR GARDINER: So putting it at its lowest. 11 MR JUSTICE HILDYARD: I see, so he's not saying he 12 disagrees. 13 MR GARDINER: That's right. 14 MR JUSTICE HILDYARD: Right. But he decides to do it on the 15 short point? 16 MR GARDINER: That's right, my Lord. 17 MR JUSTICE HILDYARD: I see. 18 MR GARDINER: So, in effect, what we have here is the Master 19 of the Rolls saying "It's not yearly interest", for the 20 reasons -- we will just look at them very briefly in 21 a moment perhaps. Lord Justice Buckley says "I'm not 22 dissenting from that but there is this alternative 23 basis", and then Mr Justice Kennedy has said "I agree, 24 but I also agree with the Master of the Rolls", in 25 effect.</p> <p style="text-align: center;">Page 77</p>	<p>1 including the interest in question, he says: 2 "That again seems to me to be clearly beyond 3 argument. I fail to see what ground there can be for 4 saying with regard to a transaction of this kind, where 5 in truth there was not even an agreement for a short 6 loan [so he says not even an agreement for a short loan, 7 therefore it must follow there wasn't even an agreement 8 for a longer loan], where there was merely a judgment 9 debt [merely a judgment debt], which it is true by law 10 carries interest for this seven days in question, that 11 that is a transaction to which the language of the 12 income tax acts about yearly interest can fairly be 13 applied. In my opinion, we must answer that question in 14 the negative." 15 So he recognises it's only carrying it for seven 16 days, but he's not saying that that is the determinant, 17 it's not the calculation period that is the determinant, 18 it's the nature of the transaction. (Pause) 19 MR JUSTICE HILDYARD: Yes, because judgment rate interest 20 says nothing about the length during which the amount is 21 to be outstanding. 22 MR GARDINER: No. I mean as we say all these cases, when 23 you actually come to analyse them, none of the judges 24 are proceeding on the simplistic basis of the argument 25 on the other side of just saying, "This is for a period</p> <p style="text-align: center;">Page 79</p>
<p>1 MR JUSTICE HILDYARD: The Master of the Rolls does say "We 2 must answer that question in the negative." Yes, I see. 3 MR GARDINER: Yes, just picking up what the Master of the 4 Rolls says at page 553 and 554, just very briefly. The 5 first break on that page, he says: 6 "When we get back into the maze of the Income Tax 7 Acts [it was a maze then, it's even worse nowadays], it 8 seems really to depend upon whether this sum can be 9 properly called yearly interest. In my opinion it 10 cannot ..." 11 Two lines further on. 12 And then you'll see he then says: 13 "The words 'yearly interest' are satisfied, although 14 the interest be not payable yearly, but be payable 15 quarterly or ...(Reading to the words)... it being 16 really in the nature of an investment." 17 So that's what he is looking at, and then at the 18 last break on the page -- well he refers to Goslings and 19 Sharpe v Blake, and then he says: 20 "Now, in the present case, I ask myself is it 21 possible to suppose this was a transaction in which 22 anybody contemplated or intended anything permanent? It 23 is quite impossible so to regard it." 24 And then over the page, at the top the page, the 25 first line, Having referred to the full amount,</p> <p style="text-align: center;">Page 78</p>	<p>1 of less than a year, ergo that's the result." None of 2 them are saying that. We pick up that little quote in 3 our paragraph 27, which I hope does encapsulate what the 4 Master of the Rolls said. 5 MR JUSTICE HILDYARD: So I suppose if you have a judgment 6 debt in those days, and you have judgment rate interest, 7 and the matter went to appeal more than a year later, on 8 the Revenue's argument, that would be yearly interest. 9 MR GARDINER: Yes. That's right, my Lord, yes. On their 10 argument. 11 MR JUSTICE HILDYARD: Yes. Mr Goy indicates no, so I just 12 put that out as an Aunt Sally for him to explain. 13 MR GARDINER: This case is not decided on that basis, that's 14 the point I made earlier, that periods that are running 15 over a year, it's not decided on that basis, but for 16 periods that are less than a year, they could have all 17 been decided on the basis of it's a period of less than 18 a year, therefore not yearly interest. They weren't 19 decided on that basis, they were decided on the nature 20 of the transaction giving rise to the type of the 21 interest we're talking about, the accrual of interest 22 and all the rest of it that I've said. 23 MR JUSTICE HILDYARD: I mean, the investment quality is 24 subsequently not approved, I can't remember whether it 25 was by Lord Donaldson or who it was by.</p> <p style="text-align: center;">Page 80</p>

<p>1 MR GARDINER: It's Sir John Donaldson in Cairns v 2 MacDiarmid, yes, a brief off the cuff remark, I'll come 3 to look at it in a minute if I might, but I don't think 4 with respect, of course, he was looking at all these old 5 authorities and the nature of it in that particular 6 case, but I'll come to deal with it if I might when I 7 look at Cairns v MacDiarmid. 8 MR JUSTICE HILDYARD: Yes. 9 MR GARDINER: But that's Cooper. The Gateshead case in 10 paragraph 28, as I said earlier this afternoon in 11 opening, we say now, in the light of my learned friend's 12 skeleton, is probably the most significant case of the 13 lot. I mean, Bebb v Bunny we started with as a really 14 significant authority, the first in definitional terms 15 of recognising what yearly interest was about, and 16 follows on with Goslings and Cooper et cetera and the 17 like. Gateshead Corporation v Lumsden, we just don't 18 see how the Revenue's argument gets over this authority. 19 It's at tab 36. It's set out in paragraph 28, and we 20 give a quote from it there, but in the light of its 21 significance, if I could just spend a little more time 22 on it. Tab 36, the headnote on the first page: 23 "The plaintiffs, as the urban authority of 24 a borough, had, under section 150 of the Public Health 25 Act 1875 and the Gateshead Improvement Act 1867, some</p> <p style="text-align: center;">Page 81</p>	<p>1 income tax therefrom." 2 MR JUSTICE HILDYARD: So Mr Justice Rowlatt was upheld. 3 MR GARDINER: Yes, and I think as I said in opening, we 4 think there is a very material analogy with the case 5 here. If one just looks at the headnote, the Gateshead 6 Corporation weren't in a position of lending money on 7 this basis as an investment or whatever, and if one 8 looks at it by reference to the situation here, Lumsden 9 is in the position of LBIE, as a debtor. It should have 10 paid off these debts, but it didn't. Now apparently 11 there was no intention by Gateshead to make a loan. In 12 our case there's no intention of LBIE's creditors to 13 make a loan, or a loan giving rise to the circumstances 14 in relation to interest that has arisen. So likewise 15 with the creditors here, no intention that they should 16 be lending to LBIE for the kind of term in respect of 17 the interest that has arisen. If I then just look at 18 the facts over the page at 884, at the top of the page: 19 "Some years before the commencement of the action, 20 the plaintiffs, who were the urban sanitary authority 21 for the Borough of Gateshead, in the exercise of their 22 powers under section 150 of the Public Health Act 1875 23 and under the Gateshead Improvement Act 1867, from time 24 to time paved and made up various streets in the borough 25 which the owners ...(Reading to the words)... had failed</p> <p style="text-align: center;">Page 83</p>
<p>1 years before action brought paved and made up certain 2 streets and have from time to time apportioned the 3 expenses thereof among the owners of the premises 4 fronting thereon. The defendant was the owner of 5 premises in these streets and the plaintiffs [that's 6 Gateshead, under the power conferred upon them by 7 section 32 of the Gateshead Improvement Act 1867, 8 allowed him time for the repayment of the sums 9 apportioned in respect of his premises, interest being 10 payable thereon at the rate of 5 per cent per annum. 11 The defendant paid to the plaintiffs varying sums at 12 irregular intervals in part payment of the amount due, 13 which the plaintiffs credited in the first place to the 14 interest due and in the second place towards payment of 15 the principal. There was no evidence to show that the 16 plaintiffs made a regular practice of allowing these 17 expenses to remain unpaid bearing interest as a mode of 18 investing their funds. The defendant claimed, upon 19 paying off the final amount due for principal and 20 interest, to be entitled to deduct the income tax upon 21 the amount due for interest as being yearly interest of 22 money within section 40 of the Income Tax Act 1853. 23 Held that the interest did not come been the words 24 'yearly interest of money' in section 40, and that 25 therefore the defendant was not entitled to deduct the</p> <p style="text-align: center;">Page 82</p>	<p>1 to pave and make up after notice duly served upon them, 2 requiring them to do so. The defendant was the owner of 3 premises in these streets and as such was ...(Reading to 4 the words)... by the defendant. Pursuant to section 32 5 of the Gateshead Improvement Act 1867, the plaintiffs 6 allowed time for payment, and pursuant to a standing 7 resolution fixed the rate of interest thereon until 8 payment at the rate of 5 per cent per annum. The 9 defendant from time to time paid to the plaintiffs 10 various sums on account of a proportion of such 11 expenses." 12 So first of all, all these statutory provisions, 13 1875, 1867, et cetera, and you'll notice just down the 14 page, toward the right hand side: 15 "In 1912 there remained a sum due from him on 16 account of the said expenses." 17 We don't know when it started from that statement, 18 but we can see that. 19 Then over the page, 885, one can see the argument 20 for the defendant, Lumsden. Lumsden as we say is in the 21 position of the debtor, it's like LBIE. They refer to 22 Goslings v Blake, the short term loan, and then refer to 23 section 40 of the Income Tax Act 1853, and they then 24 say: 25 "And therefore the customer was not entitled to</p> <p style="text-align: center;">Page 84</p>

<p>1 deduct income tax from such interest. The ground of the 2 decision in that case [that's referring to Goslings v 3 Blake] was that the loan was for a specified time less 4 than a year [referring to Lord Justice Bowen, and again 5 it's a passage referred to by my learned friends in 6 their skeleton]. We are dealing in this case with short 7 loans only, that is to say ...(Reading to the words)... 8 not intended to be continued and are not continued for 9 a long period. In order to take the case out of the 10 provisions of section 40, there must be a stipulation 11 that the loan shall not be for more than a year and the 12 person who relies upon that stipulation must prove it. 13 The money here has remained unpaid for years [for 14 years], the interest being calculated with reference to 15 a year and therefore section 40 applies." 16 That is, with respect, the argument of HMRC in this 17 case. That's the argument put forward on behalf of 18 Lumsden in that case. 19 MR JUSTICE HILDYARD: It goes on: 20 "Where an annual sum is payable and nothing is said 21 about income tax, income tax is deductible." 22 MR GARDINER: That's right, my Lord, you can see it again, 23 and it's again a similar authority as relied on in this 24 case, if you noticed just past the middle page of the 25 page of that argument when they refer to In re Barrie's</p> <p style="text-align: center;">Page 85</p>	<p>1 judgment: 2 "The sole point is whether upon payment of the 3 agreed balance of ...(Reading to the words)... He has to 4 show that he is authorised to make the deduction and 5 that involves showing that he is paying yearly interest 6 of money within the meaning of section 40 of the 1853 7 Act. Although the local authority have certain powers 8 under section 33 of the local Act to take possession of 9 the premises, which, had they exercised them, might 10 perhaps have made their position somewhat analogous to 11 that of a mortgagee ...(Reading to the words)... It was 12 apparently advantageous for the corporation." 13 But then: 14 "It is said that the payment of interest in this 15 case is a payment of yearly interest of money because it 16 does not show that there was any agreement setting 17 a short term of less than a year to the loan which in 18 fact the defendant was enjoying. The contention that is 19 in all cases, except where such a period is fixed by 20 agreement between the parties, there is a payment of 21 yearly interest of money within the meaning of 22 section 40 if the money remains for more than a year 23 outstanding and interest bearing." 24 That, with respect, is as close as it comes to the 25 arguments of HMRC in this case. Then he says the facts</p> <p style="text-align: center;">Page 87</p>
<p>1 Trusts, it then says: 2 "In re Craven's Mortgage [and again it's a case 3 relied on by my learned friends and I'm not going to go 4 to it] shows that in the case of a loan which may run on 5 beyond a year and on which the interest is calculable by 6 the year, income tax can be deducted from the interest." 7 So it's the same argument. It then refers to Bebb v 8 Bunny, and towards the end of that particular page, 9 towards the penultimate line: 10 "Here the plaintiffs consented to the money 11 remaining unpaid and to its bearing interest at the rate 12 of 5 per cent per annum and it remained outstanding for 13 many years." 14 We don't know, it could have been 30 years, but 15 I mean many years must be a number of years. 16 "Though they could have called it in at any time. 17 The course ...(Reading to the words)... therefore 18 entitled to deduct income tax." 19 And then one can see: 20 "Danckwerts' case ...(Reading to the words)... the 21 plaintiffs were not called upon." 22 That Danckwerts is the father of 23 Lord Justice Danckwerts, that was Count Otto Danckwerts. 24 And then Lord Sumner, and it's his judgment that we 25 respectfully very much rely on, the first break in his</p> <p style="text-align: center;">Page 86</p>	<p>1 are of the most meagre description, and just below the 2 middle of the page, there's a passage in the middle of 3 the page, a sentence beginning: 4 "If that case was made below, which I doubt, it was 5 not proved and upon the materials before us I cannot 6 infer a transaction of that effect." 7 That is an intended investment type transaction. He 8 says: 9 "All that we have is the fact that there was a debt 10 presently due incurred on account of the expenses, and, 11 if the Local Authority had chosen to enforce it, 12 presently payable, which debt the Local Authority under 13 the powers of section 32 of the local Act did not 14 immediately enforce and have not enforced for 15 a substantial period of time." 16 Here of course the position of the creditors is that 17 they couldn't enforce because of the administration, not 18 because they wanted to make a long term loan, and his 19 analysis of the case is that the Local Authority weren't 20 intending to make a long term loan, they were just 21 leaving the position in abeyance with the creditor, 22 allowing him to go on in that way. That's what he says 23 towards the end of that page, the penultimate sentence: 24 "All that the Local Authority did in this case was 25 to give time and to receive payment by instalments, the</p> <p style="text-align: center;">Page 88</p>

<p>1 amount of which was apparently left to the defendant, 2 with interest at the rate ...(Reading to the words)... 3 same rule must apply to the analogous case of interest 4 on purchased money." 5 And then we quote from <i>Bebb v Bunny</i> which we've 6 seen. And then there's passageway which my learned 7 friends refer to in their skeleton, so I had better read 8 it. After the reference to Lord Justice Bowen in 9 <i>Goslings v Blake</i>, my learned friends pick up the passage 10 beginning "whether or not": 11 "Whether or not the present case could have been 12 brought into line with the mortgage cases if it had been 13 shown by the evidence that the ...(Reading to the 14 words)... it is unnecessary to consider. It is 15 sufficient for the purposes of this case to say that no 16 such facts are shown here." 17 With respect, we find it quite difficult to see what 18 on earth in favour of their argument the Revenue 19 actually get out of that, because it seems to us wholly 20 against them. It is plainly contemplating a distinction 21 between a case where somebody intends to make 22 an investment giving rise to income accruing from time 23 to time and this situation, where fortuitously or 24 unfortuitously a situation has arisen and which is not 25 intended to have arisen, and that, it seems to us, is</p> <p style="text-align: center;">Page 89</p>	<p>1 "Truly speaking, there is simply a forbearance ... " 2 Here there's something more than a forbearance by 3 force of the administration. Debts are not recoverable 4 unless and until the administration determines them to 5 be recoverable. 6 "Truly speaking, there is simply a forbearance to 7 put in suit the remedy for a debt." 8 Again, directly referable here. 9 "The repayment might have been enforced at any 10 moment [no doubt the creditors would have loved to have 11 enforced it]. The debt might have been paid by the 12 debtor at any moment. It carried interest by law [in 13 that particular case, not so here] because under section 14 32 ...(Reading to the words)... could and did attach 15 a rate of interest to it. The fact that the rate of 16 interest is calculable at an annual figure is, as was 17 pointed out in <i>Goslings v Blake</i>, immaterial. The debt 18 here was well secured and the creditor, unlike the 19 creditor in <i>re Cooper</i>, did not desire immediately to 20 enforce payment of it. The plaintiffs were no doubt to 21 receive interest on it, but not in such a form as would 22 apply to it the words 'any yearly interest of money' in 23 section 40 of the Income Tax Act 1853. I am therefore 24 of the opinion that the burden falls on the defendant to 25 show he has a right to make the deduction. It has not</p> <p style="text-align: center;">Page 91</p>
<p>1 entirely consistent with all the other authorities, and 2 entirely against the Revenue's argument in this case. 3 And then towards the end of that page, four or five 4 lines up from the end, again a significant passage in 5 his judgment, he says: 6 "I do not say that the present case is concluded by 7 the conclusion in <i>re Cooper</i>, although I think it would 8 be difficult to distinguish it." 9 If I just pause there, <i>Cooper</i>, you will remember, 10 was the judgment debt case of seven days. He's saying 11 this case, the interest being outstanding, the 12 indebtedness being outstanding for years, he's saying 13 it's covered by <i>Cooper</i>. So again, if the argument of 14 the Revenue were right, it couldn't possibly be covered 15 by <i>Cooper</i>, because <i>Cooper</i> was a seven day period, this 16 is an umpteen years period. He's saying the principle 17 in <i>Cooper</i> covers it. Then he goes on by saying: 18 "But applying the principle underlying that 19 decision, I am unable to see how the words 'yearly 20 interest' can apply to this transaction. There is no 21 agreement for a short loan or a long loan. The debt is 22 due and repayment is not enforced. Only in that sense 23 is there a loan." 24 Those words, we would say, are particularly 25 applicable here.</p> <p style="text-align: center;">Page 90</p>	<p>1 been discharged and he fails in this appeal." 2 As I said earlier, that, we say, is this whole line 3 of authority, but that is the most obvious case, that 4 having regard to the factual situation arising that is 5 most relevant to our circumstance, the argument put up 6 on behalf of Mr Lumsden is, with respect, the like 7 argument at the very least to the argument that we've 8 seen in the Revenue's letters and in my learned friend's 9 skeleton in this case, and it is rejected for those 10 reasons, and for reasons in circumstances which are in 11 our respectful submission directly applicable to the 12 instant case. 13 So that's <i>Gateshead v Lumsden</i>, and we've quoted the 14 most relevant parts of it, not the part my learned 15 friend has relied on, but as I said, as far as that 16 passage is concerned, it seems to us that passage is 17 against his argument anyway. So those are the two 18 passages set out in paragraph 28 of our skeleton. 19 Then Mr Justice Rowlatt in <i>Garston Overseers v</i> 20 <i>Carlisle</i>, very much the same effect in paragraph 29 in 21 our skeleton. We pick up the quotation which we put 22 there: 23 "'Yearly' interest means substantially interest 24 irrespective of the precise time in which it is 25 collected, interest on sums which are outstanding by way</p> <p style="text-align: center;">Page 92</p>

<p>1 of investment as opposed to short loans, or as opposed 2 to monies presently payable and held over or anything of 3 that kind." 4 We do draw attention to what Mr Justice Rowlatt is 5 saying there, and it's interesting with 6 Mr Justice Rowlatt that quite often, if you read his 7 judgments in the tax cases, it's quite often different 8 from the judgment that he approves in the law reports, 9 but this is a reference to the judgment of the law 10 reports, so it's approved by him and its terminology, 11 and its terminology is very precise. So's contrasting 12 yearly interest on the one hand, which he says: 13 "Irrespective of the precise time which it is 14 collected, interest on sums which are outstanding by way 15 of investment." 16 As opposed to the other types of loans, so it's 17 short loans, but it's not just short loan loans. He 18 says: 19 "Short loans, or as opposed to monies presently 20 payable and held over or anything of that kind." 21 And we're within that latter description of this. 22 Garston is at tab 37. The headnote is actually very 23 short. One can see what it's about: 24 "The overseers of the poor for a certain district 25 kept a current account with a bank into which they paid</p> <p style="text-align: center;">Page 93</p>	<p>1 intended to accrue interest as that kind of thing, of 2 yearly interest. That again is this concept of yearly 3 interest being subject to deduction of tax at source, 4 et cetera, going right the way back in the legislation. 5 So, my Lord, it's here. The passage we've quoted, 6 and it's the bottom of 386, the latter part of 386, and 7 a small passage -- 8 MR JUSTICE HILDYARD: Broad result. 9 MR GARDINER: Yes, that's right. It's that bit. Then over 10 the page at 387, just in the middle of the page: 11 "It is no doubt contemplated that the balance will 12 continue for a long time, but what is the daily balance 13 ...(Reading to the words)... money payable on demand." 14 And again, he's recognising the fact that the 15 interest period was over all those years, the six years 16 or whatever. He says that's neither here nor there, 17 that doesn't make it yearly interest within the meaning 18 of the Act. 19 And then just following on, then, our paragraph 31, 20 Corinthian Securities v Cato, which is at tab 44. 21 I always remember the individual, Mr Cato, was I think 22 the longest standing pupil in the Middle Temple, who 23 took 28 years to take the exams. 24 MR JUSTICE HILDYARD: 28? 25 MR GARDINER: Yes, 28. He took them a number of times. He</p> <p style="text-align: center;">Page 95</p>
<p>1 the amounts collected by them as poor rate and out of 2 which from time to time they made the payments for which 3 they were liable. Under a longstanding arrangement with 4 the bank, interest was allowed by the bank half yearly 5 at an agreed rate [times, I'm afraid, have changed 6 nowadays. But anyway] without deduction of income tax 7 calculated upon the daily balances standing to the 8 credit of the overseers. The overseers, contending that 9 they were trustees for charitable purposes only within 10 section 105 of the Income Tax Act 1842 [that's a 11 charitable exemption], claimed an exemption from income 12 tax in respect of the interest on the ground that it was 13 yearly interest within that section ...(Reading to the 14 words)... was not yearly interest within section 105." 15 You can see down the page, this was interest paid 16 over a whole number of years, 1910, 1911, 1912, 1913, 17 1914, et cetera, but despite that fact, it was held not 18 to constitute yearly interest. And the particular 19 passage, I don't really want to draw a great deal of 20 attention to it, is page 386. 21 MR JUSTICE HILDYARD: Yes, you've set that out and I've read 22 that. I mean, I think Mr Justice Rowlatt seems to 23 regard this as a fairly plain case, because they were 24 merely monies that call, monies payable on demand. 25 MR GARDINER: Yes, it wasn't an investment, it wasn't</p> <p style="text-align: center;">Page 94</p>	<p>1 represented himself in this particular case and actually 2 won, so to his credit. But we're not concerned with 3 that. 4 Lord Denning you will see in the headnote, this was 5 a loan initially made on the supposed terms for six 6 months and then renewed. If one notices in the headnote 7 at page 378 per Lord Denning: 8 "Interest is yearly interest of money ...(Reading to 9 the words)... whether it was repayable on demand or 10 not." 11 That's what he identifies, and your Lordship is 12 quite right, Sir John Donaldson says, "I don't know 13 about that" subsequently. I think you can see the basis 14 of his judgment at 383, just below letter B, or at 15 letter B, it says: 16 "Although payable on demand it was unlikely that any 17 demand would be made so long as the interest -- " 18 MR JUSTICE HILDYARD: Sorry, where are you reading from? 19 MR GARDINER: Sorry, 383, the judgment of the Master of the 20 Rolls, Lord Denning, just at letter B. 21 MR JUSTICE HILDYARD: Yes. 22 MR GARDINER: "Although payable on demand, it was unlikely 23 that any demand would be made so long ...(Reading to the 24 words)... from an ordinary loan or mortgage. The 25 interest was yearly interest of money."</p> <p style="text-align: center;">Page 96</p>

<p>1 That's the basis upon which he puts it, and Sir John 2 Donaldson subsequently in Cairns v MacDiarmid says 3 "I don't know about that". But anyway, there's a lot of 4 authority to back up Lord Denning in that particular 5 case from the cases that we've seen. 6 Cairns v MacDiarmid is at tab 46. Again I can deal 7 with that very shortly, I think. This was -- the 8 headnote is long, I can state the case, really this was 9 a tax avoidance scheme and basically this was what was 10 called the advanced interest scheme. Essentially what 11 happened in these cases, this is an example of them, was 12 a taxpayer purported to borrow money for a number of 13 years, let's say five years, would pay all the interest 14 in advance on day one, so that was interest for five 15 years, and he would then by novation get rid of the 16 obligation to repay the loan to somebody else, who would 17 take it over and pay him what the right to receive the 18 amount of the repayment in five years' time would cost 19 at that particular moment of time. 20 So the intention of the parties as far as that loan 21 was concerned, albeit that in so-called contractual 22 terms it's suggested you were paying interest for 23 a period in excess of a year for a number of years, the 24 actual intention was that the loan would actually only 25 remain outstanding for a few days, and so they take the</p> <p style="text-align: center;">Page 97</p>	<p>1 interest, if calculated at a yearly rate and if the 2 intention of the parties is that it may have to be paid 3 from year to year, Bebb v Bunny and Corinthian 4 Securities v Cato ...(Reading to the words)... short 5 term and indeed a very short term investment, eg 6 overnight deposits, and such an investment does not 7 involve any annual interest, regardless of whether the 8 interest is calculated at an annual rate. On the facts 9 found by the Commissioners, the loan to Mr Cairns was 10 never intended to last for more than a few days, albeit 11 he was entitled to postpone repayment for two years. In 12 fact, as was always intended, his liability was 13 discharged within the week, not by repayment, 14 by novation. The payment of £5,000 is not, therefore, 15 annual interest." 16 So just two points that we make out of that. First 17 of all, when he's saying that the difference between 18 annual and what is short depends on the intention of the 19 parties, he's clearly in that situation, having in mind 20 the contractual situation of two people entering into 21 a contract, because it's the two people who are the 22 parties to the contract, who determine the terms of the 23 contract, so as to accord with their intentions. You 24 can't actually transpose that terminology in his 25 judgment to this type of case, because it is not my</p> <p style="text-align: center;">Page 99</p>
<p>1 view on -- they refer to Ramsay(?) and they take the 2 view that looking at it as a matter of reality this was 3 only intended to be a short loan, therefore it's not 4 annual or yearly interest, therefore you don't get the 5 deduction for yearly interest. 6 So that's what the case is about. The point that 7 Sir John Donaldson makes is on page 181, the final 8 paragraph the page, below letter H. 9 MR JUSTICE HILDYARD: This is on the non-Ramsay bit. They 10 decide it on two bases, don't they? 11 MR GARDINER: Yes, they say first of all it's not annual 12 interest, it's not yearly interest. 13 MR JUSTICE HILDYARD: Yes, and then they go on to Ramsay. 14 MR GARDINER: And, secondly, in any event, Ramsay would 15 apply and it fails for that reason, it's not real 16 interest at all. And then with respect, one would say 17 that they were correct on both bases. 18 From our point of view, the more relevant part of it 19 is the not annual interest part. Page 181, just below 20 letter H: 21 "It is well settled that the difference between what 22 is annual and what is short interest, depends on the 23 intention of the parties. Thus interest payable on a 24 mortgage provided for repayment of the money after six 25 months or indeed a shorter period, will still be annual</p> <p style="text-align: center;">Page 98</p>	<p>1 clients, the joint administrators, and it is not the 2 creditors in this particular case, who one might say are 3 parties to the situation, who have actually determined 4 the provisions that apply to the situation. It is the 5 legislature which has determined the provisions that 6 apply to this situation here, by the terms that it has 7 enacted in the Insolvency Act and the rules. And, 8 therefore, if one's trying to perceive what is the 9 relevant intention here, it is the intention of the 10 legislature in enacting what it has enacted, that is 11 what Sir John Donaldson would have been looking at in 12 a case like this, and looking at the purpose and the 13 consequence of what Parliament has enacted. And that, 14 we say, one can only discern from the terms of the 15 legislation, and here, with respect, we say correctly 16 determined from the terms of the legislation, but we do 17 actually have the assistance of that exercise having 18 already been undertaken by Mr Justice David Richards in 19 Waterfall IIA. 20 MR JUSTICE HILDYARD: I suppose on your case, you don't mind 21 about the doubt which was cast by reference to the 22 variety of loan instruments, but you say that the 23 difference, is this right, is between on the one hand, 24 money left outstanding at the will of the payee, and on 25 the other hand, some moratorium or forced or voluntary,</p> <p style="text-align: center;">Page 100</p>

25 (Pages 97 to 100)

<p>1 or some other impediment, on recovery?</p> <p>2 MR GARDINER: Yes, that is the essential distinction which</p> <p>3 I say flows through all those authorities. With the</p> <p>4 greatest of respect to Sir John Donaldson, the only</p> <p>5 authority he was referred to in this case was</p> <p>6 <i>Bebb v Bunny</i>, as far as that was concerned. <i>Corinthian</i></p> <p>7 <i>Securities v Cato</i>, he picks up and says "I don't know</p> <p>8 about that." But I mean they didn't do the analysis in</p> <p>9 the case, with respect, that we've attempted to do in</p> <p>10 our submission, and you can see that -- I mean yes,</p> <p>11 <i>Bebb v Bunny</i> and <i>Goslings and Sharpe</i> are referred to,</p> <p>12 but <i>Cooper</i> isn't referred to, <i>Gateshead</i> isn't referred</p> <p>13 to, and the rest of those cases.</p> <p>14 MR JUSTICE HILDYARD: Yes.</p> <p>15 MR GARDINER: And effectively, of course, much of it was</p> <p>16 overtaken by the <i>Ramsay</i> type argument.</p> <p>17 MR JUSTICE HILDYARD: Yes.</p> <p>18 MR GARDINER: And, of course, one remembers the Court of</p> <p>19 Appeal in those days, and I don't know how long the case</p> <p>20 went on for, but I would be very surprised if it went on</p> <p>21 for more than a couple of hours. (Pause)</p> <p>22 MR JUSTICE HILDYARD: Yes.</p> <p>23 MR GARDINER: So that, I think, is all I want to say about</p> <p>24 <i>Cairns v MacDiarmid</i>. The point, I think, I've already</p> <p>25 made, is in paragraph 33, the distinction between</p> <p style="text-align: center;">Page 101</p>	<p>1 not, and also adopted in the case of <i>IRC v Hay</i>. <i>Farmer</i></p> <p>2 is at 34 and <i>Hay</i> is at tab 38, and the way in which they</p> <p>3 approach it, and again we say helpfully, in <i>Scottish</i></p> <p>4 terminology, you can see the quotation that we have made</p> <p>5 there in paragraph 34. It says -- well perhaps if</p> <p>6 I just read the whole of that paragraph, it will save me</p> <p>7 going to the authority. He says that:</p> <p>8 "The natural inference is that a distinction is</p> <p>9 drawn ...(Reading to the words)... properly described as</p> <p>10 annual, the equivalent of yearly, though it may be paid</p> <p>11 at shorter terms, and interest that cannot be so</p> <p>12 described ...(Reading to the words)... and that,</p> <p>13 likewise, was approved in the other court of session</p> <p>14 case, <i>Inland Revenue Commissioners v Hay</i> [tab 38] by</p> <p>15 Lord Anderson ...(Reading to the words)... it must</p> <p>16 accrue over a period."</p> <p>17 So in effect there are three strands to the</p> <p>18 authority, but all coming down to the same things.</p> <p>19 There is the accruer over a period of time, which we say</p> <p>20 is essential. That also is recognised as being</p> <p>21 something that is there in all the cases where they talk</p> <p>22 about making an investment, putting out the money with</p> <p>23 the intention that it would give rise to interest income</p> <p>24 over a period of time, having an investment nature</p> <p>25 rather than circumstances being thrust upon them, so</p> <p style="text-align: center;">Page 103</p>
<p>1 a contractual case and us. We say in paragraph 33:</p> <p>2 "The reason for considering the ...(Reading to the</p> <p>3 words)... the quality and characteristics of the right</p> <p>4 to interest that have been created by the agreement</p> <p>5 between them, or in the case of statutory interest for</p> <p>6 the parties, <i>LBIE</i> and the joint administrators and the</p> <p>7 creditors, have not created the right ...(Reading to the</p> <p>8 words)... by legislation."</p> <p>9 As far as the creditors are concerned, one can say</p> <p>10 that the statutory (inaudible) has been created against</p> <p>11 them, the moratorium, et cetera:</p> <p>12 "Their intentions are not relevant in determining</p> <p>13 its nature."</p> <p>14 We say it is the legislature's intention.</p> <p>15 And I think in terminology, when we say "rather it</p> <p>16 is the legislators", I think we mean the legislature,</p> <p>17 the legislature's intention in creating the statutory</p> <p>18 right that is relevant:</p> <p>19 "Matters according to be determined are referenced</p> <p>20 to the characteristics of the right, as discerned from</p> <p>21 the legislation, as here determined by</p> <p>22 Mr Justice David Richards and <i>Waterfall IIA</i>."</p> <p>23 And then paragraph 34, we refer to what</p> <p>24 Lord Justice Johnson says in the <i>Scottish North American</i></p> <p>25 <i>Trust v Farmer</i>. It's another case on yearly interest or</p> <p style="text-align: center;">Page 102</p>	<p>1 that an interest liability arises almost by default, as</p> <p>2 per here, and thirdly, that you have to have something</p> <p>3 that is looking forward, a tract of future time. So at</p> <p>4 the outset, he must be talking about the intention at</p> <p>5 the outset, when he refers to <i>Goslings</i>. Looking at the</p> <p>6 outset, do you have something at the outset of a loan or</p> <p>7 indebtedness that is accruing forward, going forward, as</p> <p>8 a matter of time? That of course, for all the reasons</p> <p>9 that we've given, we say simply does not exist here.</p> <p>10 MR JUSTICE HILDYARD: It went to the House of Lords but they</p> <p>11 said nothing?</p> <p>12 MR GARDINER: Yes, that's right, my Lord, they don't use the</p> <p>13 terminology, perhaps because they weren't all Scottish.</p> <p>14 That, I admit. They don't dissent from the decision,</p> <p>15 they don't dissent from this particular quotation, but</p> <p>16 they don't use the same language.</p> <p>17 MR JUSTICE HILDYARD: There seems to be a reference in</p> <p>18 Lord Atkinson's speech at page 12 to <i>Goslings</i>, but maybe</p> <p>19 it's irrelevant. If it is, just tell me so.</p> <p>20 MR GARDINER: Yes. At page 12 of the --</p> <p>21 MR JUSTICE HILDYARD: Top right.</p> <p>22 MR GARDINER: Yes. (Pause) Yes, I don't find any difficulty</p> <p>23 with that particular passage, I must say --</p> <p>24 MR JUSTICE HILDYARD: No, but there's nothing you want me to</p> <p>25 look at?</p> <p style="text-align: center;">Page 104</p>

<p>1 MR GARDINER: No, as we pick it up, the real relevant part 2 of it is when he enumerates a number of propositions on 3 page 10. After the first bit, it's that paragraph, "Now 4 the authorities referred to ... establish the following 5 propositions", and then I think it's the fifth one, "and 6 that the loan must have a tract of future time, per 7 Lord Johnson Scottish North American Trust Limited". 8 Then I am going to go on to the quality of 9 recurrence. The only other authority which we wish to 10 add to what I've said hitherto, and I think I can add it 11 by just looking at the headnote, which is Moss' Empires 12 Limited v Inland Revenue which is at tab 40, and that 13 was a case on annual payments. I think as I said 14 earlier today, the concept of annual payments are in the 15 bones of all tax lawyers and the rest of it, but it's 16 just the point, and you can pick it up at the headnote, 17 I don't think I need to refer to anything else, but at 18 page 875, it's a decision in the House of Lords and it's 19 Lord Maugham. You can see that he held that "the 20 payments were annual payments", and then: 21 "Per Lord Maugham, the word 'annual' in the rule 22 must be taken to have the quality of being recurrent or 23 being capable of recurrence and in this case, the 24 payments had this quality." 25 One can refer to other authorities to that effect</p> <p style="text-align: center;">Page 105</p>	<p>1 MR GOY: I had rather thought I might have the equivalent of 2 the morning. Two and a half hours would be what I would 3 imagine. 4 MR JUSTICE HILDYARD: Right, so if Mr Gardiner stopped at 5 12, you would then have until 3.30, and Mr Gardiner 6 would then have a short reply. 7 MR GARDINER: I would be content with that, but if 8 your Lordship wants me to, I can certainly happily go on 9 another 15 minutes or so. 10 MR GOY: Or if we started at 10 o'clock in the morning, 11 would that give a bit more flexibility? 12 MR JUSTICE HILDYARD: I'm going do rather weakly say I will 13 abide by your preference really. 14 MR GARDINER: My Lord, should I go on? If your Lordship 15 listened to me another ten or 15 minutes or so and made 16 some more progress now? 17 MR JUSTICE HILDYARD: Are the transcribers all right? 18 Everyone else all right? 19 SHORTHAND WRITER: We are struggling a little bit. If it's 20 only 15 minutes, we can manage. 21 MR JUSTICE HILDYARD: All right. Mr Gardiner, shall we have 22 a further 15 minutes and we'll then -- I'm very happy to 23 sit at 10, if you think that is the safer course. 24 MR GARDINER: I suspect that if we have another 15 minutes 25 or so, we can easily finish by close of play tomorrow.</p> <p style="text-align: center;">Page 107</p>
<p>1 and all the rest of it, but we see from the very 2 beginning, the Bebb case and Vice Chancellor Page-Wood. 3 We've seen Goslings and they pick up this point about, 4 as your Lordship put it, the eiusdem generis sort of 5 rule of construction, yearly interest, annuities and 6 other annual payments. Annual payments inevitably have 7 the concept of recurrence within them. That, we say, is 8 therefore a quality that yearly interest necessarily 9 must have because it, likewise, is another annual 10 payment. 11 I don't know, my Lord, it's obviously entirely for 12 your Lordship. I'm quite happy to go on, but I think 13 we've made quite a lot of progress. If you think it's 14 an appropriate time -- I mean we could pause there which 15 might be a sensible place to pause, but I don't know. 16 MR JUSTICE HILDYARD: I'm in your combined hands. I need to 17 leave by 4.45/5 o'clock tomorrow. Obviously I kept you 18 out in the morning and so I don't want to deprive you of 19 any time that you need. I can sit late now or sit early 20 in the morning, or simply adhere to court hours, 21 depending on how long you feel that you need. 22 MR GARDINER: Well, my Lord, if we were to start at 10.30 23 tomorrow, I think I could guarantee that I wouldn't go 24 past 12 o'clock. 25 MR JUSTICE HILDYARD: Mr Goy, what do you say about that?</p> <p style="text-align: center;">Page 106</p>	<p>1 MR JUSTICE HILDYARD: Okay. 2 MR GARDINER: I had really got to paragraph 37 of our 3 skeleton, where we say "Is the interest under rule 288.7 4 yearly interest?" Perhaps if I just read the first 5 paragraph. We say: 6 "It is uncontroversial that statutory interest is 7 interest generally for tax purposes. This follows from 8 rule 288.7 itself. It mandates the paying of interest 9 ...(Reading to the words)... under section 183A [that's 10 at tab 8] and sections 369.1 and 371 ..." 11 Which are tab 7. 12 And, again, I don't I think I need take 13 your Lordship to it, because it's in those terms that 14 we've incorporated into that particular paragraph. Then 15 we say at paragraph 38: 16 "However, as explained above at paragraph 15, the 17 statutory interest does not accrue from day to day, it's 18 not payable from year to year. No period of accruer and 19 the interest is not payable unless a surplus has been 20 ascertained, following payment of the debts ...(Reading 21 to the words)... deduction of tax at source applies." 22 We say that is the tax law that I've dealt with 23 already. We then say that: 24 "That quality does not attach to yearly interest 25 because of the legislation and its proper</p> <p style="text-align: center;">Page 108</p>

<p>1 interpretation, and we say that follows from the 2 judgment of Mr Justice David Richards in Waterfall IIA, 3 summarised and quoted in paragraphs 15 and 16 above." 4 As I said when I opened, I want to come back to 5 those. If I could then come back to them now. It's 6 paragraph 13, where we set out rule 288 itself in our 7 skeleton. Obviously it's in the legislation bundle of 8 authorities but it's set out in full here, so I can deal 9 with it here. I'm sure your Lordship will be more 10 conversant with this than I. 288.1: 11 "When a debt proved in the administration bears 12 interest [so it bears interest prior to the company 13 being into administration], that interest is provable as 14 part of the debt, except insofar as it is payable in 15 respect of any period after the company entered 16 administration." 17 So pausing there, a debt of £100 bearing interest at 18 5 per cent per annum, let's assume, although I doubt 19 these debts are of that nature, but let's assume that, 20 then that will bear interest up to the date of entering 21 into the administration, but as far as rule 288.1 is 22 concerned, not thereafter. So it basically affects the 23 contractual position of the parties that from the date 24 of the administration, the interest does not accrue, it 25 does not continue to accrue:</p> <p style="text-align: center;">Page 109</p>	<p>1 "Any surplus remaining after payment of the debts 2 proved, shall before being applied for any purpose ..." 3 So any surplus, so you have to have a surplus after 4 payment of the debts proved, so the surplus only arrives 5 after the debts have been proved. So the surplus only 6 comes into being after the so-called principle amount 7 has been repaid: 8 "... be applied in paying interest on those debts 9 in respect of the periods." 10 So there is a small point, we make it in our 11 skeleton, that a small point of construction, that the 12 draftsman is careful in his terminology. Here in 7, 13 he's not talking about "after payment of the debts 14 proved shall, before being applied for any purpose, be 15 applied in paying interest on those debts for the 16 period", it's "in respect of the periods." Because he 17 is recognising that what he is doing is simply 18 a calculation by reference to a past period. So he's 19 talking about not the contractual interest accruing on 20 the debt, he's talking about a calculation calculated in 21 respect of the periods during which they have been 22 outstanding, since the company entered into 23 administration: 24 "All interest payable under paragraph 7 ranks 25 equally, whether or not the debts on which it is</p> <p style="text-align: center;">Page 111</p>
<p>1 "2. In the following circumstances, the creditor's 2 claim may include interest on the debt for periods 3 before the company entered administration." 4 So two points there. So it allows the creditor to 5 prove for interest on his debt, so contractual interest 6 on his debt, for periods before the company entered 7 administration. Again, the terminology is really quite 8 specific here. So it's talking about interest for that 9 period. Again, it must be talking about interest 10 accruing over that period, for that period. That's up 11 to, if I call it D Day, the administration: 12 "3. If the debt is due by virtue of a written 13 instrument and payable at a certain time, interest may 14 be claimed for the period from that time, to the date 15 when the company entered administration again. If the 16 debt is ...(Reading to the words)... to that of the 17 companies entering administration." 18 So all the provisions stop interest running, from 19 the moment that the company goes into administration. 20 So it stops the contractual accrual or obligation in 21 respect of the debt, from the date of the company going 22 into administration. And one notices, in particular, in 23 288.2, it's talking about interest on the debts for the 24 periods. Then we get to 7, which is our position. That 25 says:</p> <p style="text-align: center;">Page 110</p>	<p>1 payable, rank equally." 2 And indeed it may well be that there was a debt that 3 never carried any interest but in consequence of these 4 provisions, it gets interest and it gets interest at the 5 judgment rate. 6 So that's the rule in 288. Then we say this issue 7 was decided by Mr Justice David Richards, because he was 8 asked to apply, as it were, the rule in Bower v Marris 9 whereby in the past, in insolvencies, creditors have 10 been able to say "I will treat all the early payments as 11 payments of interest", and therefore the principle 12 remains outstanding for longer and that, of course, will 13 then increase the amount of interest payable to them. 14 And he was asked to apply that rule and he rejected the 15 application of that rule by reference to the 16 construction of the terms of 288. That is the point 17 that we summarised at paragraph 15. We say, and I won't 18 bother to read them out, but I would stress the points 19 in paragraph 15. They are, with respect, made out from 20 his judgment, each and every one of them, and they are 21 actually critical to the understanding of the point in 22 this case, in particular, the points that we make at 23 subparagraphs 4, 5, 6 and 7 of paragraph 15. 24 If I just read those out. We've asked your Lordship 25 to read them and I'm sure your Lordship has read the</p> <p style="text-align: center;">Page 112</p>

<p>1 substantial sort of part of his judgment that is 2 relevant to this case. 3 MR JUSTICE HILDYARD: I mean Bower v Marris occurred outside 4 a regime of statutory interest, didn't it? 5 MR GARDINER: Yes. 6 MR JUSTICE HILDYARD: And the question was whether it should 7 nevertheless apply, now that bankruptcy and liquidation 8 and administration provided for the payment of statutory 9 interest. 10 MR GARDINER: That's right, and, I mean -- perhaps if I read 11 out what he said as we summarise it, but I'm sure if 12 I were to use my own terminology, I'm bound to put it 13 slightly differently and I'm not sure that would help. 14 Subparagraphs 4, 5, 6 and 7, we say: 15 "The right to be paid statutory interest out of 16 a surplus under rule 288, is not a right to ...(Reading 17 to the words)... commencement of the administration and 18 the payment of the dividend or dividends on the proved 19 debts." 20 That's paragraph 149 of his judgment. 21 MR JUSTICE HILDYARD: Yes. 22 MR GARDINER: "5. The dividends cannot be appropriated 23 between the proved debts and interest accruing due under 24 rule 288 because at the date of the dividends, no 25 interest was payable."</p> <p style="text-align: center;">Page 113</p>	<p>1 if one notices that paragraph 129 starts after 2 paragraph 128, and after paragraph 128, he says: 3 "These are powerful submissions but I have concluded 4 that an application ...(Reading to the words)... is 5 incompatible with the regime established by rule 288." 6 Then he goes on to set out, 129 onwards, all his 7 reasons for so concluding. If I pick up just at the top 8 of -- well, paragraph 135, the last four lines of it: 9 "Importantly, interest is not therefore payable in 10 respect of any period after the relevant distribution. 11 An application of the principle in Bower v Marris will 12 involve the payment of interest in respect of periods 13 long after the distribution or distributions in 14 question." 15 But then the critical passages. 144, he says: 16 "There is a further strong factor suggesting that 17 Bower v Marris does not apply to the payment of 18 post-insolvency interest under the 1986 legislation. As 19 earlier discussed, the principle in that case is derived 20 from the legal rules as to appropriation of payments 21 ...(Reading to the words)... those rules that at the 22 date when a payment is made, there are two outstanding 23 debts payable by the debtor to the creditor. The source 24 of the debt may be, but not need be, a contract 25 ...(Reading to the words)... If only one debt is payable</p> <p style="text-align: center;">Page 115</p>
<p>1 That's paragraph 149. Now I pause there. That goes 2 back to the propositions I made earlier this afternoon, 3 our propositions 1 and 2. They're the same: 4 "6. The entitlement under rule 288 to interest is 5 a purely statutory entitlement, arising once there is 6 a surplus, after payment of the debts proved and payable 7 only out of that surplus." 8 That's paragraph 149 again. So those three points 9 all come from the same paragraph, that's why we 10 subsequently quote it in full in paragraph 16. And 11 then: 12 "7. The position is very different in relation to 13 interest on contractual debts, judgment debts or 14 analogous types of interest, for example ...(Reading to 15 the words)... deceased estate, where the interest 16 accrues due whilst it [that is the debt] is 17 outstanding." 18 That's a reference to paragraphs 109 to 114 and 145. 19 Then we say the critical passages in his judgment are in 20 that long passage. 129 is where he's actually set out 21 all the argument for the other side, and then he starts 22 from paragraph 129, saying "this is my analysis of what 23 is the right answer". Waterfall IIA is at tab 47. If 24 I perhaps just pick up the really critical passages 25 which are those four referred to there. One can see --</p> <p style="text-align: center;">Page 114</p>	<p>1 on that date, the payment by the debtor can, in the 2 absence of express agreement between the parties, be 3 applied only to that debt." 4 145: 5 "In applying the rules as to appropriation of 6 payments to the administration of estates, the 7 foundation remains that as at the date of payment from 8 the estate, it is treated as being made on account 9 ...(Reading to the words)... the creditor's claim that 10 the amount due from the co-obligor is to be calculated 11 by applying the amount of dividends from time to time 12 received from the bankruptcy estate of the other 13 co-obligor, in discharge of the interest then due and 14 the surplus, if any, in discharge ...(Reading to the 15 words)... that no creditor would apply any payment to 16 the discharge of part of the principle whilst any 17 interest remained due. In commenting on section 132 of 18 the Bankruptcy Act ...(Reading to the words)... that 19 interest which, by the course of administration in 20 bankruptcy, they had lost. If dividends were to be 21 attributed to principle instead of to the interest due, 22 the creditor would not have received interest upon his 23 debt to the same extent as he would if there had been no 24 bankruptcy. This is necessarily a reference to interest 25 falling due, apart from the insolvency process, during</p> <p style="text-align: center;">Page 116</p>

<p>1 the period of that process." 2 So that's important. That is a reference to the 3 interest falling due during, it would appear, the 4 administration process which of course it doesn't fall 5 due. 6 Then 149 is the one which is actually critical and 7 we've quoted it in full, and I don't know if I should 8 propose to read it again, but not having read it, as 9 I say, it is the most important paragraph of the lot. 10 MR JUSTICE HILDYARD: I have read it. By all means read it 11 again if you like, but it does -- I see why you rely on 12 it. 13 MR GARDINER: Yes. We've quoted it in full in paragraph 16. 14 So I'm not proposing to read it, but I would read 154, 15 which is the other one that we've particularly relied 16 on. 154: 17 "Mr Dicker(?) as counsel, submitted that the 18 principle in Bower v Marris was more fundamental than 19 simply requiring payments on account to be treated as 20 applicable, first to interest payable, at the date of 21 those payments. It was, he submitted, intended to 22 reflect an underlying principle that in an insolvency, 23 creditors should not be prejudiced by the late payment 24 of their debts." 25 Then there's this passage, this is the critical bit:</p> <p style="text-align: center;">Page 117</p>	<p>1 Mr Dicker makes, and Mr Justice David Richards says: 2 "I do not accept this submission." 3 So he doesn't accept what the Revenue rely on in 4 their letter. He gives the reason: 5 "It involves saying not only that the principle in 6 Bower v Marris is to be applied to the calculation and 7 payment of interest under rule 288 but also that the 8 principle itself is to be modified to fit in with the 9 regime created by rule 288. As will already be 10 apparent, I do not accept that the regime created by 11 rule 288 leaves room for the application of the 12 principle in Bower v Marris. I am further satisfied 13 that it contains no warrant for any statutory adjustment 14 to that principle." 15 Then he goes on to the next issue. And so, as 16 I said in opening, we apprehend that the other side, at 17 the moment at least, don't say that he was wrong, or 18 don't challenge that, but we do say, with a great deal 19 of respect, that they don't accept the rigour of his 20 judgment. They say that interest accrued during that 21 period, contingently on the payment of the surplus. 22 That's what Mr Dicker advanced as his contention in that 23 particular case and that was, for the reasons given by 24 Mr Justice David Richards, rejected and rejected for all 25 the reasons set out in his judgment.</p> <p style="text-align: center;">Page 119</p>
<p>1 "The statutory right to interest arising under rule 2 288 can be regarded with hindsight, as having accrued on 3 a day to day basis, since the commencement of the 4 insolvency process, albeit contingently on there being, 5 ultimately, a surplus." 6 If I pause there, that is part of Mr Dickers' 7 submissions. Then he says: 8 "Once the event occurs, the right to interest is 9 treated as having accrued during the relevant period." 10 And, again, that's part of his submission. But then 11 he says: 12 "I do not accept this submission." 13 Now, with respect, if one looks at that submission, 14 that is the basis of the Revenue's case in this 15 particular case. That is the basis of what they say in 16 their letter of 2 March, which I haven't shown 17 your Lordship yet, but I will show your Lordship 18 tomorrow. It's their letter of 2 March which I think is 19 at tab 5 -- 20 MR JUSTICE HILDYARD: I think you asked me to read it and 21 I did. 22 MR GARDINER: I'm sorry, my Lord, I didn't quite catch that. 23 MR JUSTICE HILDYARD: I said you asked me to read it and 24 I did. 25 MR GARDINER: I'm grateful. That is the submission that</p> <p style="text-align: center;">Page 118</p>	<p>1 That, I think, might be a convenient point, my Lord, 2 because I think what I want to go on to then, after 3 that, is that as it were, is our positive case and what 4 I wanted to go on to then, was picking up our skeleton 5 at paragraph 43, the position of the Revenue and to deal 6 relatively briefly, I suspect, with what we say about 7 what they say. That might be an appropriate time, my 8 Lord. 9 MR JUSTICE HILDYARD: Yes, that seems a good time. Now, do 10 you want 10.00 or do you want 10.30; will you agree 11 between you? 12 MR GARDINER: I would be quite content with 10.30. I think 13 we will finish it. 14 MR GOY: I would prefer 10.00. I just don't feel I would 15 like to be under pressure to finish more quickly than 16 I would otherwise want to, if that's of no difficulty. 17 MR JUSTICE HILDYARD: Mr Gardiner, are you all right for 10 18 o'clock? 19 MR GARDINER: I don't mind. 20 MR JUSTICE HILDYARD: We'll start at 10 o'clock because that 21 means we can't go wrong, he says with confidence, and if 22 we finish early, then well and good. 23 (4.57 pm) 24 (The court adjourned until 10 o'clock the following day) 25</p> <p style="text-align: center;">Page 120</p>

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