

FACV000004/2003

FACV No. 4 of 2003

IN THE COURT OF FINAL APPEAL OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION
FINAL APPEAL NO. 4 of 2003 (CIVIL)
(ON APPEAL FROM CACV NO. 118 OF 2002)

Between :

THE COLLECTOR OF STAMP
REVENUE

Appellant

AND

ARROWTOWN ASSETS
LIMITED

Respondent

Court: Chief Justice Li, Mr Justice Bokhary PJ, Mr Justice Chan PJ,
Mr Justice Ribeiro PJ and Lord Millett NPJ

Dates of Hearing: 20 - 23 October 2003

Date of Judgment: 4 December 2003

J U D G M E N T

Chief Justice Li :

1. I have read the judgment of Mr Justice Ribeiro PJ and that of Lord Millett NPJ and agree with them.
2. The decision in **Ramsay**, drawing on the approach in United States cases particularly that of Judge Learned Hand, was a landmark decision. It has subsequently been applied and developed in a number of cases. There has been a tendency to treat judicial statements in some of the cases as laying down a rigid code-like approach. This has given rise to unnecessary confusion and complication.
3. It is important to return to the roots of the **Ramsay** approach. In essence, the approach applies the purposive approach of statutory interpretation to tax statutes, particularly relief and exemption provisions therein. And it involves a realistic analysis and assessment of the facts and the transactions in question. These are the fundamentals which must be borne in mind when considering the application of the **Ramsay** approach to tax avoidance schemes.

Mr Justice Bokhary PJ :

4. In this case the Collector of Stamp Revenue advances three discrete grounds in support of his claim to stamp duty. For the reasons given by Lord Millett NPJ, I reject the first two grounds. The third ground is the one based on the approach that takes its name from the decision of the House of Lords in **WT Ramsay Ltd v. IRC** [1982] AC 300. I respectfully and entirely agree with Lord Millett NPJ's masterly elucidation of the true nature and scope of that approach and also with Mr Justice Ribeiro PJ's valuable analysis of the cases. In common with all the other members of the Court, I take the view that the Collector's third ground is well-founded so that his claim to stamp duty succeeds upon a correct application of the **Ramsay** approach to the circumstances of this case. Accordingly I too would allow the appeal to uphold that claim with costs here and below.

Mr Justice Chan PJ :

5. I agree with the judgments of Lord Millett NPJ and Mr Justice Ribeiro PJ. I would like to add a few observations on the effect which the House of Lords decision in **MacNiven (HM Inspector of Taxes) v. Westmoreland Investments Ltd** [2003] 1 AC 311 is said to have on the principle developed in **WT Ramsay Ltd v. Inland Revenue**

Commissioners [1982] AC 300.

6. The principle enunciated in **Ramsay** is "both a rule of statutory construction applicable to revenue statutes and an approach to the analysis of the facts": Sir Anthony Mason NPJ in **Shiu Wing Ltd & others v. Commissioner of Estate Duty** (2000) 3 HKCFAR 215 at 239I. What this principle entails, as elaborated and developed in subsequent cases, is this: when faced with a tax avoidance scheme, the court's task is to ascertain the nature of the transaction or composite transactions in question and the true meaning of the relevant statutory provision having regard to the purpose and intention of the legislation and then apply it to the facts of the case, not taking into account any steps in the transactions which have no commercial purpose other than to avoid tax. The court adopts a purposive construction on the tax legislation and applies it to the end result of the transactions.

7. I do not think Lord Nicholls of Birkenhead in **MacNiven** had said anything which is inconsistent with this principle. He took the view that it is an "approach to ascertaining the legal nature of transactions and to interpreting taxing statutes"; "an exemplification of the established purposive approach to the interpretation of statutes. (See p.319F) Nor had Lord Hope, Lord Hutton and Lord Hobhouse said anything which affect the **Ramsay** principle or its application.

8. However, Lord Hoffmann's judgment in **MacNiven** (with which the other members of the House agreed) is said to have given rise to the suggestion that it has limited the scope and hence the use of the **Ramsay** principle - see particularly paragraphs 32, 35, 49 and 58 of his judgment.

9. In my view, the above passages, read in the context of the whole judgment, form part of Lord Hoffmann's wider discussion on statutory construction. He was explaining the earlier decisions and commenting on the approach to be adopted in ascertaining the true meaning of the relevant statutory provisions, particularly of tax legislation, and the intention of the legislature. He was emphasizing the point that while there are many statutes which upon their true construction are intended to have a commercial meaning or content, in which case, the **Ramsay** principle would be useful, there are some statutes which do not permit such a construction, in which case, the **Ramsay** principle would not be applicable. With this, I would respectfully agree.

10. It is said that what Lord Hoffmann said was intended to limit the application of the **Ramsay** principle by setting a prerequisite to its application according to a supposed dichotomy of legal and

commercial concepts to be gathered from the relevant provisions. I doubt if that was his Lordship's intention. But if that were the effect of what he said, I would respectfully think that this would create uncertainty as the distinction between legal and commercial concepts is very often difficult to draw. While the **Ramsay** principle had been held not to apply in some previous cases, a limitation based on such dichotomy is not justified or supported by the earlier decisions. I also do not think that the rules of construction of tax legislation should be restricted to a categorization of the meaning of the relevant statutory provisions into different concepts.

Mr Justice Ribeiro PJ :

11. I have had the advantage of reading in draft the judgment of Lord Millett NPJ and respectfully agree with its reasoning and conclusion. I would only wish to add some observations regarding the principle developed in **W T Ramsay Ltd v Inland Revenue Commissioners** [1982] AC 300, in the light of recent controversies as to its scope.

12. As Sir Anthony Mason NPJ noted in **Shiu Wing Ltd v Commissioner of Estate Duty** (2000) 3 HKCFAR 215 at 239, the **Ramsay** principle is both a rule of statutory construction and an approach to the analysis of the facts.

13. The aim of the tax-avoidance scheme in **Ramsay** was to create an allowable loss for the taxpayer as part of a wider plan which involved the cancelling out of that loss by a non-taxable gain. Lord Wilberforce, giving the principal speech, focussed primarily on the proper factual approach to such transactions :-

"If it can be seen that a document or transaction was intended to have effect as part of a nexus or series of transactions, or as an ingredient of a wider transaction intended as a whole, there is nothing in the doctrine to prevent it being so regarded: to do so is not to prefer form to substance, or substance to form. It is the task of the court to ascertain the legal nature of any transaction to which it is sought to attach a tax or a tax consequence and if that emerges from a series or combination of transactions, intended to operate as such, it is that series or combination which may be regarded."
([1982] AC 300 at 323-4)

As to the particular self-cancelling schemes with which the House of Lords was faced, his Lordship stated :-

"On these facts it would be quite wrong, and a faulty analysis, to pick out, and stop at, the one step in the combination which

produced the loss, that being entirely dependent upon, and merely, a reflection of the gain. The true view, regarding the scheme as a whole, is to find that there was neither gain nor loss, and I so conclude." (at 328)

14. Treating such a loss and such a gain as "self-cancelling," necessarily involved an exercise in statutory interpretation, indeed, an exercise of purposive statutory interpretation. If the loss-producing transaction in the scheme were taken alone, it would, falling within the literal words of the statute, attract the tax consequence of being an allowable loss. It would not be "cancelled out" fiscally by the scheme gain since that gain, again if taken alone was, on a literal interpretation, non-taxable. Therefore, when in **Ramsay**, the House of Lords regarded the loss and gain as "self-cancelling," viewing them as part of a larger, composite transaction, this necessarily implied that as a matter of statutory construction, the provisions which would otherwise confer the desired tax consequences on the individual transactions were not intended to apply to them in the context of the overall scheme.

15. Lord Wilberforce acknowledged the need for such purposive interpretation, stating :-

"A subject is only to be taxed upon clear words, not upon 'intendment' or upon the 'equity' of an Act. Any taxing Act of Parliament is to be construed in accordance with this principle. What are 'clear words' is to be ascertained upon normal principles: these do not confine the courts to literal interpretation. There may, indeed should, be considered the context and scheme of the relevant Act as a whole, and its purpose may, indeed should, be regarded: see *Inland Revenue Commissioners v Wesleyan and General Assurance Society* (1946) 30 TC11, 16 per Lord Greene MR and *Mangin v Inland Revenue Commissioner* [1971] AC 739, 746, per Lord Donovan." (at 323)

Applying such an interpretation to the facts, his Lordship stated :-

"To say that a loss (or gain) which appears to arise at one stage in an indivisible process, and which is intended to be and is cancelled out by a later stage, so that at the end of what was bought as, and planned as, a single continuous operation, there is not such a loss (or gain) as the legislation is dealing with, is in my opinion well and indeed essentially within the judicial function." (at 326)

16. Another way of describing the House of Lords' approach to statutory interpretation in **Ramsay** is to say that, applying a purposive interpretation, their Lordships disregarded for fiscal purposes the self-cancelling intermediate steps and applied the legislative provisions

instead to the scheme viewed as a composite whole.

17. This was effectively Lord Diplock's approach in **IRC v Burmah Oil Co Ltd** [1982] STC 30, a case also involving a planned series of self-cancelling transactions, this time aimed at converting a non-allowable loss into a loss that would be deductible for capital gains purposes. Lord Diplock stated :-

"It would be disingenuous to suggest, and dangerous on the part of those who advise on elaborate tax-avoidance schemes to assume, that *Ramsay's* case did not mark a significant change in the approach adopted by this House in its judicial role to a pre-ordained series of transaction (whether or not they include the achievement of a legitimate commercial end) into which there are inserted steps that have no commercial purpose apart from the avoidance of a liability to tax which in the absence of those particular steps would have been payable. [T]he approach to tax avoidance schemes of this character sanctioned by *Ramsay* entitles your Lordships to ignore the intermediate circular book entries and to look at the end result ..." (at 32-33)

18. Lord Fraser, giving the main speech in **Burmah Oil**, applied the **Ramsay** approach and concluded (at p 38) that notwithstanding the literal applicability of relevant sections of the Finance Act 1965 to intermediate steps in the scheme, the proper approach was to examine the scheme when it was completely carried out. So viewed, it "did not result in a loss such as the legislation is dealing with, which I may call for short, a real loss." This obviously involved a purposive interpretation of the legislation.

19. It may be noted that Lord Diplock, in referring to the circular and self-cancelling book entries, spoke in more general terms of schemes involving the insertion of "steps that have no commercial purpose apart from the avoidance of a liability to tax." While this expression is apt to describe the self-cancelling transactions in question, it is plainly of a wider import. This was seized upon in **Furniss v Dawson** [1984] AC 474, where the tax-deferment scheme in question did not involve self-cancelling transactions.

20. In **Furniss v Dawson**, the Dawson family wished to sell the whole of the issued capital of two operating companies to an outside purchaser called Wood Bastow Holdings Ltd. They embarked upon a scheme which essentially involved incorporating and interposing a Manx company called Greenjacket Investments Ltd between themselves and Wood Bastow, followed by an exchange of their shares in the operating companies for the issue of shares in Greenjacket and the on-sale of those operating company shares by

Greenjacket to Wood Bastow for cash. The object of this scheme was to defer liability for capital gains tax which was charged on capital gains accruing on the disposal of assets. It relied on paragraphs 4(2) and 6(1) of Schedule 7 to the Finance Act 1965 which deemed there to be no disposal in cases of company amalgamations, that is, where a company's shares were transferred to another company which thereby acquired control of the first company in exchange for shares in the transferee company. The scheme's contention was accordingly that the share exchange between the Dawsons and Greenjacket led to the latter obtaining control of the former and therefore was deemed by those paragraphs of Schedule 7 not to involve a taxable disposal of the operating company shares. It would follow that any charge to capital gains tax would be deferred until such time as the taxpayers disposed of their shareholdings in Greenjacket realising a chargeable gain.

21. Plainly, unlike the schemes in **Ramsay** and in **Burmah Oil**, this scheme was not self-cancelling but had, as the Court of Appeal put it, "enduring legal consequences". Greenjacket had been brought into being for an indefinite period. The shares in the operating companies had been transferred to it. The sale was by Greenjacket to Wood Bastow and any claims in respect thereof would be made against Greenjacket and not the Dawsons. And, as Lord Brightman acknowledged :-

"..... the consideration money paid by Wood Bastow, which was the foundation of the capital gain, would never reach the hands of the Dawsons, save by way of loan, unless and until Greenjacket was wound up or its capital was reduced" ([1984] AC at 524)

22. The House of Lords decided that the **Ramsay** principle was not confined to self-cancelling transactions and, applying it to the scheme, held :-

"The result of correctly applying the *Ramsay* principle to the facts of this case is that there was a disposal by the Dawsons in favour of Wood Bastow in consideration of a sum of money paid with the concurrence of the Dawsons to Greenjacket. Capital gains tax is payable accordingly." (per Lord Brightman at 528; see also Lord Fraser at 513 and Lord Roskill at 515)

23. This conclusion necessarily involved a two-stage decision: first, that as a matter of statutory construction, the provisions in Schedule 7 were not intended to apply to the share exchange between the Dawsons and Greenjacket so as to deem it a non-disposal of the shares; and secondly, that interposition of Greenjacket could, for fiscal purposes, be disregarded so that the Dawsons could be treated as

making a taxable disposal of the shares in favour of Wood Bastow.

24. The first stage of such reasoning is straightforward. Notwithstanding the literal applicability of the Schedule 7 provisions to the share exchange between the Dawsons and Greenjacket if taken alone, it was held that such provisions were not intended to be applied to that exchange viewed in isolation, given that it was merely a step in a larger, pre-conceived scheme which involved the immediate on-sale of the shares by Greenjacket to Wood Bastow and had no commercial purpose other than tax avoidance. As Lord Bridge put it (at 518), the transfer to Greenjacket was merely "to ensure that for a *scintilla temporis* the beneficial interest in the shares was held by Greenjacket in order to found Greenjacket's claim to have been in control of the operating companies" for the purposes of the statutory exception.

25. The second stage of the decision required the **Ramsay** principle to be developed. In **Ramsay** itself and in **Burmah Oil**, the transactions had been self-cancelling. Accordingly, when one turned to examine the larger, composite transaction, the mutual cancellation of loss and gain simply meant that in the end result, there was no "loss" upon which any tax consequences could attach. The Court was not required to pronounce upon any other aspect of the scheme in order to reach its conclusion as to the taxpayer's liability. The **Furniss v Dawson** situation was different since, after reaching the first stage of its decision, namely, that on a purposive interpretation, the share exchange fell outside the statutory exception, the court had to consider how to deal with the "enduring legal consequences" of the scheme which remained. The transactions had not cancelled each other out.

26. It is in this context that Lord Brightman's oft-cited statement has to be understood. His Lordship stated :-

"The formulation by Lord Diplock in *Inland Revenue Commissioners v Burmah Oil Co Ltd* [1982] STC 30, 33 expresses the limitations of the *Ramsay* principle. First, there must be a pre-ordained series of transactions; or, if one likes, one single composite transaction. This composite transaction may or may not include the achievement of a legitimate commercial (ie business) end. The composite transaction does, in the instant case; it achieved a sale of the shares in the operating companies by the Dawsons to Wood Bastow. It did not in *Ramsay*. Secondly, there must be steps inserted which have no commercial (business) purpose apart from the avoidance of a liability to tax - not 'no business effect.' If those two ingredients exist, the inserted steps are to be disregarded for fiscal purposes. The court must then look at the end result. Precisely how the end result will be taxed will depend on the terms

of the taxing statute sought to be applied." ([1984] AC at 527)

27. In my view, Lord Brightman was seeking to do two things in this passage. First, he was seeking to demonstrate that, as a matter of authority (by reference to Lord Diplock's dictum in **Burmah Oil**), the **Ramsay** principle was capable of applying to tax-avoidance schemes which were not self-cancelling, but which were "linear" and left "enduring legal consequences". Lord Diplock's formulation neatly encompassed the latter type of scheme which could plainly be said to involve a pre-ordained series of transactions into which steps with no commercial purpose are inserted. Secondly, and by way of innovation, Lord Brightman was indicating how the court should deal with the intermediate steps which persisted after the scheme had been carried out. He held that the inserted steps "are to be disregarded for fiscal purposes" with the court then looking at "the end result" and applying the provisions of the taxing statute to that end result. He concludes: "Precisely how the end result will be taxed will depend on the terms of the taxing statute sought to be applied."

28. One can at once reject as untenable any notion that Lord Brightman's statement postulates a substantive rule of law. As Lord Steyn put it in **IRC v McGuckian** [1997] 1 WLR 991:-

"The new *Ramsay* principle [1982] AC 300 was not invented on a juristic basis independent of statute. That would have been indefensible since a court has no power to amend a tax statute. The principle was developed as a matter of statutory construction." (at 1000)

29. If the abovementioned reading of Lord Brightman's statement is correct, it also follows that one should not accept the view, discernible in some judgments, that the statement is the formulation of an overarching principle of statutory construction to be applied in the interpretation of all revenue legislation. On that approach, a finding that there has been a pre-ordained series of transactions which included steps inserted without any commercial purpose apart from the avoidance of tax, dictates a construction of the statute which requires the inserted steps to be disregarded for fiscal purposes - whatever the language of the statute - with the court thereafter applying the tax statute's provisions to the end result.

30. Such an approach may perhaps be seen in Lord Browne-Wilkinson's speech in **IRC v McGuckian** [1997] 1 WLR 991. Thus, his Lordship considered Lord Brightman to be stating "the classic requirements for the application of that principle" (at 996). Evidently treating it as laying down a principle of construction, Lord Browne-

Wilkinson continued :-

"The approach pioneered in the *Ramsay* case and subsequently developed in later decisions is an approach to construction, viz that in construing tax legislation, the statutory provisions are to be applied to the substance of the transaction, disregarding artificial steps in the composite transaction or series of transactions inserted only for the purpose of seeking to obtain a tax advantage. The question is not what was the effect of the insertion of the artificial steps but what was its purpose. Having identified the artificial steps inserted with that purpose and disregarded them, then what is left is to apply the statutory language of the taxing Act to the transaction carried through stripped of its artificial steps. It is irrelevant to consider whether or not the disregarded artificial steps would have been effective to achieve the tax saving purpose for which they were designed." ([1997] 1 WLR at 998)

31. The opposing, and in my respectful opinion, preferable, view is that the **Ramsay** principle does not espouse any specialised principle of statutory construction applicable to tax legislation, whatever its language, but continues to assert the need to apply orthodox methods of purposive interpretation to the facts viewed realistically. In common with Lord Hoffmann in **MacNiven v Westmoreland Investments Ltd** [2003] 1 AC 311 at para 49, I am of the view that Lord Brightman's formulation is not a principle of construction, but, as stated above, a decision that the Court is entitled, for fiscal purposes, to disregard intermediate steps having no commercial purpose *as a consequence of* an orthodox exercise of purposive statutory construction.

32. This is very much where the balance of authority lies.

(a) Thus, in *McGuckian*, Lord Cooke stated :-

"The principle which your Lordships have been developing in *W T Ramsay Ltd v Inland Revenue Commissioners* [1982] AC 300, *Inland Revenue Commissioners v Burmah Oil Co Ltd* (1981) 54 TC 200, and *Furniss v Dawson* [1984] AC 474 is not uncommonly seen as special to the construction of taxing Acts. Perhaps more helpfully, however, it may be recognised as an application to taxing Acts of the general approach to statutory interpretation whereby, in determining the natural meaning of particular expressions in their context, weight is given to the purpose and spirit of the legislation." ([1997] 1 WLR at 1005)

(b) In the same case, Lord Steyn saw such purposive

interpretation as a reaction against the formalistic approaches previously imbuing revenue law :-

"During the last 30 years there has been a shift away from literalist to purposive methods of construction. Where there is no obvious meaning of a statutory provision the modern emphasis is on a contextual approach designed to identify the purpose of a statute and to give effect to it. But under the influence of the narrow *Duke of Westminster doctrine* [1936] AC 1, 19 tax law remained remarkably resistant to the new non-formalist methods of interpretation. It was said that the taxpayer was entitled to stand on a literal construction of the words used regardless of the purpose of the statute: *Pryce v Monmouthshire Canal and Railway Cos* (1879) 4 App Cas 197, 202-203; *Cape Brandy Syndicate v Inland Revenue Commissioners* [1921] 1 KB 64, 71; *Inland Revenue Commissioners v Plummer* [1980] AC 896. Tax law was by and large left behind as some island of literal interpretation. The second problem was that in regard to tax avoidance schemes the courts regarded themselves as compelled to adopt a step by step analysis of such schemes, treating each step as a distinct transaction producing its own tax consequences. It was thought that if the steps were genuine, ie not sham or simulated documents or arrangements, the court was not entitled to go behind the form of the individual transactions. In combination those two features - literal interpretation of tax statutes and the formalistic insistence on examining steps in a composite scheme - separately allowed tax avoidance schemes to flourish to the detriment of the general body of taxpayers. The result was that the court appeared to be relegated to the role of a spectator concentrating on the individual moves in a highly skilled game: the court was mesmerised by the moves in the game and paid no regard to the strategy of the participants or the end result. The courts became habituated to this narrow view of their role.

On both fronts the intellectual breakthrough came in 1981 in the *Ramsay* case, and notably in Lord Wilberforce's seminal speech which carried the agreement of Lord Russell of Killowen, Lord Roskill and Lord Bridge of Harwich. Lord Wilberforce restated the principle of statutory construction that a subject is only to be taxed upon

clear words [1982] AC 300, 323C-D. To the question 'What are clear words?' he gave the answer that the court is not confined to a literal interpretation. He added 'There may, indeed should, be considered the context and scheme of the relevant Act as a whole, and its purpose may, indeed should, be regarded.' This sentence was critical. It marked the rejection by the House of pure literalism in the interpretation of tax statutes." ([1997] 1 WLR at 999-1000)

(c) In *MacNiven v Westmoreland Investments Ltd* [2003] 1 AC 311 at para 6, Lord Nicholls, referring to the passage from Lord Steyn's speech cited above, stated :-

"As noted by Lord Steyn in *Inland Revenue Comrs v McGuckian* [1997] 1 WLR 991, 1000, this is an exemplification of the established purposive approach to the interpretation of statutes. When searching for the meaning with which Parliament has used the statutory language in question, courts have regard to the underlying purpose that the statutory language is seeking to achieve. Likewise, Lord Cooke of Thorndon regarded the *Ramsay* case as an application to taxing Acts of the general approach to statutory interpretation whereby, in determining the natural meaning of particular expressions in their context, weight is given to the purpose and spirit of the legislation: see [1997] 1 WLR 991, 1005."

33. Specifically addressing Lord Brightman's formulation, Lord Cooke stated :-

"In the *Furniss* case [1984] AC 474, 527 Lord Brightman spoke of certain limitations (a pre-ordained series of transactions including steps with no commercial or business purpose apart from the avoidance of a liability to tax). The present case does fall within these limitations, but it may be as well to add that, if the ultimate question is always the true bearing of a particular taxing provision on a particular set of facts, the limitations cannot be universals. Always one must go back to the discernible intent of the taxing Act." (In *McGuckian* [1997] 1 WLR at 1005)

34. Similarly, in **MacNiven**, Lord Nicholls warned against the mistake of treating the post-**Ramsay** authorities as "laying down factual pre-requisites which must exist before the court may apply the purposive, **Ramsay** approach to the interpretation of a taxing statute." His Lordship thought that the much-quoted observation of Lord Brightman

had suffered in this way, adding :-

"..... the factual situation described by Lord Brightman is one where, typically, the *Ramsay* approach will be a valuable aid. In such a situation, when ascertaining the legal nature of the transaction and then relating this to the statute, application of the *Ramsay* approach may well have the effect stated by Lord Brightman. But, as I am sure Lord Brightman would be the first to acknowledge, the *Ramsay* approach is no more than a useful aid. This is not an area for absolutes. The paramount question always is one of interpretation of the particular statutory provision and its application to the facts of the case. Further, as I have sought to explain, the *Ramsay* case did not introduce a new legal principle. It would be wrong, therefore, to set bounds to the circumstances in which the *Ramsay* approach may be appropriate and helpful. The need to consider a document or transaction in its proper context, and the need to adopt a purposive approach when construing taxation legislation, are principles of general application. Where this leads depends upon the particular set of facts and the particular statute." ([2003] 1 AC at 320)

35. Accordingly, the driving principle in the **Ramsay** line of cases continues to involve a general rule of statutory construction and an unblinkered approach to the analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically. Where schemes involve intermediate transactions having no commercial purpose inserted for the sole purpose of tax-avoidance, it is quite likely that a purposive interpretation will result in such steps being disregarded for fiscal purposes. But not always. **MacNiven** is a good example of a case where a purposive interpretation of the statute and its application to the facts did not dictate excluding the taxpayer's payment of interest from the statutory provision treating such payments as deductible charges on income. On the true construction of the statute (for the reasons stated by Lord Nicholls at paras 14-17), it mattered not that there had been a circular movement of money between the debtor and the tax exempt creditor to fund the relevant interest payment having no commercial purpose other than to avail themselves of an allowable tax loss.

36. In the course of argument, it was suggested by Lord Goodhart QC, appearing for the Collector, that in **MacNiven**, Lord Hoffmann had re-interpreted the **Ramsay** principle in a way which should not be followed in this jurisdiction. Lord Hoffmann was said to have introduced a dichotomy between statutory concepts which may be characterised as "commercial" and those which are purely "legal" to be used as a filter to determine which statutory provisions are and are not

susceptible to the **Ramsay** approach. This was said to be inconsistent with authority and, in any event, to involve an unworkable exercise in legal taxonomy, some of the difficulties of which had been noted by the English Court of Appeal in **Barclays Mercantile Business Finance Ltd v Mawson** [2003] STC 66.

37. While I can see that Lord Hoffmann's speech may be capable of being read in the manner suggested, I very much doubt that his Lordship actually intended to lay down any mechanistic test based on a "commercial"/"legal" dichotomy for pre-determining whether a particular statutory provision is or is not susceptible to a **Ramsay** approach, as was suggested.

38. There seems no doubt that Lord Hoffmann accepts that the **Ramsay** principle involves the court adopting well-known techniques of purposive interpretation. Thus, having noted the difficulties which the Crown had experienced from an insufficiently differentiated application of Lord Brightman's formulation in **Furniss v Dawson**, Lord Hoffmann states ([2003] 1 AC 311 at paras 55 to 57):-

"My Lords, I think that it was for these reasons that their Lordships in the McGuckian case went back to Lord Wilberforce's analysis in the *Ramsay* case [1982] AC 300 and tried to identify the principle of construction in play. Lord Steyn said that the decision marked a shift away from literalism to a 'broad purposive interpretation' and from 'formalistic insistence on examining steps in a composite scheme separately' to 'a more realistic legal analysis': [1997] 1 WLR 991, 999-1000. Lord Cooke of Thorndon suggested, at p 1005, that it was:

'an application to taxing Acts of the general approach to statutory interpretation whereby, in determining the natural meaning of particular expressions in their context, weight is given to the purpose and spirit of the legislation.'

My Lords, these are valuable insights and I respectfully suggest that particular attention should be paid to the way Lord Cooke of Thorndon dealt with the criteria stated by Lord Brightman in *Furniss v Dawson*:

'Lord Brightman spoke of certain limitations (a pre-ordained series of transactions including steps with no commercial or business purpose apart from the avoidance of a liability to tax). The present case does fall within these limitations, but it may be as well to add that, if the ultimate question is always the true bearing of a particular taxing provision on a particular set of facts, the limitations cannot be

universals. Always one must go back to the discernible intent of the taxing Act. I suspect that the advisers of those bent on tax avoidance ... do not always pay sufficient heed to the theme in the speeches in the *Furniss* case ... to the effect that the journey's end may not yet have been found.'

I would only add that it is not only tax avoiders who may not pay sufficient heed to the necessity of concentrating on the application of the particular taxing provision to the particular facts. The Inland Revenue sometimes also fails to do so. The journey's end may be different because the journey itself is not the same."

39. The "valuable insights" that Lord Hoffmann was acknowledging were all centred on the proposition that the **Ramsay** doctrine has at its core the purposive interpretation of statutes applied to facts viewed realistically and untrammelled by "limitations" which might be thought to arise out of Lord Brightman's formulation. Such an approach strikes me as the antithesis of a mechanistic use of the "commercial"/"legal" dichotomy as a straitjacket limiting construction of the relevant statute. I am reinforced in this view by Lord Hoffmann stating :-

"I would only add by way of caution that although a word may have a 'recognised legal meaning', the legislative context may show that it is in fact being used to refer to a broader commercial concept." (at para 50)

This seems to me quite inconsistent with using the dichotomy as a means of determining a *priori* whether the **Ramsay** doctrine is applicable.

40. I may of course be wrong in my understanding of Lord Hoffmann's speech and if it was indeed intended to suggest that the dichotomy should be used in the manner suggested, I would respectfully decline to adopt such approach in this jurisdiction. However, I am content to proceed for present purposes on the basis that the dichotomy proposed by Lord Hoffmann was no more than an analytical attempt at identifying a common theme in the way in which statutes have been purposively construed under the **Ramsay** rubric. For my own part, I would prefer not to refer to the dichotomy, but to see the approach to statutory construction required by **Ramsay** as purely the orthodox purposive approach, untrammelled by any limitations.

41. I respectfully agree entirely with Lord Millett's statement of the purpose of section 45 of the Stamp Duty Ordinance and the manner of his application of the **Ramsay** principle to the facts of the present

case.

Lord Millett NPJ :

42. The question in this appeal is whether a Memorandum of Sale of land for residential development which was duly completed by assignment is chargeable to stamp duty. The assignee failed before the District Judge but succeeded in the Court of Appeal in maintaining that the Memorandum attracts relief from duty under s.45 of the Stamp Duty Ordinance, Cap. 117 ("the Ordinance") because it was an agreement for and was completed by a transfer between associated companies. Some HK\$350 million of duty is at stake.

43. Section 4 of the Ordinance taken with ss 29A(5) and (6) and 29C(2) has the effect of making the Memorandum of Sale rather than the assignment the document which is liable to be stamped. Under Head 1(1A) in the First Schedule to the Ordinance *ad valorem* duty is charged on "the amount or value of the consideration".

The background

44. In January 1997 Shiu Wing Steel Limited ("Shiu Wing") owned a lease of industrial land at Tseung Kwan O ("the Development Land") which it wished to sell for residential redevelopment. To enable it to do so it had entered into a non-binding agreement with the Government for the surrender and regrant of the Development Land at a premium of HK\$5,853,000,000.

45. Two property developers, the Sun Hung Kai Properties group and the Swire group, were interested in buying the Development Land and undertaking the redevelopment as a joint venture. They formed Calm Seas Developments Limited ("Calm Seas") as a vehicle to carry it out. Calm Seas was a joint venture company which they owned through their subsidiaries New Town (N.T.) Properties Limited ("New Town"), a member of the Sun Hung Kai group, and Swire Properties Limited ("Swire"), a member of the Swire group.

46. Shiu Wing wished to retain an interest in the project in the form of a 12% share in the profits of the development together with a 2% equity holding in the company which carried it out. This meant that it was necessary to form another joint venture company in which Calm Seas would have a 98% interest and Shiu Wing 2%. It also meant that elaborate provisions needed to be included to safeguard Shiu Wing's small but valuable stake in the development from being eroded by

actions taken by its majority partners.

The Heads of Agreement

47. On 3 January 1997 Shiu Wing entered into a binding but preliminary agreement ("the Heads of Agreement") with New Town, Swire, and Calm Seas. The basic structure of the transaction was to consist of a sale of the Development Land by Shiu Wing to a wholly owned indirect subsidiary followed by a sale of 98% of the shares in the subsidiary's immediate parent to Calm Seas. If it had taken this form, the sale of the Development Land by Shiu Wing to its own wholly-owned subsidiary would have been initially relieved from stamp duty under s.45(2) of the Ordinance as a transfer between associated companies. If the arrangement included a sale of more than 10% of the shares in the subsidiary's parent to Calm Seas, however, relief would be lost by the operation of s.45(4)(c) of the Ordinance; and even if not envisaged by the arrangement a similar sale to Calm Seas within two years of the assignment would cause relief to be lost by the operation of s.45(5A).

48. The Heads of Agreement did not commit Shiu Wing to sell the Development Land but merely obliged the parties to take various steps if it did so. The sale and assignment of the Development Land by Shiu Wing to its subsidiary was merely a condition precedent which automatically triggered the parties' contractual obligations. This may have been a precaution taken in order to prevent the Heads of Agreement attracting liability to stamp duty as an agreement for sale of land before any steps had been taken to obtain relief from duty; but if so nothing turns on it.

49. It is not necessary to set out the terms of the Heads of Agreement in full. Shortly summarised, they provided as follows:

(1) Shiu Wing was to form two British Virgin Islands subsidiaries with a share capital of 1,000 ordinary shares of HK\$1 each. One, which when formed was Prepared Holdings Limited ("Prepared"), was to be a wholly owned subsidiary of the other, which in turn was to be a wholly owned subsidiary of Shiu Wing and when formed was Super Charge Developments Limited ("Super Charge"). In what follows I shall refer to these and other companies involved by the names which they took when incorporated and not by the names by which they are described in the pre-incorporation documents.

(2) Calm Seas would buy 980 of the 1,000 ordinary shares in Prepared from Super Charge for a consideration of HK\$12,460,559,737. This represented 98% of the sale price of the Development Land which was HK\$12,714,856,874. This would leave Shiu Wing with an indirect holding of 2% of the equity in Prepared through Super Charge.

(3) Payment of the purchase price for the shares was to be satisfied by

(i) an immediate deposit of HK\$1,869,083,960;

(ii) the provision by Calm Seas of the sum of HK\$5,853,000,000 required by Shiu Wing to pay the premium for the regrant of the Development Land; and

(iii) payment of the balance on completion.

(4) The sale of the shares was conditional on the assignment of the Development Land by Shiu Wing to a wholly owned subsidiary of Prepared (which when formed was the Respondent Arrowtown Assets Limited ("Arrowtown")) at an initial price of HK\$12,714,856,874.

(5) On completion of the sale of the shares Shiu Wing was to deliver to Calm Seas an Agreement relating to the Deferred Consideration ("the Deferred Consideration Agreement") executed by Arrowtown. This was to include the terms set out in Part 2 of Schedule 2 to the Heads of Agreement. They provided for payment by Arrowtown to Shiu Wing of 12% of the "Surplus Proceeds of the Development" as defined in the Schedule as deferred consideration for the Development Land.

(6) The parties agreed to use their best endeavours to negotiate a further agreement. This was to include

"terms for the constitution and operation of the business of each of Prepared and Arrowtown and, in particular, terms permitting *Shiu Wing* to nominate one director of Prepared and one director of Arrowtown, terms giving protection for Shiu Wing as a *minority shareholder of Prepared*, and terms to ensure that Calm Seas (or as the case may be) Prepared does not take or omit to take any action

with the sole or main intention of preventing Arrowtown from meeting the deferred consideration for the assignment of the Development Land" (emphasis added).

(7) Calm Seas was concerned that provision should be made (*inter alia*) to enable relief from stamp duty to be obtained on the sale of the Development Land. Accordingly the Heads of Agreement included a provision that the parties would

"use their respective best endeavours to agree and co-operate with each other to formulate optimum structures so as to minimise the liability for stamp duty on the assignment of the Development Land to Arrowtown In particular Shiu Wing shall agree to such structures as may be advised by Calm Seas's tax advisers to structure Prepared as an associated company of Shiu Wing within the meaning of section 45 of the Stamp Duty Ordinance by the holding of non-voting and non-participating deferred shares in Prepared"

50. Thus from the outset the arrangements contemplated that there would be four distinct but linked transactions, that is to say:

(i) *the land exchange* by which Shiu Wing would surrender its lease to the Government and receive in exchange a fresh lease of the Development Land on payment of a premium of HK\$5,853,000,000, which sum it would obtain by the share sale referred to below;

(ii) *the land sale* by which Shiu Wing would sell and assign the Development Land to its wholly owned indirect subsidiary for HK\$12,714,856,874;

(iii) *the capital reorganisation* by which the share capital of the immediate parent company of the subsidiary which acquired the Development Land would be restructured for the avowed purpose of avoiding the loss of relief from stamp duty which would otherwise occur when the share sale referred to below took place; and

(iv) *the share sale* by which 98% of the equity in the parent company of the subsidiary which had acquired the Development Land would be sold and transferred to Calm Seas for a sum representing 98% of the HK\$12,714,856,874.

51. If the arrangements were to achieve relief from stamp duty, it was necessary that the land sale should take place while the assignee remained a wholly owned subsidiary of Shiu Wing, that is to say before the capital reorganisation; and that the share sale should not take place until after the capital reorganisation had been completed.

The formation of the chain of subsidiaries

52. Following the Heads of Agreement, Shiu Wing formed four British Virgin Islands subsidiaries. These were Eastview Holdings Limited ("Eastview"), a wholly owned subsidiary of Shiu Wing which seems to have been inserted into the chain of subsidiaries merely to lengthen the chain; Super Charge, a wholly owned subsidiary of Eastview; Prepared, a wholly owned subsidiary of Super Charge and 98% of the shares of which (after an appropriate capital reorganisation for the stated purpose of attracting relief from stamp duty) were to be the subject of the sale to Calm Seas; and Arrowtown, the wholly owned subsidiary of Prepared which was to acquire the Development Land from Shiu Wing.

The capital reorganisation

53. Calm Seas, Super Charge and Prepared were all incorporated and had their registered offices in the British Virgin Islands. Their shares were not "Hong Kong stock" within the meaning of the Ordinance so that the transfer of the shares in Prepared to Calm Seas was outside the scope of Hong Kong stamp duty. The Development Land, however, was immovable property in Hong Kong and its assignment on sale would attract liability to *ad valorem* stamp duty on the amount or value of the consideration unless relief could be obtained under s.45. This gives relief from stamp duty where the transfer is between associated companies, that is to say where "one is beneficial owner of not less than 90% of the issued share capital of the other".

54. It was thus necessary to provide Prepared with a capital structure contrived to ensure that, even after the sale of its shares to Calm Seas when Shiu Wing would be, in the words of the Heads of Agreement, "a minority shareholder of Prepared", Shiu Wing would nevertheless retain (indirectly through its wholly owned subsidiary Super Charge) not less than 90% of the issued share capital of Prepared.

55. This was to be achieved by the reorganisation of the share capital of Prepared so that it had a nominal capital of HK\$1,010 consisting of 1,000 ordinary shares of HK\$0.01 each and 100,000 "B" non-voting shares of HK\$0.01 each. Following the sale of 980 of the 1,000

ordinary shares to Calm Seas, therefore, Super Charge would retain only 2% of the ordinary shares but more than 99% of the total issued share capital of Prepared after the "B" non-voting shares are taken into account.

56. It was, of course, necessary to ensure that the "B" non-voting shares which Super Charge was to retain were effectively valueless. Their sole purpose was to satisfy the statutory test for relief from stamp duty, not to provide Shiu Wing with an additional commercial interest in Prepared beyond its 2% share of the equity.

The Share Sale Agreement

57. On 7 April 1997 the parties to the Heads of Agreement entered into a Sale and Purchase Agreement ("the Share Sale Agreement") for the sale of shares in Prepared to Calm Seas. By the Share Sale Agreement Shiu Wing undertook, before paying the premium for the regrant of the Development Land, to reorganise the share capital of Prepared so that it should consist of 1000 ordinary shares of HK\$0.01 each and 100,000 "B" non-voting shares of HK\$0.01 each having in each case the rights set out in new Articles of Association which were annexed to the Agreement. Following the capital reorganisation of Prepared, Shiu Wing undertook to procure the sale of 980 ordinary shares in Prepared by Super Charge to Calm Seas at the price of HK\$12,460,559,737.

58. Other provisions reproduced or amplified the terms of the Heads of Agreement. Completion of the Share Sale Agreement was conditional upon (i) the Development Land being assigned to Arrowtown immediately following the regrant of the Development Land at the price of HK\$12,714,856,874; and (ii) completion of the capital reorganisation which Shiu Wing had contractually undertaken to procure.

59. Schedule 2 to the Share Sale Agreement contained elaborate provisions designed to protect Shiu Wing's continuing investment in the development through its 2% holding of ordinary shares and its right to deferred consideration. These have played an important part in the argument, and are described in more detail later.

60. Schedule 3 to the Share Sale Agreement provided that the initial consideration for the sale of the Development Land by Shiu Wing to Arrowtown was not to be paid in cash but left outstanding and secured by a loan note. The loan note was to be assigned by Shiu Wing to Eastview in consideration of the issue to Shiu Wing of shares in

Eastview. There were then to be successive assignments of the loan note by Eastview to Super Charge and by Super Charge to Prepared in each case in consideration of the issue of shares. The last of these assignments, that is to say the assignment to Prepared, was to be in consideration of the issue to Super Charge of 999 ordinary shares and all 100,000 non-voting "B" shares in Prepared.

61. On completion of the sale of the shares to Calm Seas, Shiu Wing was to deliver to Calm Seas the Deferred Consideration Agreement by which Arrowtown undertook to pay the deferred consideration to Shiu Wing as further consideration for the sale of the Development Land and Calm Seas was to deliver to Shiu Wing a Shareholders' Deed to which Shiu Wing, Super Charge, Calm Seas, New Town and Swire were parties.

The rights of the "B" non-voting shares in Prepared

62. Under the Articles of Association of Prepared which Shiu Wing was required to procure Prepared to adopt and which were set out in Annex B to the Share Sale Agreement, the "B" non-voting shares were rendered effectively valueless. They had a right to dividend only for a year in which the net profits of Prepared exceeded HK\$1 million billion (said to be a sum larger than the gross national product of the USA) and a right to distribution on a winding up only after the holders of all other shares had received the somewhat more modest distribution of HK\$100,000 billion per share. In reality, the ordinary shares carried 100% control of the business of Prepared together with the right to the whole of its capital and profits. The holders of the "B" non-voting shares had voting rights only on resolutions varying their rights (which they would have had in any case under the provisions of the Companies Ordinance as members of a separate class).

63. The holders of the "B" non-voting shares enjoyed one significant right, viz. the right to appoint a director of Prepared and a director of Arrowtown. This was no doubt something which Calm Seas would not wish to continue once Shiu Wing's investment in the development was realised; and accordingly Prepared was given the right to buy back the "B" non-voting shares for their nominal value of HK\$1,000 (a right which it would obviously not exercise during the critical two year period if it wished to retain relief from stamp duty). Shiu Wing was not given a corresponding put option.

The successive assignments of the loan note

64. The successive assignments of the note from Shiu Wing to

Prepared were also prompted by the need to avoid loss of stamp duty relief. Although Arrowtown was its wholly owned indirect subsidiary, Shiu Wing had agreed to assign the Development Land to it for a substantial monetary consideration representing what was considered to be its full value. Immediately following the sale of the Development Land to Arrowtown and the issue of the loan note, therefore, the shares in Arrowtown and Prepared were virtually worthless because the value of the Development Land was equalled by Arrowtown's liability to meet the loan note. Calm Seas would certainly not pay some HK\$12 billion for a company which owned the Development Land but was liable to pay full value for it.

65. The simplest way of dealing with this problem would have been for Shiu Wing to transfer the benefit of the loan note to Calm Seas along with the sale of the shares in Prepared. This, however, would have meant Shiu Wing parting with the consideration which it had received from Arrowtown (i.e. the loan note) and by virtue of the operation of s.45(5) of the Ordinance relief from stamp duty would have been lost. Accordingly, the loan note was assigned down the chain of subsidiaries to Prepared but no further. This had the effect of putting sufficient value into Prepared to justify the sale of its shares to Calm Seas.

The protective provisions

66. Once the sale of the shares in Prepared to Calm Seas was completed, Shiu Wing would be left with a very small (2%) voting equity stake in Prepared and a larger (12%) interest in the Surplus Profits of the development by way of deferred consideration due from Arrowtown. It was necessary to make provision to safeguard Shiu Wing's investment from harmful actions by its majority partners; and the Heads of Agreement recognised this.

67. Provisions were therefore included in the documents to protect Shiu Wing's continuing investment in the development. The Share Sale Agreement included undertakings by Calm Seas, New Town and Swire to act in good faith and not to take any action with the sole or main intention of prejudicing Shiu Wing's rights under the Agreement. In addition Part 2 of Schedule 2 to the Share Sale Agreement set out elaborate terms to be contained in the Deferred Consideration Agreement defining "Surplus Proceeds", stipulating for the payment by Arrowtown of 12% of the Surplus Profits by way of deferred consideration for the Development Land, and providing Shiu Wing with valuable safeguards to protect its continuing investment.

68. Part 2 of the Schedule permitted Arrowtown to make interim payments of the Deferred Consideration to Shiu Wing and dividends to Prepared pending the completion of the development. The projected amount of future Surplus Profits was likely to fluctuate from time to time, and it was appreciated that when the final accounts were taken it might be found that Shiu Wing had received too much or too little as interim payments of Deferred Consideration. If Shiu Wing had received too much, it was to be required to repay the excess to Arrowtown.

69. Since Shiu Wing was entitled to 12% of the Surplus Profits but only 2% of the dividends, however, there was a greater risk that it might be found that Arrowtown had in all good faith distributed too much by way of dividend to Prepared to enable it to pay Shiu Wing the full amount of the Deferred Consideration to which it was entitled. Para. 2.14 of the Schedule (on which the Collector places much reliance) accordingly provided that if Arrowtown was found to have distributed too much by way of dividends or other distributions to Prepared, the excess should be repaid by Prepared to Arrowtown; and if Prepared had passed on the excess by way of dividends or other distributions to its shareholders Super Charge and Calm Seas, they should repay to Arrowtown with interest the excess up to the amounts they had respectively received.

70. Para. 2.14 of the Schedule also contained a guarantee by Swire and New Town to Shiu Wing of the repayment of excess dividends due to Arrowtown from Prepared or Calm Seas. In the event this was omitted from the Deferred Consideration Agreement but was included in the Shareholders' Deed instead.

The Deferred Consideration Agreement

71. The Deferred Consideration Agreement provided for by the Share Sale Agreement contained provisions substantially the same as those in Part 2 of Schedule 2 to the Share Sale Agreement except that the guarantees by Swire and New Town were omitted.

The Shareholders' Deed

72. The last of the material documents was the Shareholders' Deed to which Shiu Wing, Super Charge, Calm Seas, New Town and Swire were parties. It was described as a deed "relating to the operation of Prepared and Arrowtown". It was needed because Shiu Wing had a continuing interest in the Deferred Consideration ("the land interest") and a continuing interest as a minority shareholder (through Super

Charge) in Prepared ("the share interest"). The value of those interests depended on the proper management of the development by Prepared and Arrowtown, and this would be under the control of Calm Seas once the sale of the shares in Prepared had been completed. Some of the provisions of the Shareholders' Deed safeguarded Shiu Wing's land interest; others protected its share interest; and others protected both.

73. Provisions of the Shareholders' Deed which the Collector relies upon as specifically protecting the land interest included

(a) a provision which prohibited the declaration or payment of any dividend or other distribution in respect of share capital by Arrowtown or Prepared without the written consent (not to be unreasonably withheld) of Shiu Wing and Super Charge;

(b) a provision that Shiu Wing and Super Charge would be acting reasonably if they withheld consent to a dividend distribution by Arrowtown or Prepared unless a satisfactory guarantee was available to ensure that any excess distribution was repaid to Arrowtown in accordance with para. 2.14 of Schedule 2 to the Share Sale Agreement;

(c) an undertaking by Calm Seas, New Town and Swire replicating their undertaking in the Share Sale Agreement not to take or omit to take any action with the sole or main intention of prejudicing the right of Shiu Wing to receive the Deferred Consideration; and

(d) a provision which required New Town and Swire, in the event of their proposing to transfer shares in Calm Seas in circumstances which would result in a third party obtaining control of Calm Seas, either to procure that the third party should offer to acquire Shiu Wing's right to Deferred Consideration at a fair price or to make such an offer themselves.

Completion

74. Completion took place on 22 April 1997, when the following transactions took place:

(i) Calm Seas paid to Shiu Wing's solicitors the sum of HK\$5,853,000,000 in part payment for the shares in

Prepared as required by the Share Sale Agreement.

(ii) This sum was immediately applied in payment by Shiu Wing to the Government of the premium for the surrender and regrant of the Development Land.

(iii) Shiu Wing and Arrowtown entered into a Memorandum of Agreement for Sale and Purchase of the Development Land by Shiu Wing to Arrowtown, this being the document which (unless attracting relief) is liable to stamp duty. The Memorandum contained the statement required by the Ordinance that the amount or value of the consideration was HK\$12,714,856,874. The Collector accepts the accuracy of this statement and claims *ad valorem* duty by reference to the amount so stated. No reference was made to the Deferred Consideration, the amount or value of which was unascertainable at the date of the Memorandum; and the Collector accepts that this was properly omitted.

(iv) Shiu Wing assigned the Development Land to Arrowtown, which was at that stage still its wholly owned indirect subsidiary. The purchase price for the Development Land was not paid in cash but, as provided by the Share Sale Agreement, was left outstanding on the security of a loan note issued by Arrowtown to Shiu Wing.

(v) The successive assignments of the loan note which were intended to put value into Prepared were executed, the last such assignment (to Prepared) being made by Super Charge in consideration of the allotment of ordinary shares and the "B" non-voting shares in Prepared.

(vi) The assignment of the Development Land to Arrowtown satisfied the condition precedent to the operation of the Share Sale Agreement which became unconditional.

(vii) The Deferred Consideration Agreement and the Shareholders' Deed were executed and completion of the Share Sale Agreement took place. Calm Seas paid the balance of the purchase price for the 980 ordinary shares in Prepared which it had purchased and the shares in

question were duly transferred to Calm Seas.

Section 45 of the Ordinance

75. Section 45 of the Ordinance provides relief from stamp duty in the case of a transfer of the beneficial interest from "one associated body corporate to another". In order for the relief to be available, the transfer must fall within s.45(2) and outside ss 45(4) and (5).

76. So far as material s.45(2) applies

"to any instrument as respects which it is shown to the satisfaction of the Collector that the effect thereof is to convey a beneficial interest in immovable property from one associated body corporate to another where in each case the bodies are associated, that is to say, one is beneficial owner of not less than 90 per cent of the issued share capital of the other, or a third such body is beneficial owner of not less than 90 per cent of the issued share capital of each."

77. So far as material s.45(4) provides that s.45

"shall not apply to any instrument unless it is also shown to the satisfaction of the Collector that the instrument was not executed in pursuance of or in connexion with an arrangement under which-

(a) the consideration, or any part of the consideration, for the conveyance, transfer, sale or purchase was to be provided or received, directly or indirectly by a person other than a body corporate which at the time of the sale or purchase, or of the execution of the conveyance or transfer, was associated within the meaning of subsection (2) with either the transferor or the transferee (meaning respectively, the body corporate from whom and the body corporate to whom the beneficial interest was conveyed or transferred...)"

78. Section 45(5) provides

"Without prejudice to the generality of paragraph (a) of subsection (4), an arrangement shall be treated as within that paragraph if it is one under which the transferor or the transferee, or a body corporate associated with either as there mentioned, was to be enabled to provide any of the consideration, or was to part with any of it, by or in consequence of the carrying out of a transaction or transactions involving, or any of them involving, a payment or other disposition by a person other than a body corporate so associated."

79. Section 45(5A) provides that relief is lost if the transferor and

transferee cease to be "associated" within a period of two years after the execution of the instrument in question.

80. In order to obtain relief from stamp duty on the Memorandum of Sale, therefore, it must be shown to the satisfaction of the Collector

(i) that at the time the Development Land was transferred to Arrowtown, Shiu Wing and Arrowtown were "associated" with each other within the meaning of the Ordinance. This is not disputed; Arrowtown was a wholly owned indirect subsidiary of Shiu Wing at the relevant time;

(ii) that they did not cease to be so "associated" by reason of the sale of 980 of the 1,000 ordinary shares in Prepared to Calm Seas. The Collector accepts that they did not cease to be so associated if the "B" non-voting shares in Prepared are taken into account;

(iii) that no part of "the consideration for the transfer" of the Development Land to Arrowtown was to be provided or received directly or indirectly by a body not "associated" with Shiu Wing ("an outsider"); and

(iv) that Shiu Wing did not part with any of the consideration for the Development Land, that is to say the loan note, in the circumstances mentioned in s.45(5).

The issues

81. The Collector contends that s.45 relief is not available on three distinct grounds:

(i) that part of the consideration for the transfer of the Development Land was provided by outsiders - namely Calm Seas, New Town and Swire;

(ii) that Shiu Wing parted with part of the consideration for the transfer of the Development Land - namely, the loan note - in the circumstances described in s.45(5);

(iii) that under the principle established by *W T Ramsay Ltd v. IRC* [1982] AC 300 and later cases the "B" non-voting shares in Prepared should be disregarded in determining what was at the material times its issued share capital.

The first issue: was any part of the consideration for the Development Land provided by an outsider?

82. The Collector contends that the consideration received by Shiu Wing for the transfer of the Development Land comprised every contractual promise made to Shiu Wing which induced it to assign the Development Land to Arrowtown. Such promises included the undertaking by Calm Seas under para. 2.14 of Schedule 2 to the Share Sale Agreement and clause 14 of the Deferred Consideration Agreement to refund excess dividends to Arrowtown, the guarantees given to Shiu Wing by Swire and New Town by the same paragraph, and certain of the provisions of the Shareholders' Deed, in particular those mentioned in paragraph 73 above.

83. I am unable to accept this argument.

84. It is first necessary to understand what is meant by "consideration" in s.45. Arrowtown contends for the narrowest possible meaning and submits that it refers to the consideration which forms the basis for the charge to stamp duty, in the present case the amount of the initial consideration of HK\$12,714,856,874 only. Stamp duty is charged by reference to the amount or value of the consideration for the transfer, and consideration the amount or value of which is unascertainable at the time the document falls to be stamped is disregarded: see *Sergeant & Sims on Stamp Duties* para. 468.

85. Support for this submission may be found in the speech of Lord Wilberforce in **Shop and Store Developments Ltd v. CIR** [1967] AC 472 at p.504. Apart from the terminological argument for reading the two expressions in the same way, which he described as "not conclusive but surely strong", he considered it strange "to rest the test for exemption from stamp duty upon consideration in one sense and the charge upon consideration in another sense".

86. But the context in which Lord Wilberforce made these observations was very different from the present. He was concerned to emphasise that the consideration must be consideration for the transfer and not consideration for the arrangement as a whole of which the transfer formed part. The question with which we are concerned is whether consideration for the transfer includes any part of the consideration the value of which, being unascertainable, is left out of account for the purpose of calculating the amount of duty payable. As the Collector observed, consideration the amount or value of which is unascertainable is still consideration; moreover, there is no necessary

correlation between the amount or value of the consideration which forms the basis of the charge (which may be very large) and the amount or value of the consideration which is provided by outsiders and so disqualifies the instrument from relief (which may be very small).

87. Given the statutory purpose which s.45 is intended to achieve, I incline to the view that, contrary to Arrowtown's submission, consideration in s.45 does include consideration of an unascertainable amount or value. But it is not necessary to form a concluded view on this question because in my opinion the Collector's argument fails for other reasons; and I prefer to leave the point open for decision in a case where it is necessary to decide it. In what follows I shall assume that the consideration for the assignment of the Development Land by Shiu Wing to Arrowtown included both the initial and the Deferred Consideration.

88. In order to support a contract at common law, there must be consideration moving from the promisee. Such consideration may consist of an act or, in the case of an executory contract, a promise. But the word consideration in s.45 cannot mean consideration in quite this sense. It includes consideration which does not move from the promisee; which can be provided directly or indirectly; and with which the promisor can part.

89. In my opinion s.45 is not concerned with the promise which forms the contractual consideration, but with the subject-matter of the promise. It does not consist of Arrowtown's promise to pay the initial and Deferred Consideration, but with the initial and Deferred Consideration themselves. This is in conformity with the approach adopted by the majority in **Shop and Store Developments Ltd** who asked themselves "what did the clothing company get for the transfer" and answered "the shares in the property company".

90. It is also in line with the earlier case of **Curzon Offices Ltd v. IRC** [1944] 1 All ER 163. In that case a company transferred a property to its wholly owned subsidiary in return for a cash consideration which the subsidiary borrowed on commercial terms from a bank. Borrowed money belongs to the borrower, not the lender; and it was not suggested that the borrowing meant that the consideration was indirectly provided by the bank. But the loan was secured by a mortgage on the property sold and a guarantee by an outsider. The Court of Appeal held that relief was excluded because part of the consideration was provided by an outsider. It is clear, however, that the consideration in question was not the guarantee but

the money, which was indirectly provided by the outsider without whose guarantee the money would not have been made available to the transferee.

91. In **Shop and Store Developments Ltd**, as in the present case, the transfer was part of a larger arrangement planned as a whole from the outset. The House of Lords held by a majority that the consideration referred to in the United Kingdom statute (on which s.45 of the Ordinance is closely modelled) was the consideration for the transfer alone and not the consideration receivable by the transferor under the arrangement as a whole. Not every term in such an arrangement is consideration for the transfer.

92. What Shiu Wing got for the Development Land was the initial consideration and the right to receive the Deferred Consideration and, in my opinion, nothing else. The protective provisions on which the Collector relies formed no part of the consideration for the Development Land. It is true that they protected Shiu Wing's land interest, that is to say its right to payment of the Deferred Consideration for the Development Land, but they were given in consideration for the shares in Prepared, not for the assignment of the Development Land to Arrowtown, and were consequential on the loss of control of Arrowtown which the sale of the shares entailed. The Collector relies on the fact that the clawback provisions were included in the Deferred Consideration Agreement as well as in the Schedule to the Share Sale Agreement and the Shareholders' Deed; but the question is one of substance not form and does not depend on the particular document in which the provisions were contained.

93. The clawback provision in para. 2.14 was merely a condition on which interim distributions of profits from the development could be made, whether by way of payment towards Shiu Wing's entitlement to Deferred Consideration or by way of dividends to Prepared. If it was consideration for anything, it was for the right to pay interim dividends notwithstanding the possibility that it would result in an overpayment of Prepared and an underpayment of Shiu Wing. It was an undertaking to put the position right. It was not an undertaking to put Arrowtown in funds to enable it to pay the Deferred Consideration, which would have been indirect provision of the consideration for the Development Land. It was limited to the amount by which Prepared was found on a final accounting to have received excessive interim distributions, and was neither limited nor extended to the full amount if any which might be required to enable Arrowtown to pay the Deferred Consideration.

94. In my opinion the whole of the consideration for the assignment of

the Development Land was provided by Arrowtown and no part of the consideration was provided directly or indirectly by an outsider.

The second issue: did Shiu Wing part with any part of the consideration for the Development Land (i.e. the loan note) in the circumstances described in Section 45(5)?

95. Section 45(5) reproduces an amendment to the United Kingdom legislation which was made by the Finance Act 1967 to reverse the decision in **Shop and Store Developments Ltd.** In that case the arrangement had contemplated that the transferor would part with the consideration for the transfer, which consisted of renounceable letters of allotment, by renouncing them in favour of an issuing house and ultimately by way of sale to the public. The House of Lords held that the money received by the transferor from the public was not consideration for the transfer but for the letters of allotment. There was, as Lord Morris of Borth-y-Gest observed at p.495, all the difference between what the transferor got and what it did with what it got.

96. Arrowtown contends that there is no room for the application of s.45(5) in the present case since Shiu Wing and its subsidiaries did not part with the loan note to an outsider. The Collector responds that this is not a condition for the application of s.45(5), which speaks simply of parting with any of the consideration, not of parting with any of it to an outsider.

97. The Court of Appeal ruled unanimously in favour of Arrowtown on this point. Fastening on the opening words of subsection (5) "without prejudice to the generality of paragraph (a) of subsection (4)" they held that subsection (5) was not an enlarging provision to subsection (4) but must be read subject to it. I do not think that this is right. Subsection (4) does not grant relief; it denies it. The opening words of subsection (5) prevent it from prejudicing, that is to say cutting down, the denial of relief by subsection (4). It is in my opinion an additional denial of relief which, insofar as it may overlap with subsection (4), is not to be taken as cutting down the scope of the latter.

98. That this is the true relationship of the two subsections is, I think, further demonstrated by the fact that subsection (5) provides that, in prescribed circumstances, the arrangement "shall be treated as within" subsection (4). No further conditions are prescribed. If the transferor parts with any part of the consideration in the circumstances

prescribed, the arrangement is to be treated as within subsection (4), that is to say denied relief as an arrangement under which part of the consideration has been provided or received directly or indirectly by an outsider.

99. The objections that the subsection was enacted in order to reverse the decision in **Shop and Store Developments Ltd**, where the consideration was disposed of to outsiders, and that a disposal in favour of an associated company is not within the mischief at which the subsection is aimed, miss the point. The width of subsection (5) is limited, not by the character of the transferee who need not be an outsider, but by the concluding words of the subsection. These suggest that the vice of the transaction in **Shop and Store Developments Ltd**, as Parliament saw it, was not that the consideration was disposed of to outsiders, but that it was disposed of to them by way of sale, that is to say "by or in consequence of the carrying out of a transaction or transactions involving, or any of them involving, a payment or other disposition by" an outsider.

100. The Collector maintains that this condition is satisfied in the present case, but in agreement with the Court of Appeal I consider this to be untenable. The assignments of the loan notes were not "by or in consequence" of the payment of the consideration for the sale of the shares; it was the other way round. The payment of the consideration for the sale of the shares was a consequence of the assignments of the loan note; without them the shares in Prepared would have been worthless.

101. I would rule against the Collector on this issue also.

The third issue: should the "B" non-voting shares in Prepared be disregarded in considering whether Shiu Wing and Prepared were "associated" for the purpose of Section 45(2)?

102. Section 45(2) of the Ordinance defines bodies which are "associated" as bodies where one is beneficial owner of "not less than 90% of the issued share capital of the other". The reference to issued share capital is a reference to the nominal value of the issued share capital which is constant and not its market value which may fluctuate from day to day: see **Canada Safeway Ltd v. IRC** [1973] 1 Ch 374. The Collector accepts that, if the "B" non-voting shares in Prepared are taken into account, then Shiu Wing and Arrowtown continued to be "associated" after the completion of the Share Sale Agreement and the requirements of s.45(2) were satisfied. This is hardly surprising,

given that the "B" non-voting shares were created and issued for the sole purpose of complying with those requirements.

103. The Collector contends that, by the application of the approach to artificial tax avoidance schemes adopted by the House of Lords in **Ramsay**, the "B" non-voting shares in Prepared should be disregarded for the purpose of determining whether Shiu Wing and Arrowtown were "associated". This makes it necessary to examine the nature and scope of the **Ramsay** approach in some detail.

The Ramsay approach

104. In **Shiu Wing Ltd v. Commissioner for Estate Duty** (2000) 3 HKCFAR 215 this Court held that the **Ramsay** approach forms part of the law of Hong Kong. This does not mean that we must slavishly follow every twist and turn of an approach which, even after 20 years, is still in course of development in the United Kingdom. But it does behove us to understand its nature and the basis on which it rests, possibly with a greater recourse to comparative law and more explicit recognition that it derives from principles developed in the United States than the English cases have accorded it.

105. In **Shiu Wing Ltd v. Commissioner for Estate Duty** Sir Anthony Mason NPJ (at p.240) explained that the approach adopted by the House of Lords in **Ramsay**, which he observed accords with the basic legal principle adopted in the United States, is both a rule of statutory construction and an approach to the analysis of the facts. These two aspects of the principle have been present from the start. The doctrine cannot but involve an approach to statutory construction. It is a fundamental principle of the constitution of Hong Kong, as of the United Kingdom and the United States, that the subject is to be taxed by the legislature and not by the courts. In all three jurisdictions, therefore, every tax case, that is to say every question of tax or no tax, is ultimately a question of statutory construction. The question is always whether what the taxpayer did was within the intendment of the particular statutory provision which is invoked. Before construing the statute and applying it to the facts, however, it is first necessary to analyse what the taxpayer did.

106. **Ramsay** and its sister case **Eilbeck v. Rawling**, which were heard at the same time, both concerned circular self-cancelling paper transactions which were designed to return the taxpayer to the position from which he started. If the series of transactions were regarded as a whole, the taxpayer made neither gain nor loss beyond the fees he paid for the scheme. If each transaction in the series was considered

separately, however, they were said (incorrectly as it happened, for both schemes failed on technical grounds) to produce an allowable loss and an exempt gain. The loss was not independent of the gain; it was entirely dependent on, and merely a reflection of, the gain. It was quite impossible to have the one without the other.

107. The Crown conceded, as it was bound to do, that the subject is to be taxed by Parliament and not by the courts; that he is to be taxed on the basis of what he has done and not on the basis of what he might have done to achieve the same result; that he is to be taxed in accordance with the legal consequences of his acts and not in accordance with some supposed "substance of the transaction"; and that neither scheme was vitiated by the fact that it was undertaken by the taxpayer in order to avoid tax. The case law of the United States shows that all four concessions would have been equally demanded by its jurisprudence.

108. The Crown advanced two propositions. It submitted (i) that the court is not bound to treat each of the individual steps in a composite and preconceived arrangement in isolation and having its own fiscal consequences; and (ii) that it was not possible to create a deduction from tax by entering into a transaction which had no purpose or effect beyond the generation of the deduction itself. The first was an invitation to the House to adopt a more realistic analysis of the facts than the previous authorities indicated was open to the court; the second invited it to adopt the "no business purpose test" to reflect a purposive approach to the construction of the relevant statutory provisions.

109. Neither proposition was original. Both were inspired by the work of Judge Learned Hand in the United States and in particular his seminal judgment in **Helvering v. Gregory** (1934) 69 F.2d 809. Before turning to the decisions in **Ramsay** and the cases which followed it, it is convenient to examine the US decisions to see the extent to which they are echoed in the development of the jurisprudence of the United Kingdom and should influence the future development of our own.

The American cases

110. In **Helvering v. Gregory** the question was whether a transfer of shares by way of share exchange was within a statutory exemption from tax as a "reorganisation". The word "reorganisation" was defined in the statute and the transaction relied upon fell fairly and squarely within the definition. But Judge Learned Hand held that this was not

decisive:

"..... it does not follow that Congress meant to cover such a transaction, *not even though the facts answer the dictionary definitions of each term used in the statutory definition.*" (emphasis added).

He explained that this was because the statute was based on an underlying presupposition that the reorganisation should be

"undertaken for reasons germane to the conduct of the venture in hand, not as an ephemeral incident, egregious to its prosecution. To dodge the shareholders' taxes is not one of the transactions contemplated as corporate 'reorganisations'."

111. Judge Learned Hand did not disregard any of the transactions which had taken place:

"We cannot treat as inoperative the transfer of the Monitor shares by the United Mortgage Corporation, the issue by the Averill Corporation of its own shares to the taxpayer, and her acquisition of the Monitor shares by winding up that company. The Averill Corporation had a juristic personality, whatever the purpose of its organization; the transfer passed title to the Monitor shares and the taxpayer became a shareholder in the transferee. All these steps were real, and their only defect was *that they were not what the statute means by a 'reorganization'*, because the transactions were no part of the conduct of the business of either or both companies" (emphasis added).

112. This was the business purpose test. The transactions were not treated as if they had not occurred ("as inoperative") but as falling outside the exemption even though they fell within the statutory definition of "reorganisation". They fell outside it, not because they were undertaken in order to avoid tax, but because they had no other purpose. This was a manifestation of a purposive approach to the statutory construction of a tax exemption.

113. In **Gilbert v. CIR** (1957) 248 F.2d 399 at p.411 Judge Learned Hand explained the rationale of the business purpose test in a celebrated passage cited by Sir Anthony Mason NPJ in **Shiu Wing Ltd v. Commissioner for Estate Duty** at p.240 (and which includes a passage cited by Lord Wilberforce in **Ramsay** at p.326):

"It is a corollary of the universally accepted cannon of interpretation that the literal meaning of the words of a statute is seldom, if ever, the conclusive measure of its scope. Except in rare instances statutes are written in general terms and do not undertake to specify all the occasions that they are meant to cover; and their 'interpretation' demands the projection of their expressed purpose,

upon occasions, not present in the minds of those who enacted them. *The Income Tax Act imposes liabilities upon taxpayers based upon their financial transactions, and it is of course true that the payment of the tax is itself a financial transaction. If, however, the taxpayer enters into a transaction that does not appreciably affect his beneficial interest except to reduce his tax, the law will disregard it; for we cannot suppose that it was part of the purpose of the Act to provide an escape from the liabilities that it sought to impose.*" (emphasis added).

The United Kingdom authorities:

(1) Ramsay

114. In his speech in **Ramsay**, Lord Wilberforce accepted the Crown's submissions on the proper approach to the facts. In much cited passages at pp.323-326 he said:

"If it can be seen that a document or transaction was intended to have effect as part of a nexus or series of transactions, or as an ingredient of a wider transaction intended as a whole, there is nothing in the doctrine [of *IRC v. Duke of Westminster*] to prevent it being so regarded: to do so is not to prefer form to substance, or substance to form. It is the task of the court to ascertain the legal nature of any transaction to which it is sought to attach a tax or a tax consequence and if that emerges from a series or combination of transactions, intended to operate as such, it is that series or combination which may be regarded

[The courts] are not, under the *Westminster* doctrine or any other authority, bound to consider individually each separate step in a composite transaction intended to be carried through as a whole. This is particularly the case where (as in *Rawling*) it is proved that there was an accepted obligation once a scheme is set in motion, to carry it through its successive steps. It may be so where (as in *Ramsay* or in *Black Nominees Ltd. v. Nicol* (1975) 50 T.C. 229) there is an expectation that it will be so carried through, and no likelihood in practice that it will not

To force the courts to adopt, in relation to closely integrated situations, a step by step, dissecting, approach which the parties themselves may have negated, would be a denial rather than an affirmation of the true judicial process

To say that a loss (or gain) which appears to arise at one stage in an indivisible process, and which is intended to be and is cancelled out by a later stage, so that at the end of what was bought as, and planned as, a single continuous operation, there is not such a loss (or gain) as the legislation is dealing with, is in my opinion well and indeed essentially within the judicial function."

115. Lord Wilberforce did not expressly deal with the Crown's second submission; but he implicitly accepted it. He considered that the loss (or gain) in the paper transaction were "not such a loss (or gain) as the legislation is dealing with". He said that the capital gains tax operated "in the real world and not in the world of make-belief", and he cited what he described as "key passages" from **Knetsch v. United States** (1960) 364 US 361, 366 and **Gilbert**

"as examples, expressed in vigorous and apt language, of a process of thought which seems to me not inappropriate for the courts in this country to follow."

These were illustrations of the business purpose test.

116. Whatever else the word "loss" in the Capital Gains Tax legislation might mean, therefore, it did not include a "loss" which the taxpayer sustained only in the course of a preconceived series of transactions deliberately designed to produce neither loss nor gain. But why not? It was not, in my opinion, because the word "loss" is an ordinary English word understood by businessmen and accountants rather than a technical legal term: there is no hint in Lord Wilberforce's speech of any such distinction. Nor was it because of some perceived distinction between "the real world" and the "world of make-belief". These are forensic expressions which yield no criterion for distinguishing between them. The key lies in Lord Wilberforce's approval of the United States decisions and his indication that they encapsulated a process of thought which it would not be inappropriate for the courts of the United Kingdom to adopt. It was because it is the likely (though not inevitable) result of a purposive construction of fiscal legislation that it should normally be confined to transactions which have some purpose beyond the mere generation of tax relief. The no business purpose test provides a practical criterion for distinguishing between transactions which operate "in the real world" and transactions which operate in "the world of make-belief" and an appropriate criterion for distinguishing between losses of a kind which were within the contemplation of the legislature when granting relief from tax and losses which were not. It also provides a defensible rationale for leaving intermediate steps out of account, not because they did not take place, but because they fell outside the legislative intent.

(2) Burmah Oil

117. Ramsay was followed and applied by the House of Lords in **IRC v. Burmah Oil Co. Ltd** [1982] STC 30. This also concerned a circular

and self-cancelling transaction which was entered into for the sole purpose of obtaining tax relief. In this case it was designed to convert a bad debt into an allowable loss. At pp.32-33 Lord Diplock described the case before the House as concerning

"a pre-ordained series of transactions (whether or not they include the achievement of a legitimate commercial end) into which there are inserted steps that have no commercial purpose apart from the avoidance of a liability to tax which in the absence of those particular steps would have been payable [T]he approach to tax avoidance schemes of this character sanctioned by *Ramsay* entitles your Lordships to ignore the intermediate circular book entries and to look at the end result"

118. This was a straightforward application of **Ramsay**. But the no business purpose test was now explicit. The case did not depend upon an analysis of the meaning of the word "loss" or the nature of the concept which that word involves, but upon the absence of any purpose to the relevant transactions apart from the generation of tax relief.

119. Lord Diplock adopted the word "pre-ordained" rather than the word "pre-conceived", and this was to cause some difficulty later. He also referred to the courts "ignoring" the intermediate steps, a concept which called for further elaboration.

(3) Furniss v. Dawson

120. Had the cases stopped there, it might have been thought that the test was satisfied only where the transaction was circular and self-cancelling so that any loss was matched by a corresponding gain. **Furniss v. Dawson** [1984] 1 AC 474 showed that this was not the case.

121. The case was essentially a replay of **Helvering v. Gregory**. The taxpayers negotiated a sale to a prospective purchaser of their shares in a family company for a price which would yield a substantial but taxable capital gain. In order to avoid the liability to tax they split the transaction into two. First they transferred their shares in the family company to an Isle of Man company called Greenjacket in exchange for the issue of the entire share capital in Greenjacket, and on the following day Greenjacket sold the shares in the family company for the agreed price to the purchaser. The first disposal was by way of share exchange and if it had stood alone would have come squarely within an exemption from tax. The second disposal was taxable in principle but caused no tax to be payable because the gain had arisen

on the first.

122. The question was: what was the relevant disposal? Were there two disposals, as the taxpayers claimed, the first being a disposal by way of share exchange within the express words of a statutory exemption? Or was there only one disposal for the purpose of the statutory exemption, being a disposal by way of sale, as the Crown claimed? The Crown did not invite the House to ignore or disregard the disposal to Greenjacket as if it never happened or to treat it as a sham. It did happen; it was genuine; and the Crown accepted that it transferred the full legal and beneficial ownership of the shares to Greenjacket by way of share exchange. The Crown's case was that the fiscal consequences of the share exchange were to be disregarded because it was not the relevant disposal but only part of it. The relevant disposal was the composite transaction, which consisted of two steps and constituted a disposal of shares by way of sale, with the result that it fell outside the exemption for disposals by way of share exchange. The House of Lords agreed.

123. The kernel of Lord Brightman's reasoning is to be found in the following passage at p.526:

"..... in my opinion the rationale of the new approach is this. In a pre-planned tax-saving scheme, no distinction is to be drawn for fiscal purposes, because none exists in reality, between (i) a series of steps which are followed through by virtue of an arrangement which falls short of a binding contract, and (ii) a like series of steps which are followed through because the participants are contractually bound to take each step seriatim. In a contractual case the fiscal consequences will naturally fall to be assessed in the light of the contractually agreed results. For example, equitable interests may pass when the contract for sale is signed. In many cases equity will regard that as done which is contracted to be done. *Ramsay* says that the fiscal result is to be no different if the several steps are pre-ordained rather than pre-contracted this fiscal result cannot be avoided because the pre-ordained series of steps are to be found in an informal arrangement instead of in a binding contract. The day is not saved for the taxpayer because the arrangement is unsigned or contains the words 'this is not a binding contract'."

124. This is sometimes taken to be an exhaustive formulation of the **Ramsay** principle, but it is merely one example of a variety of different processes of reasoning which may be involved in its application. In the next passage of his speech Lord Brightman summarised the circumstances in which the **Ramsay** approach was appropriate:

"The formulation by Lord Diplock in [*Burmah Oil*] expresses the

limitations of the *Ramsay* principle. First, there must be a pre-ordained series of transactions; or, if one likes, one single composite transaction. This composite transaction may or may not include the achievement of a legitimate commercial (i.e. business) end. The composite transaction does, in the instant case; it achieved a sale of the shares in the operating companies by [taxpayers] to [the ultimate purchaser]. It did not in *Ramsay*. Secondly, there must be steps inserted which have no commercial (business) *purpose* apart from the avoidance of a liability to tax - not 'no business *effect*'. If those two ingredients exist, the inserted steps are to be disregarded for fiscal purposes. The court must then look at the end result. Precisely how the end result will be taxed will depend on the terms of the taxing statute sought to be applied."

125. The Court of Appeal had rejected the Crown's claim, ruling that the disposal to Greenjacket could not be disregarded because it had "enduring legal consequences". Greenjacket remained in existence after completion of the sale and received the purchase money which the taxpayers could not extract from it without adverse tax consequences to themselves. The insertion of Greenjacket therefore had a commercial effect, but the House of Lords held that this did not matter. It was no part of the taxpayers' purpose, but rather the price they had to pay for the hoped for exemption from tax. Lord Brightman did not disregard it in the sense of treating as if it had never taken place. He disregarded it "for fiscal purposes", that is to say for the purpose of applying the statutory charge to tax on a disposal (which had certainly taken place) and the statutory exemption in respect of a disposal by way of share exchange (which had not). He did not disregard it because Greenjacket's acquisition of the shares was and was always intended to be ephemeral, nor because the routing of the shares through it was motivated by a desire to obtain the benefit of a tax exemption, but because it had no other purpose.

126. There is usually no difficulty in determining whether the transaction in question formed part of a larger transaction or series of transactions planned as a whole; or in determining whether the inserted steps (or in **Ramsay** the whole transaction) had any purpose other than avoidance of tax. These are questions of fact. The difficulty usually arises in determining how the words of the statute are to be applied to the end result. This is a question of law and depends on the legislative purpose of the relevant charging or exempting provision as the case may be.

127. In **Ramsay, Burmah and Furniss v. Dawson** the words "loss" and "disposal" were given their ordinary legal meaning but were taken to refer to losses or disposals occurring in the course of transactions

undertaken for a purpose other than the avoidance of tax. Taken as a whole the arrangements did not produce such a loss or disposal by way of share exchange.

(4) McGuckian

128. After further intervening cases to which it is not necessary to refer, the **Ramsay** approach was authoritatively summarised by the House of Lords in **IRC v. McGuckian** [1997] 1 WLR 991. The question was whether moneys received as consideration for the assignment of a right to dividends from a third party were received as capital or income. This depended on whether the sale could be disregarded for tax purposes, not in the sense of being treated as if it had not taken place (which would not have suited the Crown's purpose since it wished to bring the receipt within a charge to tax), but in the sense that it did not have the desired effect of converting income into capital.

129. Lord Browne-Wilkinson held that the case fell squarely within the **Ramsay** approach. No business purpose for the assignment of the dividend rights had been suggested; and given that it had its genesis in the mind of a tax consultant, the only possible inference was that it was entered into for the sole purpose of obtaining a tax advantage. He summarised the **Ramsay** approach at p.998 as follows:

"The approach pioneered in the **Ramsay** case and subsequently developed in later decisions is an approach to construction, viz. that in construing tax legislation, the statutory provisions are to be applied to the substance of the transaction, disregarding artificial steps in the composite transaction or series of transactions inserted only for the purpose of seeking to obtain a tax advantage. The question is not what was the effect of the insertion of the artificial steps but what was its purpose. Having identified the artificial steps inserted with that purpose and disregarded them, then what is left is to apply the statutory language of the taxing Act to the transaction carried through stripped of its artificial steps. It is irrelevant to consider whether or not the disregarded artificial steps would have been effective to achieve the tax saving purpose for which they were designed."

130. Lord Steyn, who described **Ramsay** as marking an "intellectual breakthrough", and Lord Cooke of Thorndon also insisted that the principle was one of statutory construction. Lord Steyn said at p.1000:

"The new development was not based on a linguistic analysis of the meaning of particular words in a statute. It was founded on a broad purposive interpretation, giving effect to the intention of Parliament. The principle enunciated in the **Ramsay** case was

therefore based on an orthodox form of statutory interpretation. And in asserting the power to examine the substance of a composite transaction the House of Lords was simply rejecting formalism in fiscal matters and choosing a more realistic legal analysis."

Lord Steyn followed this passage with a warning:

"Given the reasoning underlying the new approach it is wrong to regard the decisions of the House of Lords since the *Ramsay* case as necessarily marking the limit of the law on tax avoidance schemes."

131. In considering the facts of the case before the House in the light of **Ramsay**, Lord Steyn remarked that neither the individual steps nor the composite transaction which the taxpayer had undertaken were simulated or shams in the sense in which those terms are used in contract or trust law. On the contrary, tax avoidance was the spur to executing genuine documents and entering into genuine arrangements. But the appeal was concerned with a different question: namely the fiscal effectiveness of the scheme as a whole. He held that it was fiscally ineffective to convert taxable income into non-taxable capital, because while the declaration of the dividend itself was "an ordinary commercial decision", the other steps, including the critical assignment, were not taken "for any business or commercial reason".

132. Lord Cooke of Thorndon said at p.1005:

"The principle which your Lordships have been developing in *W. T. Ramsay Ltd. v. Inland Revenue Commissioners* [1982] A.C. 300, *Inland Revenue Commissioners v. Burmah Oil Co. Ltd.* (1981) 54 T.C. 200, and *Furniss v. Dawson* [1984] A.C. 474 is not uncommonly seen as special to the construction of taxing Acts. Perhaps more helpfully, however, it may be recognised as an application to taxing Acts of the general approach to statutory interpretation whereby, in determining the natural meaning of particular expressions in their context, weight is given to the purpose and spirit of the legislation."

He, too, gave a similar warning:

"..... it may be as well to add that, if the ultimate question is always the true bearing of a particular taxing provision on a particular set of facts, the limitations cannot be universals. Always one must go back to the discernible intent of the taxing Act."

(5) *MacNiven*

133. *MacNiven v. Westmoreland Investments Ltd* [2003] 1 AC 311 involved a circular movement of money said to have been undertaken

for the sole purpose of obtaining a tax advantage, but the House of Lords held that it was fiscally effective because it fell within the legislative intent of the relevant statutory provision purposively construed.

134. A tax-exempt pension fund had a wholly-owned company as a vehicle for its investments, using money lent to it by the fund. After a series of disastrous investments the company's liabilities greatly exceeded its assets, and it owed the fund some £70 million including £40 million of accrued interest which it was unable to pay. Under s.338 of the Income and Corporation Taxes Act 1988 payments of interest, other than interest on bank loans, may be set against profits and any unused excess carried forward under s.75 of the Act. If it paid the fund the arrears of interest, therefore, the company would have a potential value to a purchaser as a company with established tax losses. But it had first to find the money to enable it to pay the interest. It had no resources of its own, and it obviously could not borrow the money from a third party. So it arranged to borrow the money from the fund.

135. This meant that the money went round in a circle. The company borrowed the money from the fund and used it to pay the fund the arrears of interest, deducting tax from the payment and accounting to the revenue for the tax which it had deducted. This had the effect of replacing its liability to pay interest with a liability for an equivalent capital sum, and preserving the tax loss which would make it attractive to a purchaser. The fund successfully reclaimed the tax and sold the company as a tax loss company. The revenue, however, disallowed the subsequent claim by the company to set the interest payment against profits on the ground that it had not been "paid" within the meaning of s.338.

136. The Crown based its case on **Ramsay**. It contended that a payment which comprised a circular flow of cash between borrower and lender and was made for no commercial purpose other than gaining a tax advantage did not constitute "payment" within the meaning of s.338. This was an attractive argument which at first sight appeared to be a straightforward application of **Ramsay**. But the House of Lords unanimously rejected it. It is of the first importance to understand why.

137. The answer is most clearly to be found in the speeches of Lord Nicholls of Birkenhead and Lord Hutton. Lord Nicholls observed that in the ordinary case the source from which a debtor obtains the money he uses to pay his debt is immaterial for the purpose of s.338. It does

not matter whether the debtor uses his own money or borrows money for the purpose. The question was whether it made a difference that the debtor borrowed the money from his creditor. So long as the lending is genuine, however, borrowed money belongs to the debtor not the creditor. As between the parties themselves, therefore, a debt may be discharged and replaced with another even when the only persons involved are the debtor and the creditor. So the question was whether the payment was fiscally effective if it had no purpose except to obtain a tax advantage.

138. Ramsay did not, as the Crown contended, dictate a negative answer. There was nothing in the language or context of s.338 to indicate that the purpose for which a payment of interest was made should be material to the question whether it should be allowed as a charge against profits. There was no reason why a genuine discharge of a genuine debt should cease to qualify as a payment for the purpose of s.338 merely because it was made solely to secure a tax advantage. (Similar reasoning might have led to a different result in **Ensign Tankers Ltd v. Stokes** [1992] 1 AC 655).

139. Lord Hutton based his conclusion on the fact that the company's liability to pay interest on its borrowings from the fund pre-dated the scheme and did not arise under the scheme itself. By discharging its pre-existing liability to pay interest the company incurred the economic burden which Parliament intended should give rise to the allowance provided by s.338, and the company was entitled to take steps to obtain the tax advantage which Parliament intended it to have in those circumstances. The company had not created an artificial loss in order to obtain a tax advantage; it had incurred a genuine loss and taken steps to enable it to claim relief in respect of it.

140. Two observations may be made at this point. First, as Lord Nicholls pointed out, the tax advantage which the payment was designed to achieve was not the fund's ability to reclaim the tax. It was this feature which made the scheme unattractive to the revenue, but it was the consequence of the fund's tax exempt status and was not challenged by the revenue. The scheme's object was to preserve the company's claim to charge interest payments against its profits, and it was this claim which the revenue challenged. It was a claim which pre-dated the inception of the scheme but which the company would have lost if it could not obtain the money with which to pay the interest. Consideration of the purpose underlying s.338 showed that Parliament cannot have intended to draw a distinction between a payment made with money borrowed from a third party and money

borrowed from the creditor; or (in this particular context) to exclude relief because the payment was made with a view to obtaining it.

141. Secondly, as Lord Hutton's speech indicates, it is unlikely that the same conclusion would have followed if the scheme had included the creation of the company's liability to pay interest in the first place.

142. I am not myself convinced that the object of the scheme was solely to obtain a tax advantage. Its object was to crystallise an existing liability in order to enable the company to be sold as a tax loss company instead of merely put into liquidation; and this strikes me as a commercial purpose. It is true that the company could only be sold as a tax loss company if it had a tax loss; but if it did the sale would be in accordance with the philosophy which underlies the taxation of company profits. I would not myself regard the crystallisation of an existing liability in these circumstances as having no business purpose.

143. But the basis of the decision is that, even if the payment in question was undertaken solely for the purpose of obtaining tax relief, the granting of such relief in such circumstances was nevertheless within the intendment of the statute. The importance of the case is that the no business purpose test is not a free-standing principle which yields an automatic solution in every case. It is rather a manifestation of a purposive construction of the relevant statutory provision, and even transactions undertaken for the sole purpose of obtaining relief from tax may be within the intendment of the statute. There is no alternative to a careful consideration of the reasons which motivated the legislature to impose the tax or to grant the relief in question.

144. However it is Lord Hoffmann's speech (with which the other members of the House agreed) which has caused difficulty in the United Kingdom. He agreed with Lord Nicholls that on the true construction of s.338 the purpose for which a payment of interest is made is not material to the question whether it should be allowed as a charge against tax. But he appears to have done so because he treated the word "payment" in the section as embracing a legal concept and not a commercial one. As a result he has been taken to have introduced a new limitation on the scope of the **Ramsay** approach by drawing a distinction between "commercial" and "juristic" concepts. **Ramsay**, it is said, is applicable where the statute invokes a commercial concept like "loss" or "disposal" but not where it invokes a "juristic" concept like "indemnity" or "payment" (or, it was contended in the present case, "issued share capital").

145. Like Carnwath LJ in **Barclays Mercantile Business Finance**

Ltd v. Mawson [2003] STC 66 I have some difficulty in fitting the authorities into Lord Hoffmann's analysis. **Ramsay** itself cannot depend on what a businessman would regard as a "loss", still less on what an accountant would. Fiscally the gain and the loss were incommensurable, for the gain was exempt and the loss was taxable. The accountant would net them off against each other off-balance sheet; but it does not follow that he would regard them as if they did not have separate existences of their own. Whether they did so for the purpose of the fiscal legislation would be a matter for the courts to decide; and the decision in **Ramsay** that they did not depend on the fact that the word "loss" involved a commercial concept but on the absence of any commercial purpose in the transaction in which the alleged loss was incurred.

146. Nor can **Furniss v. Dawson** be easily accommodated. Lord Hoffmann explained that the question there was the identity of the donee. But with respect this was not the case, except at the most superficial level; nor could it have been. The statutory exemption did not depend on the identity of the donee but on the nature of the consideration given for the disposal. The nature of the consideration depended on the identity of the disposal, and this was the crucial issue. The Crown argued that the disposal by way of share exchange was not the relevant disposal but only part of it. The intermediate disposal to Greenjacket could be disregarded for the purpose of applying the terms of the share exchange exemption, because in granting the exemption Parliament did not intend to include a share exchange undertaken for the sole purpose of obtaining it. Of course, the statutory words might compel such a construction in a given case; but not, I respectfully think, because of some supposed difference between commercial and legal concepts.

147. The question in **McGuckian** was whether a payment was received as capital or as income. These are economic concepts rather than legal or commercial ones; but the question was not whether an economist or a businessman would regard the receipt as capital or income, but how it should be regarded for the purpose of applying the taxing Acts. This is a question of law, and the question is notoriously difficult to answer.

148. The supposed dichotomy between legal and commercial concepts has caused great difficulty. In **Barclays Mercantile** neither Peter Gibson LJ nor Carnwath LJ could understand it, and counsel were unable to explain it. Nor is its source discernible. It makes no previous appearance in the many authorities in which **Ramsay** has been applied

or distinguished. It does not appear in the speeches of Lord Nicholls or Lord Hutton in **MacNiven**. It leads Lord Hoffmann to the conclusion that the word "payment" embraces a legal rather than a commercial concept, a conclusion which I respectfully regard as questionable. And it would seem to lead to the conclusion that the result would have been the same even if the liability to pay interest had been created as part of the scheme, a conclusion which I find difficult to accept.

149. If Lord Hoffmann was merely saying that the statutory language must be construed in the light of its purpose, and that a provision granting relief from tax is generally (though not universally) to be taken to refer to transactions undertaken for a commercial purpose and not solely for the purpose of complying with the statutory requirements for tax relief, it is an accurate description of the **Ramsay** principle. Nor can objection be taken to the idea that the words of a particular statute may be too closely articulated to admit of an application of the principle: Judge Learned Hand had said as much in **Helvering v. Gregory**. I am not at all sure that Lord Hoffmann intended more than this.

150. But his speech has had most unfortunate consequences. It has led to arid debates in an endeavour to fit the statutory language into one or other conceptual category. But the distinction is not clear cut and yields an uncertain answer, for the concepts overlap; and it cannot be drawn in the abstract, for it depends on context and statutory purpose. If the disposal to Greenjacket in **Furniss v. Dawson** was not within the concept which Parliament meant by "share exchange", then had the disposal been for money (and the basis for exemption different) it would not have been within a concept like "sale" either. Yet when the courts have had to consider in other contexts whether a transaction constitutes a sale they have treated the word as a term of art and looked to Roman law for an answer.

151. It may be that the dichotomy is the result of a misunderstanding of what Lord Hoffmann intended; but if not then I respectfully think that it should not form part of the jurisprudence in this jurisdiction. In the present case the argument for the taxpayer was founded on the submission that issued share capital is a legal concept and not a commercial one. For the reasons I have given, I reject this approach. The question is not whether "share capital" is a legal or commercial concept, but whether share capital with the characteristics of the "B" non-voting shares and issued for the sole purpose of complying with the statutory formula were within the contemplation of the legislature when enacting s.45 of the Ordinance.

The application of the Ramsay principle in the present case

152. In my opinion the present case falls squarely within the **Ramsay** approach. The creation and issue of the "B" non-voting shares formed part of a larger transaction under which the Development Land was to be sold and transferred to a joint venture company in which Shiu Wing would retain a small 2% equity stake. The shares were created and issued in order to meet the qualifications for exemption from stamp duty in s.45 of the Ordinance. This was explicitly stated in the Heads of Agreement. They had no other purpose. This was not seriously disputed. Leaving aside for the moment their nominal value and the right to appoint a director of Prepared and Arrowtown which was attached to them, they had no commercial content at all. They carried no rights to dividends or capital on a winding up. If shares are considered as a bundle of rights, they had barely even a shadowy existence.

153. Prepared had the right to buy the shares at their nominal value, but Shiu Wing could not compel it to do so. The right to appoint a director was originally conferred on Shiu Wing, but later as the documentation developed the opportunity was taken to attach the right to the "B" shares instead, no doubt in the belief that this would provide some much needed content to the shares. But **Ramsay** allows steps to be disregarded if they have no business purpose, not no business *effect*. It is fanciful to suppose that the shares were issued in order to give Shiu Wing an additional albeit miniscule investment in Prepared or to allow it to appoint a representative director to look after its interests. The former was merely a by-product of the scheme rather than an object of it; the latter would have been an essential protection for Shiu Wing on which it would have insisted even if there had been no stamp duty scheme. It was necessary precisely because Prepared was, to all intents and purposes, a member of the Calm Seas group and not the Shiu Wing group. As the Heads of Agreement recognised from the outset, completion of the share sale would leave Shiu Wing as "a minority shareholder of Prepared". This was not affected by the issue of the "B" non-voting shares; Shiu Wing still needed the protective provisions which it had demanded.

154. Whether the "B" non-voting shares can be left out of account when applying s.45 of the Ordinance depends on the purpose for which the section was enacted. Lord Denning explained the purpose of the corresponding United Kingdom provision in **Escoigne Properties Ltd v. IRC** [1958] AC 549 at p.567:

"[Its purpose] was to give relief from stamp duty on an instrument by which one company transfers property to its associated company: provided that the association is so close that the transfer is little more than a change in the nominal ownership, with the underlying control remaining the same: and a 90 per cent. shareholding is made the test of closeness."

155. There is no magic in the figure of 90%. The legislature could have chosen a different figure for its purpose. It is not its purpose to grant relief in respect of a transfer to a company which is 90% controlled by the transferor. Its purpose is more general: to grant relief to transfers between associated bodies. 90% is merely the test of association. If the test is not satisfied, there can be no relief. But it does not follow that, if the test is satisfied, there must be relief. That depends on whether the test is satisfied in circumstances contemplated by the section, that is to say where it can be said that the bodies are genuinely associated so that the transfer does not involve a significant change of ownership.

156. The legislature could have confined relief to the case where the transferor was the beneficial owner of 100% of the issued share capital of the transferee. Had it done so, the present scheme would not have been possible. But the legislature was content with 90%. It must have recognised the commercial need for flexibility in order to permit the holding of small minority stakes without jeopardising the relief. But the legislature cannot have intended the 10% allowance to outsiders to be exploited so as to permit relief to be available in a case where the property was to all intents and purposes transferred to a 98% owner with the transferor retaining only 2% even if the literal requirements for exemption were complied with.

157. Section 45 is not an end in itself. The words "issued share capital" in the section, properly construed, mean share capital issued for a commercial purpose and not merely to enable the taxpayer to claim that the requirements of the section have been complied with. It follows that the "B" non-voting shares issued to Shiu Wing are not "share capital" within the meaning of the section, and should be disregarded when calculating the proportions of the nominal share capital owned by Shiu Wing and Calm Seas respectively.

Conclusion

158. I would allow the appeal with costs here and below and uphold the Collector's claim to stamp duty.

Chief Justice Li :

159. The Court unanimously allows the appeal with costs here and below and upholds the Collector's claim to stamp duty.

(Andrew Li)

(Kemal Bokhary)

(Patrick Chan)

Chief Justice

Permanent Judge

Permanent Judge

(RAV Ribeiro)

(Lord Millett)

Permanent Judge

Non-Permanent Judge

Representation:

Lord Goodhart QC and Mr Eugene Fung (instructed by the Department of Justice) for the appellant

Mr David Goldberg QC and Mr Chua Guan Hock SC (instructed by Messrs Johnson, Stokes & Master) for the respondent