

Appeal number SC/3027/2008

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

ANDREW BERRY

Appellant

- and -

**THE COMMISSIONERS FOR HER MAJESTY'S
REVENUE AND CUSTOMS (Income Tax)**

Respondents

**TRIBUNAL: SIR STEPHEN OLIVER QC
IAN MENZIES-CONACHER**

Sitting in public in London on 12-15 and 26 October 2009

Aparna Nathan, counsel, for the Appellant

Malcolm Gammie QC, instructed by the **General Counsel for HM Revenue and Customs**,
for the Respondents

DECISION

1. The Appellant, Mr Andrew Berry, appeals against an amendment to his self-assessment in respect of the 2003-2004 year of assessment made on 20 April 2007. The amendment increased the tax due by £157,397.76. The amendment to Mr Berry's self-assessment reflects the denial of relief for losses that Mr Berry claims arose as a result of what he describes as the "Gilt Strip Planning".
2. The only issue for determination in this appeal is whether, as Mr Berry contends, he realised an income tax loss for the purposes of paragraph 14A Schedule 13 Finance Act 1996 ("FA 1996" : all statutory references, unless otherwise stated, will be to FA 1996) by virtue of entering into the Gilt Strip Planning.
3. A gilt strip is a UK Treasury Government stock issued by the Bank of England. "Strip" is an acronym for Separate Trading of Registered Interest and Principal flows which can be traded separately as zero-coupon gilts. Thus a three year gilt will have seven individual cash flows comprising six (semi-annual) coupon payments and a principal repayment. The strip market began in the UK on 6 December 1997 and broadly all new issues of conventional fixed coupon gilts are "strippable" (with a delay after the first issue date).
4. The object of the Gilt Strip Planning is to create an income tax loss representing the difference between the amount paid by a person for the particular gilt strip and the amount payable when a transfer is made of that gilt strip. Mr Berry claims that the Gilt Strip Planning created a loss of £400,000. He says that the amount paid by him for the gilt strip in question was £6.5 million, while the amount payable on his onward transfer was £6.1 million. His income tax loss was therefore £400,000. HMRC, the Respondents, say there was no such loss.

The legislation upon which the Gilt Strip Planning is based

5. ICTA 1988 section 18(1) charged "discounts" to tax under Schedule D. According to section 64 of that Act –

"Income tax under Case III of Schedule D shall be computed on the full amount of the income arising within the year of assessment, and shall be paid on the actual amount of that income, without any deduction."
6. Within that general framework section 102 and Schedule 13 of FA 1996 were enacted to deal with discounts on relevant discounted securities. Paragraph 1(1) of the Schedule provides that –

"Where a person realises a profit from the discount on a relevant discounted security, he shall be charged to income tax on that profit under Case III of Schedule D ..."

Paragraph 1(2) and (3) cover the situation where a person is to be regarded as realising a profit from the discount. Paragraph 14(1) states that –

“Every strip is a relevant discounted security for the purposes of this Chapter”.

7. Coming now to the specific provisions upon which the Gilt Strip Planning were based, para 14A of Schedule 13 (as it then was) provides:

“(1) A person who sustains a loss in any year of assessment from the discount on a strip shall be entitled to relief from income tax on an amount of his income for that year equal to the amount of the loss.

...

(3) For the purposes of this paragraph a person sustains a loss from the discount on a strip where [*so far as relevant*]

- (a) he transfers the strip ... and
- (b) the amount paid by him for the strip exceeds the amount payable on the transfer ... (no account being taken of any costs incurred in connection with the transfer or redemption of the strip or its acquisition).

The loss shall be taken to be equal to the amount of the excess, and to be sustained in the year of assessment in which the transfer or redemption takes place.

(4) In subparagraph (3) above, the reference to a transfer in paragraph (a) includes a reference to a deemed transfer under paragraph 14(4) above 9 and paragraph (b) shall be read accordingly.”

The term “transfer” is defined in paragraph 4(1) Schedule 13:

“... in this Schedule references to a transfer, in relation to a security, are references to any transfer of the security by way of sale, exchange, gift or otherwise.”

The term “strip” is defined in paragraph 15(1) Schedule 13 as:

“anything which, within the meaning of section 47 of the Finance Act 1942, is a strip of a gilt-edged security”.

The Gilt Strips used for the purposes of the present “Planning” are “strips” as defined.

8. “Relevant discounted security” is defined in paragraph 3 Schedule 13:

“Subject to the following provisions of this paragraph and paragraph 14(1) below, in this Schedule “relevant discounted security” means any security which (whenever issued) is such that, taking the security as at the time of its issue, the amount payable on redemption –

- (a) on maturity, or

(b) in the case of a security of which there may be a redemption before maturity, on at least one of the occasions on which it may be redeemed,

is or would be an amount involving a deep gain, or might be an amount which would involve a deep gain”.

The participants in the Gilt Strip Planning

9. “Abacus”, short for Abacus Wealth Planning, is the firm that designed, marketed and implemented the Gilt Strip Planning. In return, Abacus was paid a fee by its customers who included Mr Berry.

“Amaryllis Pride” was a limited company owned apparently by a charitable trust. It was established by, and its directors were provided by, and it was stated to be under the control of, S G Hambros Bank and Trust (Jersey) Ltd. It was established, according to an application of 2 December 2003 made to the Jersey Financial Services Commission “for the sole purpose of transacting in the purchase and sale of UK Government Gilt Strips as part of a financial planning exercise for a number of clients”. (In the context of Mr Berry’s “planning” Amaryllis Pride took over as “special purpose vehicle” from another such company called “Adamantine Investments”.)

“Mr Andrew Berry”, the taxpayer, is a UK resident individual employed by a financial organisation at the time called Prebon Marshal Yamane. Abacus had made a presentation at Prebon’s premises at which an explanation had been given of the “tax shelter” to be obtained from the Gilt Strip Planning. Abacus offered it as a “product”. Mr Berry gave oral evidence.

“Stuart Gower” was a director of the Offshore Tax Services Department within S G Hambros. He gave oral evidence.

“Andrew Robins” who also gave evidence is a chartered accountant and chartered tax adviser who at the time of the Gilt Strip Planning to which this appeal relates was a tax manager employed by Abacus.

“S G Hambros”, S G Hambros Bank and Trust (Jersey) Ltd, is a financial organisation with a registered office in Jersey. It provided facilities for the purposes of the Gilt Strip Planning.

“Louise Somerset” is a solicitor and at the time of the Gilt Strip Planning was a Director of Abacus. She gave oral evidence.

Designing the Product

10. The Gilt Strip Planning was designed as a product for sale to customers. The price charged to the customer was to be a percentage of the shelter that the customer was seeking. The design called for three ingredients.

11. The function of the first ingredient was to satisfy the formalities of paragraph 14A of Schedule 13. This consisted of (a) documentation to show the amount paid by the customer for the gilt strip, (b) documentation to show the amount payable on the transfer by the customer and (c) a gilt strip of the size required to achieve the shelter. The documentation showing the amount payable on the transfer by the customer had to evidence a transaction producing the requisite loss. For these purposes ingredient (b) was designed as a call option with an option price equal to the loss required by the customer and a strike price of a lesser amount (i.e. such amount as, when aggregated with the strike price, matched the amount paid by the customer for the strip). Underpinning the project was the legal proposition that the grant of an option is separate from and not part of the transaction that occurs on the exercise of the option; the option price will not, therefore, come into the reckoning as an amount payable on the transfer of the gilt strip.
12. It was a fundamental requirement of the arrangements as a whole (and the second ingredient in the design) that neither the customer nor S G Hambros nor the special purpose vehicle (eg Amaryllis Pride) could suffer any economic loss as a result of fluctuations in the price of the gilt strips. For this purpose documentation was required to ensure that the funds provided by S G Hambros and the sale proceeds of the gilts were always under the total control of S G Hambros.
13. The product appears to have been designed in reliance on a decision of the Court of Session in Scotland of 3 July 2003 upholding the appeal of *Scottish Provident Institution* [2003] STC 1035. For that purpose a third ingredient was designed into the product as protection against a possible HMRC attack on the grounds that the Gilt Strip Planning produced a preordained and therefore self-cancelling result. The advice received by the designers of the product was that there had to be a real possibility of the gilt strip price falling below a level at which the special purpose vehicle would wish to exercise its call option. Only by demonstrating a possibility that the customer might be left holding the gilt strip in a falling market could the product withstand the reasoning of the House of Lords in *Ramsay (WT) Ltd v IRC* [1981] STC 174, [1982] AC 300 as applied in *Furniss v Dawson* [1984] STC 153, [1984] AC 474 and place it on the safe side of the line established by cases such as *Craven v White* [1988] STC 476, [1989] AC 398 and later by *Campbell v IRC* [2004] STC (SCD) 396.

Selling the Product

14. The product was expected to have a short shelf-life. The Chancellor's "Pre Budget Review" was to be made on 10 December 2003 and Gilt Strip Planning was a likely candidate for legislative intervention.
15. Mr Berry became aware of the Gilt Strip Planning idea at the presentation made by Louise Somerset in the latter part of November 2003. The presentation had taken the form of a slide show supported by some explanatory material.

16. The explanatory material states that “the planning” has been devised by Abacus to be implemented by Abacus and a counter party bank in the Channel Islands. The material explains that –

“Under the planning, the taxpayer realises a capital gain that is exempt from capital gains tax and a loss that is allowable as a deduction for income tax purposes. The planning ... involves the sale and purchase of gilt strips to and from a special purpose vehicle provided by the Bank.”

17. The material goes on to explain how the planning makes use of a “principal strip” of a government gilt, being the right to receive the capital due on redemption of the gilt. It stresses that there must be uncertainty about the outcome: to quote –

“In order for the tax planning to be effective, there must be a real possibility that the market price of the gilt strip will, during the option/contract period, fall below a level at which the special purpose vehicle will wish to exercise its call option. ... On the basis of legal precedents and the advice of leading Tax Counsel, we consider that the statistical probability of this happening must be at least 7%.”

It goes on to say that in the event that the price does fall below “the water line” (i.e. the strike price under the call option) –

“... the purchase contract will provide that the taxpayer may default from completion, and instead may pay the special purpose vehicle fixed compensation approximately equal to the option premium In this way the taxpayer’s economic position is broadly preserved, as is the special purpose vehicle.”

18. The material then summarises the steps to be undertaken. These start with the customer identifying the amount of shelter he requires. He then signs a letter engaging Abacus and pays Abacus a fee of 1% of the required shelter. He is to be provided with a “letter of suitability” as to the choice of a suitable gilt strip. (No evidence of such a letter was provided and Mr Berry could not recall ever having received one.) A meeting is to follow at which the customer will complete a call option agreement and a purchase contract and at which the bank will provide him with a facility letter. The option premium is to be deposited in an account that the customer has opened with the bank. The customer is told –

“At the end of the option/contract period, your purchase of the gilt strip, and its sale under the option agreement, will occur in quick succession (it is anticipated that the interval will be mere minutes). Because you will buy the gilt strip before selling it, you will need to borrow funds from the Bank for a short period using [a facility letter provided to you by the Bank].

The loan will be repaid from the proceeds of sale of the gilt strip under the option agreement. The transaction costs will also be taken by the Bank at this

time, from the funds already deposited by you for this purpose [i.e. an amount deposited by the customer equivalent to the anticipated costs of the planning].

After the transactions are completed the Bank will supply you with the relevant contract notes.

Abacus will provide you with the information required to complete your tax return and claim loss relief in due course.”

19. In the explanation of “costs” are these words:

“The precise amount of your costs will depend upon the size of the loss required and the length of the option/contract period. In general, costs will be a lower percentage the larger the transaction, but will increase for shorter option/contract periods. Abacus will advise you of the approximate cost of the transactions when you confirm the amount of the required loss.

If the SPV does not exercise the call option then only the bank’s 0.5% fee for the borrowing facility, together with the Abacus fee of 0.85% plus VAT, is non-refundable.

If the SPV does not exercise its option as a result of movements in market values, you will be invited – as far as it is practicable and possible to do so – to participate in the planning afresh, in which case Abacus will make no further direct charge to you, and the bank’s borrowing facility will roll over at no further cost to you.”

20. Mr Berry explained in oral evidence his understanding of the risk of loss to him as having been capped by the £12,000 he paid into the scheme. He understood that if gilt prices fell “below the water line” the option would not be exercised and the cost would be limited and could be credited against the costs of undertaking the planning again – if that could be arranged. We accept that evidence.

Mr Berry engages Abacus

21. Mr Berry was one of at least twenty customers to buy the product, the “planning” of which was concluded by 9 December 2003. He and Louise Somerset had met on 21 November. On 28 November Abacus wrote a letter to Mr Berry containing their terms of engagement. These included:

“We will perform the following services ... :

- (a) We will advise you on the tax treatment of various transactions ... with principal strips of government gilts, intended to generate a capital profit and an income loss under the relevant discounted security tax legislation
- (b) We will facilitate and oversee the implementation of the Transactions, including introducing you to an appropriate counter

party ... and assisting you with completion of all relevant paperwork.”

The “counter party” was to be S G Hambros with which Abacus had agreed standard form scheme documentation. Mr Berry played no part in the negotiation or agreement of any documentation.

22. Under the heading “Investment Requirements” in the Schedule to the letter containing the terms of engagement are these words of explanation :

“We understand that the size of the gilt strip you intend to acquire will vary, depending on which gilt we advice you to be suitable. To determine this, we need to know the amount of income you wish to shelter.”

Against that is entered the sum of £400,000.

The Four Attorneys

23. As regards “the relevant paperwork” Abacus’ services of “assisting” involved Abacus providing their Four Attorneys. These were members of Abacus’ staff. Mr Berry signed a special power of attorney dated 2 December in favour of the Four Attorneys. Mr Berry explained that the power of attorney had been needed because Louise Somerset had told him that –

“... for administrative purposes, it will be simpler if I signed a Power of Attorney allowing her and a colleague to sign on my behalf all of the documents required for the planning”.

The power of attorney gave the Four Attorneys power to act on the customer’s behalf. The document authorised a minimum of two of the Four Attorneys acting jointly to execute the following documents:

The Forward Purchase Contract;
The Option ;
The SPC Premium Deposit Charge;
The SPC Premium Deposit Additional Charge (i.e. security interest agreement in connection with the option contract);
The Forward Purchase Contract Security Interest Agreement (“the FPC Security”);
The Bank Account Security Interest Agreement and
The Individual Notice and Acknowledgement.

Clause 3.2 of the Power of Attorney authorised a minimum of two attorneys, acting jointly:

“... to execute any deed or sign any document which may be required to do any other act, matter or thing which my Attorney shall consider necessary or expedient for the purposes of ... putting into effect any of the documents ...

and performing any of my obligations under the provisions of the documents.”

The power of attorney did not give the Four Attorneys or any of them power to borrow on Mr Berry’s behalf.

Preparations for the Gilt Strip Planning

24. S G Hambros’ function was to provide funding as part of the product and to supply and staff the special purpose vehicles. The provenance of Amaryllis Pride and the other special purpose vehicle was not explained to us: nor were we told what control S G Hambros had over the charitable trust that owned them. On 26 November 2003 S G Hambros wrote to the Jersey Financial Services Commission for approval of a £62 million overnight facility to be granted to a special purpose vehicle to enable a series of purchases and sales of gilt strips to be effected. To avoid any market risk the purchases and sales were to take place contemporaneously : the market maker was to take a pre-agreed turn on the price. The letter states that the special purpose vehicles are owned by a charitable trust but that control of the gilts remains with S G Hambros throughout. Approval was given on 2 December “for an exposure to Amaryllis Pride Ltd to the sterling value of £62 million for the purchase and sale of UK gilt strips until 10 December 2003”.
25. The next day, Wednesday 3 December, S G Hambros opened an account with the name Andrew Berry. S G Hambros made a “credit application” on 3 December to its headquarters in Paris. We understand this was granted. The application specifies as “Loan 1”, the sum of £390,000 to be made to Adamantine Investments Ltd. Apparently Adamantine was another of the special purpose vehicles employed in the planning (presumably for other customers). “In the event”, so we were informed by Abacus (quoting S G Hambros), Amaryllis Pride was used as the special purpose vehicle for Mr Berry’s planning. It was to borrow £390,000 “on demand terms with a review in one week”. The £390,000 loan was to be made to Amaryllis Pride to fund the premium payable to Mr Berry for the call option (see paragraph 34 below). The “purpose” was stated in the credit application to be to enable Mr Berry “to participate in the ‘Abacus Plan’, which is a structure designed to mitigate income tax liabilities”.
26. The credit application states of “Loan 2” (£5,309,901) that this is to be lent “overnight” to the special purpose vehicle to buy the gilt strips in the market. (The figures in the credit application are different from the actual amounts involved in the Planning itself.) This is to be followed by “delivery” of the gilt strips to Mr Berry for £5.3m (using the amount paid under the option plus the balance to come from the Bank). The application goes on to say that “simultaneously” the special purpose vehicle will exercise its option and pay £4.9m “which he immediately pays back to the bank and the special purpose vehicle receives the gilt strips back from” Mr Berry. The £5.3m loan by S G Hambros to the special purpose vehicle was to be overnight; the special purpose

vehicle will have “hedged” its purchase of the gilt strips by (the same day) entering into a matching contract to sell these in the market. £4.9m was to be lent “intra day” to Mr Berry to cover the cost (i.e. £5.3m) of the gilt strips which he was to buy from the special purpose vehicle (for £5.3m, i.e. the £4.9m loan plus the £390,000 option proceeds). By this means (we observe) Mr Berry obtains the gilt strips and is put in a position to deliver when the special purpose vehicle exercises its call option.

27. S G Hambros’ credit application states the purpose of the £4.9m loan to Mr Berry as “purchase of gilt strips from Adamantine Investment ...”. It explains that while specific permission has been obtained from the Jersey Financial Services Commission for exposures to the special purpose vehicle “the intra day exposure to the client has been exempted”. It goes on to say –

“The repayment of all the loan facilities are from the proceeds of other loans and the sale of the UK gilt strips purchased with loan proceeds ... [and] ... all facilities will be repaid in their entirety within one week of the initial option premium loan”.

28. Every transaction and every exposure is (we observe) perfectly matched or hedged so far as concerns S G Hambros and the special purpose vehicle. The credit application refers to concerns of tax counsel that HMRC might be able to run an argument under “preordination principles” that “the existence of the option should be ignored in these arrangements, particularly so, because there is no likelihood that the option will NOT be exercised”. As a result of those concerns, it says, “Abacus wish to put in place a variant of the planning with the intention of avoiding the possibility that the Revenue could run such an argument”. The credit application goes on to explain that the option premium corresponds directly to the income “to be sheltered” and that that amount “drives the remainder of the figures”. It illustrates how no economic loss will be suffered by anyone whether the special purpose vehicle exercises its call option (as planned) or not. Where the premium is duly exercised –

“The tax loss ... is the difference between the price paid by Mr X [£5.2m in the example] and that received by him for the gilt strips [£4.9m in the example]. The premium received by Mr X (£300,000 in the example) is tax exempt ...”

The credit application goes on to state what would happen should the market price of the gilt strip fall below the water line (i.e. to a price lower than the strike price under the option). We quote:

“In the unexpected event that the current market value of the gilt strips is below the exercise price, SPV will not wish to exercise its option. The purchase contract will be drafted in such a way that there is no specific performance requirement enforceable upon Mr X but rather Mr X can pay damages to SPV for the difference in the exercise price and the fixed price rather than completing the contract. This will equal the amount of the Option Premium paid to him originally by the SPV.

In either event the position for SPV and Mr X is certain and neither party, nor the bank, can suffer an economic loss as a result of the fluctuations in the price of the gilt strip.

From a credit perspective the bank's risk in this transaction has been entirely hedged and there will be no market risk at all. All other risks as regards the tax planning rationale have already been the subject of due consideration in the proposal [*relating to another named customer*].

As with [*the proposal for that other named customer*] the Bank is not providing any tax advice as this is being carried out solely by Abacus in conjunction with leading tax counsel. Bird & Bird will be responsible for preparing the documentation. SPV's directors will be provided by S G Hambros Trust Co in Guernsey and hence control will at all times be maintained within S G Hambros. Abacus has been well known to the bank for many years and currently has assets under administration in excess of US dollars 15 billion with over 40 directors and 400 staff.

The bank's fees will be approximately 1% of the amount of income to be sheltered to include commissions on the gilt purchases

The principal exposure we will have will be over a five day period and as per this example will be relatively small. However there is a requirement for the bank to enter into two intra day facilities to the SPV and to Mr X to deal with the sale and purchase of the gilt strip on day five. These loans are contemporaneous and the use of the funds and receipt of the sale proceeds are always under the control of the bank."

The Planning – 3 December 2003 : The First Business Day

29. By the First Business Day the Four Attorneys had taken on the role of facilitating, implementing and doing everything necessary or expedient for the purposes of the transactions required by the Planning. Mr Berry's oral evidence shows that he regarded his role in the Planning as finished once he had signed the power of attorney and paid over the sum of £12,000 as the price for the Product to S G Hambros on the First Business Day. He confirmed that Louise Somerset's presentation of the Planning accorded with his understanding of how the Product would work.

The Forward Purchase Contract and the Option are executed on the First Business Day

30. Mr Berry, acting through his attorneys, entered into the forward purchase contract to purchase, by 5.00pm on the Fourth Business Day after the date of the forward purchase contract gilt strips with SEDOL Code 0913904 with a nominal value of £24,953,210 at a price made up of four elements totalling £6,496,308 plus a "Spread Component".
31. Amaryllis Pride was the other party to the forward purchase contract.

32. The “Spread Component” was defined and essentially means the difference between the buy and sell prices of the gilt strips. Business Day was defined to mean a day other than a Saturday or a Sunday.
33. Clause 2.1 of the forward purchase contract required Mr Berry to deliver a purchase notice in the prescribed form to Amaryllis Pride by 5.00pm on the Fourth Business Day after the date of the forward purchase contract together with evidence of the receipt of the purchase price said to be payable to Amaryllis Pride. In the event of the failure to deliver a purchase notice and/or the evidence of receipt of the purchase price, Mr Berry was liable to pay an amount, referred to as “the Liquidated Sum”: this was made up of £390,000 plus the Spread Component.
34. Also on 3 December 2009 Mr Berry, through his attorneys, sold a call option to Amaryllis Pride and they entered into an option agreement, under which £390,000 was to be paid by Amaryllis Pride. “Account Statements”, apparently compiled on later dates, record Mr Berry as being credited with £390,000 with a “value” date of 3 December and Amaryllis Pride being debited with the same amount on the same “value” date. The terms of the option provided that it could be exercised for a limited period of one day, that period to commence at 4.00pm on the Fourth Business Day after the option, i.e. on 9 December, and ending at 5.30pm on Fifth Business Day after the date of the option, i.e. on 10 December. The option gave Amaryllis Pride the right to acquire the gilt strips at the total price of £6,102,308.
35. On 3 December 2003 S G Hambros wrote to Mr Berry offering a credit facility (“the Facility”) to borrow up to £6,102,308 or such other sum as might be agreed by S G Hambros from time to time for the purpose of assisting with the purchase of the gilt strips. No interest was chargeable but an arrangement fee was payable to S G Hambros. In accordance with the terms of the Facility, at Mr Berry’s request to draw on the Facility an advance of sums would be made to Amaryllis Pride in discharge of the purchase price of the gilt strips. In the events that occurred, an arrangement fee of £2,000 was debited to Mr Berry and the Facility was drawn down in full. The facility letter was signed by two of the Four Attorneys for Andrew Berry. (The special power of attorney granted to the Four Attorneys made no provision for the Four Attorneys either to borrow money or to sign any facility letter.)
36. With one exception the security documents and other related documents set out in paragraph 23 above were signed by Amaryllis Pride and S G Hambros. One of the security documents, “the FPC Security” was never signed. Subject to that, their execution enabled S G Hambros to make good its commitment to the Jersey Financial Services Commission expressed in the application letter of 26 November 2003:

“The SPV’s account with the Bank will be overdrawn overnight, however, it must be stressed that the timing of the trade settlement does not in any way

affect the risk as there is no market/price risk and as the Bank will transact the purchase, hold the gilts in custody and transact and deliver the gilts as part of the sale, control remains with the Bank throughout. Furthermore the gilts are at all times charged to the Bank as collateral under bespoke documentation which has been prepared by the Bank's London based legal advisers, Bird & Bird, as the transaction is carried out under English law. The Bank is also in control of the SPV directors”

8 December 2003 : the Third Business Day : Gilt strips are bought and sold

37. S G Hambros operate a custodian account with a third party bank which in turn operates a nominee client account arrangement with CREST. S G Hambros maintains a separate sub-account for each client to record that client's holdings of securities.
38. On Monday 8 December, a “Transaction Advice” showed an acquisition of gilt strips from an independent third party. Amaryllis Pride is referred to as the holder. For a sum of £57,969,432 debited to Amaryllis Pride, Amaryllis Pride obtains £218,340,611 UK 4¼% 7 June 2032 Treasury Strip. Delivery date is stated to be 9 December 2003.
39. Also on 8 December is a Transaction Advice showing a sale of £218,340,611 nominal of UK 4¼% 7 June 2032 Treasury Strip by Amaryllis Pride to a third party purchaser. Delivery date is 10 December. The price is £57,836,681.
40. These transactions (we observe) ensured to Amaryllis Pride enough gilts to cover the planning requirements of all the customers buying the product for which Amaryllis Pride has been made the special purpose vehicle; the transactions ensure an exit to Amaryllis Pride at no loss (other than the “spread” between the buying and the selling prices) should the value of the gilts fall below the striking prices under the options granted by customers such as Mr Berry.

The Fourth Business Day (9 December)

41. At 4.36pm (i.e. 24 minutes before the end of the “sale date” in the forward purchase contract) the Four Attorneys, represented by Louise Somerset and Andrew Robins, reappeared in the planning and faxed a signed copy of a purchase notice. In this Andrew Berry “requires SPC to transfer the gilt strips to him in accordance with Clause 2 of the forward purchase contract”. Stuart Gower of S G Hambros, who was in the office and ready for the transactions, received a telephone call from Louise Somerset and Andrew Robins at about 4.40pm and by 4.45pm the purchase notices have been received in his office. The purchase notices confirm that “the conditions set out in Clause 2.1 of the [forward purchase contract] have been satisfied”.

42. An “accounting set inquiry”, timed at 4.41pm, records the “purchase of gilts” by Andrew Berry from Amaryllis Pride: the “amount” is recorded as £6,502,308. A transaction advice shows £24,953,213 nominal of 4¼% Treasury Strip 7 June 2032 as being “delivered” from the Amaryllis Pride account to an account held in the name of Andrew Berry. The price is shown as £26.55 per £100 nominal. This was an inaccurate entry : the price should, according to a corrected transaction advice of 7 January 2004, have been £26.058 per £100 nominal.
43. An accounting set inquiry of 5.15pm on 9 December records Amaryllis Pride’s “exercise of option over gilt strip”. The amount is shown as £6,102,308. A Transaction Advice records that £24,953,213 of 4¼% Treasury Strip 7 June 2032 at a price of £26.55m is transferred from Amaryllis Pride to Mr Berry’s account. (This again was an inaccurate entry: the price, according to the corrected Transaction Advice of 7 January 2004, should have been £26.455m.)
44. Those transactions brought to an end the Gilt Strip Planning.

The rival contentions

45. The case for Mr Berry, presented by Aparna Nathan, is that he acquired beneficial ownership of the gilt strips. Nothing prevented him, legally or otherwise, from dealing with the gilt strips once they were in his ownership until such time, if ever, as the option was exercised. From the moment when he delivered the purchase notice in the prescribed form to Amaryllis Pride he was the owner of the gilt strips and, although they were subject to a charge in favour of S G Hambros, he was in the same position as any other person who has given a charge over his property. When the option was exercised, Mr Berry was required to sell the gilt strips to Amaryllis Pride. That contention is essentially based on the primary contention for Mr Berry in which, to quote from the Appellant’s Reply, he “denies that the documents should be considered as part of a package. Each is a separate document, legally independent of the others and so should be construed independently.” The option premium, being the amount paid when Mr Berry did not own the gilt strips, could not properly be included as part of “the amount payable on the transfer” within the meaning of paragraph 14A(3)(b). So examined, the transactions result in the loss determined for purposes of the “closely articulated” and “purely mechanistic computational provisions” of paragraph 14A of Schedule 13, namely the difference between what Mr Berry paid to acquire the gilt strips and what he received on the transfer of them to Amaryllis Pride; see the approach of the Special Commissioners in *Campbell v IRC supra*.
46. HMRC argue that the reality of the arrangements is that the product was designed and sold to customers as a package. As such the package was intended to be carried through from beginning to end and it was never intended to involve any customer, such as Mr Berry, in any loss within the meaning of paragraph 14A and never in fact did so. Thus, on the proper interpretation of paragraph 14A of Schedule 13, which requires that the taxpayer claiming a loss

should have “sustained a loss from the discount” in the year as a result of two transactions being an acquisition and a transfer in respect of which he has paid something and received less for the subject matter of the transaction, he fails to satisfy the statutory test. The alleged 7% “statistical risk” (see paragraph 54 below) that Amaryllis Pride would not exercise the option to reacquire the gilt strips was a meaningless sham. Even if it had had any reality, it would still fall to be ignored in applying the relevant legislation. This is because it was a commercially irrelevant contingency that had been installed as part of the package: see the approach of the House of Lords in *IRC v Scottish Provident Institution* (2004) 76 TC 538.

Conclusion

47. Adapting the words of the House of Lords in *Barclays Mercantile Business Finance Ltd v Mawson* (2003) 76 TC 446 and [2005] STC 1, the question for us is whether paragraph 14A of Schedule 13, construed according to its purpose, intended to apply to the transactions comprised in the Gilt Strip Planning viewed realistically.
48. The purpose of the statutory provision is identified in the opening words of paragraph 14A(1), namely – “A person who sustains a loss in the year of assessment from the discount on a strip shall be entitled to relief from income tax on the amount of his income for that year according to the amount of loss.”
49. The decision in *BMBF* establishes that it is irrelevant to the construction of the particular provision that the arrangement is designed to produce a tax advantage or, absent any specific anti-avoidance wording, that one or more component parts of the transaction have no commercial or investment purpose but have been inserted for tax reasons. Nonetheless, in determining the reality of the transaction, the fact that the arrangements were designed and implemented as a scheme or package, whether to achieve a tax or some other advantage, will be a relevant consideration in determining as a factual matter the reality of the transaction.
50. The House of Lords in *IRC v Scottish Provident Institution supra* 76 TC 538 was concerned with the question whether “entitlement” to gilts relied upon to found a loss claim could be established in circumstances where the right upon which the entitlement depended could be cancelled by the exercise of an option. The option in question had been matched by a separate but distinct cross-option. The special commissioners had found as a fact that there had been an outside but nonetheless real possibility that circumstances might occur in which the two options would not be exercised so as to cancel each other out. The House of Lords nevertheless went on to ignore the contingency that had been built into the scheme to produce that finding of fact and construed the relevant legislation by reference to the reality of the arrangement and whether the relevant statutory provisions, construed purposively, were intended to apply to that reality. In this connection we mention the decision of Arden LJ in *Astall v HMRC* 2009

EWCA 1010 Civ at para 34 where she said of the fact that “a real commercial possibility has been injected into a transaction does not mean it can never be ignored”:

“It can be disregarded if the parties have proceeded on the basis that it should be disregarded.”

51. We will need to address the question whether, in the present circumstances, there was a real possibility of the special purpose vehicle (Amaryllis Pride) not exercising the option. If there was, we will examine whether the possibility was so much part of the Gilt Strip Planning scheme as to affect the reality of the arrangements by reference to which paragraph 14A of Schedule 13 are to be applied.
52. Turning now to the specifics of the present case and assuming that Mr Berry obtained ownership of the gilts when he exercised the purchase notice, is that enough for paragraph 14A? We observe in parenthesis that it has not been obvious to us where legal ownership of the gilts lay at the critical time, i.e. between 4.45pm and 5.15pm on the Fourth Business Day. They were registered in the name of a third party bank. They were charged to S G Hambros to protect the loan to Amaryllis Pride and to enable Amaryllis Pride to meet its own obligations to sell on the gilts to the third party purchaser on the Fifth Business Day. All changes effected for the purposes of the Gilt Strip Planning were recorded as account entries leaving S G Hambros’ control undisturbed.
53. In the context of paragraph 14A the service of the purchase notice and the consequent activation of the forward purchase contract were said, for Mr Berry, to have given him an entitlement to the delivery of the gilt strips in return for an “amount paid” of £6.5m for the strip. However, viewing those transactions as part of a package (as HMRC see it), if Mr Berry’s entitlement was bound to be cancelled by Amaryllis Pride’s exercise of its option, then in a practical sense Mr Berry will have had no entitlement to the gilts. Moreover, if for all practical purposes the gilts will not have been placed at Mr Berry’s disposal when he serves the purchase notice (and satisfies the cash conditions of the Forward Purchase Contract), Mr Berry will have had no real ability to assert either that the gilt strips were transferred to him such that for purposes of paragraph 3(b) he paid an amount “for the strip” or that he transferred the strips for purposes of paragraph 3(a). All depends upon whether the admitted scheme “amounted in practice to a single transaction”: see the words in the House of Lords in *Scottish Provident Institution* at paragraph 19. A finding that the taxpayer who participates in the scheme and takes a position in the gilt strips market at a real and significant risk to himself could result in a conclusion that the scheme was not to be regarded for tax purposes as a single transaction. Did Mr Berry take any such risk? A further examination of the facts is now required.
54. It will be recalled that Abacus received advice that there had to be a real possibility that the market price of the gilt strips would, during the option/forward contract period (i.e. between the First Business Day and the

Fourth Business Day) fall below a level at which the special purpose vehicle would wish to exercise its call option. Abacus had, on the basis of advice, taken the statistical probability of that happening as being at least 7%. Abacus learnt from S G Hambros that Bloombergs provided the standard trading screen used by S G Hambros to identify prices for gilt strip options based on different economic models and historic price details. The screen has a so-called “Delta” figure to show the probability of an exercise or strike price being at or below the open market of a stock at the option’s maturity. Thus a Delta of 0.93 would represent a 93% chance of an option being exercised on maturity. Following from that the price at which the option was to be sold by Mr Berry to Amaryllis Pride was fixed at the prevailing rate for an option over the gilt strips in question with a Delta of 0.93.

55. The effect of the letter of engagement is that Abacus undertakes to provide Mr Berry with £400,000 shelter (from which £10,000 is subtracted for fees etc). Starting from that, it appears, £390,000 was taken as the option price and it was calculated that the strike price should be £6,102,308. To make the figures balance, £6,502,308 (i.e. £6,102,308 plus £390,000 option price plus £6,000 “spread component” and £4,000 as “third component”) worth of gilts had to be purchased for Mr Berry’s Planning.
56. The risk was said for Mr Berry to be based on the probability that by the end of the Fourth Business Day the option would not be exercised because the gross value of the gilt strips had fallen below the “water line” and Mr Berry would be left holding the strips. But, until the purchase notice has been served, Mr Berry has no gilt strips and so is exposed to no risk. If the value of the gilt strips held up he would serve the purchase notice and buy the gilt strips from Amaryllis Pride and Amaryllis Pride could then exercise its option to purchase them. Mr Berry would then have lost nothing, and only incurred the cost of buying the package. If the value of the gilt strip had fallen below the water line by the Fourth Business Day, Mr Berry would have chosen not to serve the purchase notice and Amaryllis Pride would have decided not to exercise the option to purchase them. This was contemplated by the parties who did not envisage that Mr Berry would have to complete the purchase: see, for example, the credit application referred to in para 28 above. Mr Berry (who had already been credited with £390,000 as the option price) would be debited with that amount plus the spread component as the so-called liquidated damages under the Forward Purchase Contract; overall he would have lost nothing. S G Hambros were completely protected by the matching sale of the gilts purchased on the Fourth Business Day and completely protected by the charges in their favour.
57. In theory the Four Attorneys might have served a purchase notice and bought gilt strips from Amaryllis Pride and Amaryllis Pride might have decided not to exercise its option to purchase them. In theory the Four Attorneys might have chosen not to serve the Purchase Notice while Amaryllis Pride might have exercised its option to purchase them. Bearing in mind that S G Hambros was completely protected and that it had complete control over all the funds put in to

make the Gilt Strips Planning work and that Amaryllis Pride stood to lose nothing, it is inconceivable that those eventualities would have happened. It would have required Amaryllis Pride and the Four Attorneys to have acted so irrationally as to defy credibility. The reality is that the parties proceeded with the Planning on the basis that the possibility of Mr Berry being exposed to any real risk of being left holding the gilt strips in a falling market should be disregarded. See *Astall supra*.

58. We recognise the 7% risk that the option might not be exercised using the information drawn from the Bloombergs screen; but that is not the same thing as saying that Mr Berry is at risk of loss. He is kept virtually harmless from the start because, as we have observed, he has the opportunity of backing out of the forward purchase contract; in which case the £390,000 is taken from him as liquidated damages, instead of it being debited to him as consideration for the purchase of the gilt strips.
59. So far our examination has been of the documentation and of the steps involved in the Gilt Strip Planning itself. This has indicated to us that any risk to the Bank, to Amaryllis Pride and to any of the participators in the Gilt Strip Planning was a façade. It had no reality. It was built into the Gilt Strip Planning scheme, but the parties proceeded on the basis that it should be disregarded.
60. This is confirmed by the oral evidence. Mr Berry, for example, accepted that the £12,000 that he put into the scheme was the cap on his risk. He was unable to suggest any other significant risk that the scheme might involve. Mr Berry had been sold the Gilt Strip Planning on the basis that he would not be left holding the gilt strips. His evidence was clear that if any of the gilt strip prices fell the option would not be exercised and any fees incurred by him could then be credited in part against the costs of undertaking the planning again. His ignorance of the implementation of the scheme is borne out by the fact that he left Abacus, through the Four Attorneys, to complete all the details in the agreements and to carry the transactions through. He knew that gilts of substantial value were to be involved in the scheme but he was completely unaware what denominations and classes of gilts were to be purchased and how much was to be borrowed by him and on what terms. He made no formal application for any loan. And the facility letter, signed by two of the Four Attorneys without any express authority from him, committed him to pay a fee of £0.5% of the facility amounts (£30,000) whereas his understanding had been that the scheme would cost him £12,000 in all.
61. The impression we obtained from the evidence was that the paperwork was there largely to protect S G Hambros. Even then it was processed without any close interest from anyone. For example the Four Attorneys failed to execute the FPC security; they had no express authority to execute the Facility Letter and to borrow and the Facility Letter, as noted, charged Mr Berry nearly three times what he had been told he was to pay. (The Four Attorneys, it will be

recalled, had at least twenty other Gilt Strip Plannings going through at the same time). Moreover the accounting entries, which produced a self-cancelling outcome, were made some days after the event. We observed that the entries for the option premium of £390,000, said to have been credited to Mr Berry on 3 December, were recorded on 8 and 9 December. Those features tell us that the Four Attorneys were purporting to commit Mr Berry to an intra day liability of £6.1m to enable the gilt strip planning scheme to be processed at its conclusion; and the accounting entries were made to provide evidence of steps in the scheme.

62. The implementation of the Gilt Strip Planning was exactly as the parties had intended. The self-cancelling result was entirely in line with their expectations which were that Amaryllis Pride and the Bank would be protected by the matching purchase and sale of gilt strips in the market and that Mr Berry would pay his fee. This leaves the option contract and the forward purchase contract and the associated debits and credits entries as ingredients in a single scheme. The scheme was designed to ensure that no “real” money ever reached Mr Berry. The £390,000 “premium” may have been credited to him; but it was retained under the Bank’s control for use in financing the exercise of the forward purchase contract. The proceeds of sale when the option was exercised were to be applied in discharging Mr Berry’s intra-day liability to the Bank. The gilt strips were kept securely under the control of the Bank and away from the hands of Mr Berry; they were needed to meet Amaryllis Pride’s agreement to sell them to the outside third party.
63. Looking at the transactions in the realistic manner required by the House of Lords in *BMBF v Mawson* and *Scottish Provident Institution* and construing paragraph 14A of Schedule 13 in the light of what it requires, we conclude that no loss was sustained by Mr Berry; nor was any amount paid by him for the gilt strips, nor was there any transfer of the strips. The present transactions are different and distinguishable from the two separate transactions found in *Campbell, supra*. There, the reality of the taxpayer’s transaction comprised first, a subscription for “relevant discounted securities” at an overvalue and, second, a gift of those securities to his wife. The reality of the transaction was not a gift to the company issuing the securities nor was it a gift to his wife.
64. For those reasons we have concluded the appeal fails.
65. In case the matter should become relevant we mention that HMRC contended that the scheme was based on a sham. In essence their case proceeds by pointing out that the contractual documents, if taken at face value, are designed to suggest four possible outcomes. The first is that Mr Berry could serve a purchase notice and buy gilt strips from Amaryllis Pride under the forward purchase contract but that Amaryllis Pride could then decide not to exercise its option to purchase them. The second is that Mr Berry could choose not to serve the purchase notice under the forward purchase contract but that Amaryllis Pride could exercise its option to purchase them. The third is what actually

happened. The fourth is that Mr Berry could choose not to serve the purchase notice under the forward purchase contract and that Amaryllis Pride could decide not to exercise its option to purchase them.

66. The evidence shows, say HMRC, that the agreements cannot be taken at face value because neither the first nor the second possible outcomes were ever intended by the parties. Instead what the parties had intended was that if Mr Berry served a purchase notice Amaryllis Pride would exercise its option and that if Mr Berry did not serve a purchase notice Amaryllis Pride would not exercise its option. The documents should therefore be construed accordingly with the result that Mr Berry acquired no beneficial ownership in the gilt strips and neither paid nor received any amount in respect of them, his only expenditure being fees he paid to Abacus and to the Bank.
67. If we had had to decide the point we would have concluded that transactions and the documentation were not a sham, either in their entirety or in part, in the *Snook v London and West Riding* [1967] 2 QB 786 sense. There was sufficient legal reality to displace a conclusion of sham. What was missing was the tax reality in the sense contemplated by the House of Lords in *Scottish Provident Institution*.
68. Appeal dismissed.